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Response to Consultation Paper, 'Climate-related financial disclosure' (December 2022)

Introduction

1. The New South Wales Bar Association (**the Association**) thanks the Treasury for the opportunity to respond to its December 2022 Consultation Paper, 'Climate-related financial disclosure' (**Consultation Paper**).
2. The Association notes that 19 key consultation questions were identified in the Consultation Paper. Of those questions, the Association wishes to provide responses to Questions 1, 4-11, 14-15, and 17-19. The Association's responses are set out below.

Association's responses

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

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

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

3. The Association believes that the primary challenge of meeting "existing climate reporting expectations" are that the expectations are to a large degree undefined. In an effort to meet those expectations, companies are and will be making statements which expose those companies to, for example, "greenwashing" claims for contravention of misleading and deceptive conduct norms. Yet it is difficult for companies to predict the "expectations", and it is difficult to advise companies about their liability exposure for failing to meet those expectations. The Association therefore believes that Australia *should* align itself with emergent international practice and in particular global baseline standards for climate reporting.

4. Many Australian entities are acutely exposed to climate-related risks, with the ASX50 being the most exposed major stock exchange in the world to stranded asset risks.¹ It is being reported that, already, 46% of companies are experiencing resource scarcity or increased cost of resources due to climate change, and 45% are experiencing changed demand for their products.² Australian companies are therefore expected to confront and disclose the risks which climate change may present to their businesses. There is widespread recognition amongst Australian regulators that the duty of care, skill and diligence imposed (for example, by section 180(1) of the *Corporations Act 2001* (Cth)) requires directors to consider climate risk, and to develop strategies to respond to it. Further, Australian companies are increasingly expected to disclose these matters to the market because of profound investor interest in those matters. As at 2022, 49% of ASX200 companies had net zero emissions targets.³ However, there is a risk that such disclosures generate legal liability because they may be found to be misleading or deceptive.
5. These dynamics present an acute problem for Australian companies, and for lawyers who advise them. The problem is the absence of a clear framework for considering and disclosing climate risk. While Australian regulators have sought to provide guidance regarding the disclosure of climate-related risks and opportunities in operating and financial reviews, corporate governance statements, and financial statements,⁴ and have recommended the use of the Task Force on Climate-Related Financial Disclosures (TCFD) framework,⁵ these existing climate reporting expectations are not standardised, certain, or even (necessarily) very well-known. There is therefore significant uncertainty for entities wishing to provide informative climate reporting without a standard disclosure framework to do so. This is impeding the provision of consistent, comprehensive, and comparable decision-useful information about entities' climate-related risks and opportunities to investors and other stakeholders.
6. According to analysis by the Australian Council of Superannuation Investors, investors regularly express concerns about the difficulty of comparing the climate resilience of companies, even within the same sector, and the lack of detail and quantification as to how climate-related risks and opportunities may impact companies' future financial performance and prospects.⁶

¹ S & P Dow Jones Indices, *The Carbon Scorecard* (May 2017).

² Deloitte, *2023 CxO Sustainability Report: Accelerating the Green Transition* (January 2023) p 7.

³ PWC, *ESG Reporting in Australia* (2022) pp 5, 7.

⁴ See, for example, ASIC, *Regulatory Guide 247: Effective disclosure in an operating and financial review* (August 2019); ASIC, *Report 593: Climate risk disclosure by Australia's listed companies* (September 2018); ASX Corporate Governance Council, *Corporate Governance Principles and Recommendations* (Fourth Edition, February 2019); AASB, *Climate-related and other emerging risk disclosures: assessing financial statement materiality using AASB Practice Statement 2* (December 2018).

⁵ ASIC, *Regulatory Guide 247: Effective disclosure in an operating and financial review* (August 2019) pp 19-20, paras 247.64-247.66; APRA, *Prudential Practice Guide CPG 229 Climate Change Financial Risks* (November 2021), para 50.

⁶ Australian Council of Superannuation Investors, *Promises, pathways & performance: Climate change disclosure in the ASX200* (July 2022) p 28.

7. The Association understands that the United Kingdom,⁷ European Union (EU),⁸ United States (US),⁹ New Zealand,¹⁰ Switzerland,¹¹ Hong Kong,¹² and Japan¹³ have introduced or are contemplating the introduction of mandatory climate-disclosure requirements that broadly align with the recommendations of the TCFD. The International Sustainability Standards Board's (ISSB) recent Exposure Drafts of *IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information (Draft IFRS S1)* and *IFRS S2 Climate-related Disclosures (Draft IFRS S2)* (collectively, the **ISSB Draft Standards**) build on the framework provided by the TCFD to provide a more comprehensive global baseline of climate-related disclosures.
8. The ISSB Draft Standards would include the following specific requirements:
 - a. Entities would be required by Draft IFRS S2 to disclose significant climate-related risks and opportunities that could reasonably be expected to affect their business model, strategy and cash flows, access to finance and cost of capital over the short, medium or long term (paragraph [9]).
 - b. Further, entities would be required by Draft IFRS S2 to disclose the anticipated effects of significant climate-related risks and opportunities on entities' financial position, financial performance and cash flows over the short, medium and long term (paragraph [14]).
 - c. Entities would be required by Draft IFRS S2 to disclose targets set to mitigate or adapt to climate-related risks or maximise climate-related opportunities (paragraph [20](d)), and particular information about those targets (paragraph [23]), including their reliance on offsets (paragraph [13](b)(iii)).
 - d. Entities would be required by Draft IFRS S2 to disclose the anticipated effects of significant climate-related risks and opportunities on their value chains (paragraph [12](b)).
9. In at least these respects, the Association believes that the ISSB Draft Standards have a significant capacity to assist Australian entities and officers by identifying with clarity and particularity the things that Australian law may already require them to be doing:
 - a. As for paragraphs [10](a)-(b), these are things that entities may already be considering and disclosing in their financial reports¹⁴ and directors' reports,¹⁵ and in the discharge of their duties on the basis that the consideration of risks and opportunities is a core function of a company director, and is central to the duty of care. Although 49% of ASX200 companies had net zero

⁷ *Companies (Strategic Report) (Climate-related Financial Disclosure) Regulations 2022* (UK); *Limited Liability Partnerships (Climate-related Financial Disclosure) Regulations 2022* (UK).

⁸ *Directive (EU) 2022/2464 of the European Parliament and of the Council of 14 December 2022 amending Regulation (EU) No 537/2014, Directive 2004/109/EC, Directive 2006/43/EC and Directive 2013/34/EU, as regards corporate sustainability reporting* [2022] OJ L 322/15 (**EU Directive**).

⁹ US Securities and Exchange Commission, *Proposed rule on the Enhancement and Standardization of Climate-Related Disclosures for Investors* (4 November 2022) 87 FR 21334.

¹⁰ *Financial Sector (Climate-related Disclosures and Other Matters) Amendment Act 2021* (NZ).

¹¹ *Ordinance on Climate Disclosures* (Switzerland) SR 220.

¹² *Main Board Listing Rules* (Hong Kong) Appendix 27: Environmental, Social and Governance Reporting Guide.

¹³ JPX, *Corporate Governance Code* (11 June 2021) Principle 3.1.

¹⁴ *Corporations Act 2001* (Cth) s 296(1); AASB 101; AASB, *Climate-related and other emerging risk disclosures: assessing financial statement materiality using AASB Practice Statement 2* (December 2018).

¹⁵ *Corporations Act 2001* (Cth) s 299A; ASIC, *Regulatory Guide 247: Effective disclosure in an operating and financial review* (August 2019) RG 247.66; ASIC, *Report 593: Climate risk disclosure by Australia's listed companies* (September 2018).

emissions targets as at 2022, it is reported that only 55% of these companies disclose a reasonable level of detail on a plan to achieve these targets.¹⁶

- b. As for paragraph [10](c), arguably, entities may already be considering how they intend to achieve any climate-related targets to ensure they have “reasonable grounds” for any forward-looking statements (see further our response to Question 15 below), and that directors are fulfilling their duty of due care, skill and diligence to a company.
 - c. As for paragraph [10](d), if it be accepted that a company’s “value chain” is central to its financial health and stability, then it would seem to follow that company directors may already be considering this matter in the discharge of their duties to a company.
10. It has been reported that, as at 2022, only 103 of the ASX200 companies were fully or partially aligned with the TCFD framework.¹⁷ If this is correct, or even close to correct, it would seem to follow that the introduction of mandatory climate-related disclosure requirements that align with the above international frameworks would impose additional regulatory burdens and costs on Australian entities who are not already reporting against those standards. Australian entities and officers will no doubt also be concerned about heightened liability risks attendant on more rigorous climate-related disclosure requirements.
11. Whilst it is true that the adoption of the ISSB Draft Standards would increase the number and kinds of climate-related information that entities are required to disclose, the Association endorses this as a welcome development on the basis that it will provide clarity about what is required in the discharge of corporate disclosure obligations and directors’ duties of care, skill and diligence, and in ensuring compliance with misleading or deceptive conduct laws (see further our response to Questions 4, 6 and 15 below).
12. The Association also notes that, whilst comprehensive, the ISSB Draft Standards are generally directed only to that which is material for the entity in question, and thus to what entities and officers may already be considering. To this extent, the Association believes that the ISSB Draft Standards have a significant capacity to *assist* entities and officers by identifying with clarity and particularity the things that Australian law may already require them to be doing, where those things are otherwise perhaps currently not very well appreciated. Further, the ISSB Draft Standards will *assist* entities and officers to ensure they are carrying out the kinds of functions that will minimise liability risk to the greatest extent possible.
13. The Association’s view is that the potential costs of aligning with international climate reporting practice are significantly outweighed by the benefits, including but not limited to the following:
- a. Facilitating Australian entities and officers to have clarity and certainty regarding their climate-related disclosure obligations.
 - b. Facilitating Australian entities to understand, and to navigate, the risks and opportunities presented by the energy transition.

¹⁶ PWC, *ESG Reporting in Australia* (2022) pp 5, 7.

¹⁷ Australian Council of Superannuation Investors, *Promises, pathways & performance: Climate change disclosure in the ASX200* (July 2022) p 6.

- c. Providing investors and other stakeholders with consistent, comprehensive, and comparable information regarding Australian entities' climate-related impacts, risks, and opportunities that can inform financial decision-making.
- d. Increased transparency of Australian entities' management of, and resilience to, climate-related risks and opportunities. This will in turn minimise the risk of investors being exposed to unexpected losses and of markets being unfairly skewed in favour of entities failing to adequately disclose climate-related risks.
- e. Facilitating Australia's integration into international markets.
- f. Helping Australia fulfil its international and statutory climate-related commitments, including its legislated net zero emissions by 2050 target.¹⁸

14. To directly answer Question 1.2, the costs and benefits of Australia *not* aligning with international practice, and in particular global baseline standards for climate reporting, are the converse of those identified at paragraphs [3] – [13] above.

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

15. The Association supports alignment of climate reporting requirements in Australia with the global baseline envisaged by the International Sustainability Boards, subject to the qualifications articulated below in response to:

- a. Question 7 (consistency with Australian materiality standards);
- b. Question 10 (consistency of emissions accounting methods); and
- c. Question 11 (alignment of scenario analysis and climate-related targets with Australia's international and statutory climate-related commitments).

16. The ISSB Draft Standards are designed to be a global baseline that builds on the earlier work and learnings of the TCFD, and which will improve the consistency, transparency, and comparability of climate-related disclosures. The Association believes that derogation from this baseline would be detrimental to Australia's integration into international markets.

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

17. As detailed in our response to Questions 7, 11, and 15 below, the implementation of climate-related disclosure requirements should have regard to existing Australian laws on corporate disclosures and misleading or deceptive conduct, including those pertaining to forward-looking statements and materiality standards. Disclosure requirements should also be consistent with Australia's international and statutory climate-related commitments (see our response to Question 11 below).

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

¹⁸ *Climate Change Act 2022* (Cth) s 10(1)(b).

18. The Association has no further comments in relation to this question.

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

19. The Association believes that the key considerations are certainty, materiality and competence.

20. As for *certainty*, Australia's climate reporting framework should achieve the appropriate balance between covered entities' need for *certainty* regarding their disclosure obligations, and flexibility to accommodate the rapidly evolving regulatory and market landscape prompted by the energy transition. It is important that the reporting framework is, as much as possible, consistent with existing corporate disclosure and misleading or deceptive conduct laws (see our response to Questions 7 and 15 below), Australia's international and statutory climate-related commitments (see our response to Question 11 below), and international practice on climate-related disclosures.

21. As for *materiality*, we suggest that the design of the new regulatory framework recognise that the driving dynamic is to provide a framework for investors to understand (and companies fairly to disclose) climate risk and opportunity. Materiality is discussed further in our response to Questions 6 and 7 below.

22. As for *competence*, we also suggest that it be recognised that the subject-matter of the required disclosures will, to a significant extent, depend upon technical/professional judgments by the company, and also by independent consulting experts. A practical example is emissions data, which is likely to be of interest to investors and is widely reported (for example, by resources companies), but where there are indications of serious under-reporting at present: see further paragraph [42] below. Companies have a degree of protection in that they are permitted to rely upon experts, and because there may be a range of available views which reasonable experts may be permitted to hold. But investors depend heavily upon the competence of those carrying out technical assessments. It is appropriate that these dependencies be transparent and acknowledged – as occurs for example in the context of the Australasian Code for Reporting of Exploration Results, Mineral Resources and Ore Reserves (**JORC Code**), where a competent person is required to sign off on geological and engineering announcements made by a company. This then provides comfort to the investing public, for whom the areas of judgment and discretion, and any reliance upon independent experts, can be clearly identified.

23. The Association considers the balance is best achieved by the *first* regulatory framework proposal in the Consultation Paper. That is, by overarching climate-disclosure obligations being embedded into legislation and the detail of those obligations being provided through regulatory standards and guidance. Incorporating overarching obligations into legislation would help rectify the current fragmentation of climate reporting expectations in Australia, and improve their accessibility. The details of those obligations being contained in regulatory standards and guidance allows them to readily adapt to subsequent developments, such as the recommendations of the Taskforce on Nature-related Financial Disclosures, which are currently under development.

24. Of the frameworks currently available, the Association considers that the adoption of the ISSB Draft Standards would best provide covered entities with sufficient certainty regarding their minimum disclosure obligations, and create a common lexicon for climate-related disclosures, including in relation to emissions scopes (see our response to Question 10 below).

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

25. The Association believes that, where climate-related risks and opportunities are *material*, it is appropriate that they continue to be disclosed in operating and financial reviews, financial reports, and as part of continuous disclosure obligations, as would any other type of material information.

26. Under the *Corporations Act 2001* (Cth), listed disclosing entities are required to prepare and lodge a financial report and a directors' report each financial year (section 292), as well as comply with other periodic disclosure requirements and continuous disclosure obligations (section 674).

27. Financial reports must comply with Australian Accounting Standards promulgated by the Australian Accounting Standards Board (**AASB**) (section 296(1)). AASB 101 defines information as material, in relation to omissions or misstatements, if it "could reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statements", and lists examples of material information.

28. Directors' reports for a company, registered scheme, or listed disclosing entity must, subject to certain exceptions, contain information that members of the listed entity would reasonably require to make an informed assessment of the entity's operations, financial position, business strategies, and prospects for future financial years (section 299A).

29. Listed disclosing entities' continuous disclosure obligations require them to notify the ASX of information that is not generally available if a "reasonable person would expect the information, if it were generally available, to have a material effect on the price or value" of the entity's securities, and provisions of the ASX Listing Rules require disclosure of that information (section 674).¹⁹ ASX Listing Rule 3.1 requires listed entities immediately to disclose information to the ASX if they are or become aware of any information that a "reasonable person would expect to have a material effect on the price or value of the entity's securities", subject to the exceptions in Rule 3.1A, and lists examples of such information. A reasonable person would be taken to expect information to have a material effect on an entity's securities if the information "would, or would be likely to, influence persons who commonly invest in securities in deciding whether to acquire or dispose" of the entity's securities (section 677(1)).

¹⁹ Section 674A of the *Corporations Act 2001* (Cth) creates a civil penalty provision that requires listed disclosing entities to disclose information that is not generally available if the entity "knows, or is reckless or negligent with respect to whether, the information would, if it were generally available, have a material effect on the price or value" of the entity's securities.

30. Australian regulatory guidance has confirmed that climate-related risks and opportunities may be “material” for the purposes of these disclosure requirements.²⁰

31. To the extent Australia’s new climate reporting framework requires disclosures above and beyond these existing requirements, such as the disclosure of entities’ greenhouse gas emissions and transition plans, the Association considers that covered entities should be afforded flexibility in how they comply with these requirements. Covered entities necessarily have varying circumstances that will inform how they report mandated climate-related disclosures in a manner that minimises any additional regulatory burden and costs. Beyond baseline requirements such as disclosures occurring on an annual basis and being easily accessible for users, covered entities should be afforded flexibility to accommodate these varying circumstances.

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

32. The Association believes that materiality in the context of climate reporting should be consistent with existing Australian materiality standards, which are discussed in our answer to Question 6 above.

33. The definitions of materiality contained in our response to Question 6 above are broadly consistent with the definition in Draft IFRS S1, except that they omit any concept of “enterprise value”. As the Association understands it:

- a. “enterprise value” reflects expectations of the amount, timing and uncertainty of future cash flows over the short, medium and long term and the value of those cash flows in light of the entity’s risk profile, and its access to finance and cost of capital;
- b. The assessment of “enterprise value” would require inclusion of sustainability-related financial information, including the entity’s governance of, and strategy for, addressing sustainability-related risks and opportunities and about decisions made by the entity that could result in future inflows and outflows that have not yet met the criteria for recognition in the related financial statements. Sustainability-related financial information also depicts the reputation, performance and prospects of the entity as a consequence of actions it has undertaken, such as its relationships with, and impacts and dependencies on, people, the planet and the economy, or about the entity’s development of knowledge-based assets.

34. The Association considers it may be unhelpful to incorporate enterprise value into materiality judgments for climate reporting. This could create unnecessary inconsistencies with the well-understood definitions of materiality in the *Corporations Act 2001* (Cth), ASX Listing Rules, and AASB 101. The Association considers that the only potential *benefit* of using enterprise value would be alignment with the definition of materiality in Draft IFRS S1. However, similar concerns regarding potential inconsistencies prompted the ISSB to “tentatively decide” in its most recent meeting in December 2022 to remove enterprise value from the objective description of materiality in Draft IFRS

²⁰ See, for example, ASIC, *Regulatory Guide 247: Effective disclosure in an operating and financial review* (August 2019); ASIC, *Report 593: Climate risk disclosure by Australia’s listed companies* (September 2018); ASX Corporate Governance Council, *Corporate Governance Principles and Recommendations* (Fourth Edition, February 2019).

S1.²¹ It was also concerned that the concept of enterprise value unduly narrows the scope of disclosures and would exclude decision-useful information.²² The Association therefore perceives minimal, if any, benefit to using enterprise value to inform materiality judgments for climate reporting.

35. The Association supports the inclusion of “double materiality” for the purposes of climate reporting, as was adopted by the EU in December 2022.²³ Whereas existing Australian materiality standards are directed to the impact of climate *upon the company*, “double materiality” would also require covered entities to also disclose their material impacts *on the climate*. This is on the basis that the Association perceives that investors want to know information of this kind, i.e. it is decision-useful information, albeit that it may not be material to the company in a financial sense. Relatedly, the Association supports a requirement that covered entities’ greenhouse gas *emissions* should be disclosed regardless of materiality, as encouraged by the TCFD²⁴ and required by Draft IFRS S2 (see further our response to Questions 9 and 10 below).²⁵ In both respects, requiring covered entities to comply with international best practice also minimises the risk of future regulatory ‘lag’ and fragmentation, and resulting administrative costs and burdens.

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

36. The Association considers that existing auditing frameworks for financial reports provide adequate assurance of climate-related financial disclosures, and that these requirements should be extended to covered entities’ greenhouse gas emissions disclosures.

37. The financial reports of companies, registered schemes and disclosing entities (and other entities that meet certain thresholds) must be audited in accordance with Division 3 of Part 2M.3 of the *Corporations Act 2001* (Cth).²⁶ Audits must be conducted in accordance with accounting and auditing standards,²⁷ and auditors must provide a declaration that, to the best of their knowledge and belief, there have been no contraventions of the auditor independence requirements of the Act or any applicable code of professional conduct.²⁸ Registered company auditors are regulated under Chapter 9 of the Act, which requires that auditors meet extensive conditions relating to education, experience, competency and integrity in order to be registered with the Australian Securities and Investment Commission (**ASIC**).

²¹ IFRS Sustainability, ‘Staff paper: General Sustainability-related Disclosures’ (December 2022) paragraph 8; IFRS Sustainability, ‘Staff paper: General Sustainability-related Disclosures’ (October 2022) paragraph 54.

²² IFRS Sustainability, ‘Staff paper: General Sustainability-related Disclosures’ (October 2022) paragraph 54.

²³ *Directive (EU) 2022/2464 of the European Parliament and of the Council of 14 December 2022 amending Regulation (EU) No 537/2014, Directive 2004/109/EC, Directive 2006/43/EC and Directive 2013/34/EU, as regards corporate sustainability reporting* [2022] OJ L 322/15 (**EU Directive**), arts 19a(1) and 29a(1).

²⁴ The TCFD encourages all organisations to disclose Scope 1 and 2 emissions independent of an assessment of materiality. The disclosure of Scope 3 emissions is subject to materiality, but the TCFD encourages organisations to disclose these emissions: TCFD, *Implementing the Recommendations of the Task Force on Climate-related Financial Disclosures* (October 2021), p 6.

²⁵ TCFD, *Implementing the Recommendations of the Task Force on Climate-related Financial Disclosures* (June 2017), Draft IFRS S2, paragraph 21(a).

²⁶ *Corporations Act 2001* (Cth) s 301.

²⁷ *Ibid* ss 296 and 307A.

²⁸ *Ibid* s 307C.

Where concerns about audit quality have been raised, appropriate reviews and reforms designed to rectify these concerns have occurred.²⁹

38. Auditors have a right of access to the books of a company, registered scheme or disclosing entity, and may require any officer to provide information, explanations, or other assistance for the purposes of an audit or review.³⁰ Where appropriate, this might include independent expert assurance of an entity's claims.
39. The Association is of the view that these requirements are sufficient and well-adapted to the assurance of climate-related disclosures in covered entities' financial reports, and that similar requirements should apply to covered entities' greenhouse gas emissions disclosures, as will be required in New Zealand.³¹
40. As a practical example, the Association believes that auditors are well qualified by training, experience and the above-described statutory framework to assist the efficient operation of the market by providing assurance that covered entities' *emissions data* is being appropriately reported. Auditors are well-accustomed (for example, in the context of impairment testing) to review management's internal work, and any external assurance obtained by management as to specific subject-matters. The Association highlights emissions' reporting because, whilst it is critical to ensuring Australia fulfils its international and statutory climate-related commitments, there seems to be considerable uncertainty about it. Using satellite data, the International Energy Agency (IEA) estimates that Australian coal mines emit double the amount of methane – a particularly potent greenhouse gas – than has been officially reported.³² Recent analysis suggests that emissions from oil and gas facilities around the world are about three times higher than has reported.³³ This is a practical example of the importance of *competence* as a key consideration underpinning the design of the new regulatory system.

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

41. As noted above, the Association believes that covered entities should be required to report their greenhouse gas emissions in accordance with paragraph [21] of Draft IFRS S2. Draft IFRS S2 requires entities to report their Scope 1, 2 and 3 absolute greenhouse gas emissions in accordance with the widely-used *Greenhouse Gas Protocol Corporate Standard (GHG Protocol)*. The main principles and calculation methodologies of the *National Greenhouse and Energy Reporting Act 2007 (Cth) (NGER Act)* and related regulations are already aligned with the GHG Protocol.

²⁹ See, for example, Commonwealth Parliamentary Joint Committee on Corporations and Financial Services, *Regulation of Auditing in Australia: Final Report* (November 2020); Commonwealth Parliamentary Joint Committee on Corporations and Financial Services, *Regulation of Auditing in Australia: Interim Report* (February 2020).

³⁰ *Corporations Act 2001* (Cth) s 310.

³¹ *Financial Sector (Climate-related Disclosures and Other Matters) Amendment Act 2021* (NZ) s 461ZH. This provision comes into effect on the third anniversary of the Act obtaining Royal Assent, i.e. October 2024 (s 2(3)(b)).

³² Sabina Assan et al, *Tackling Australia's Coal Mine Methane Problem* (June 2022) p 17.

³³ Climate Trace, 'More than 70,000 of the highest emitting greenhouse gas sources identified in largest available global emissions inventory' (Website, 26 January 2023) <available at: <https://climatetrace.org/news/more-than-70000-of-the-highest-emitting-greenhouse-gas>>.

42. The key difference between the emissions disclosures required by Draft IFRS S2 and the NGER Act is that, under Draft IFRS S2, entities are required to disclose Scope 3 (upstream and downstream) emissions. The Association supports this as a positive improvement on the NGER Act. Scope 3 emissions disclosures are critical for investors and other stakeholders to be able to assess the risks in a covered entity's value chain, for example, the covered entity's financed emissions. However, it has been reported that, as at 2022, only 49% of ASX200 companies disclosed some Scope 3 emissions, and only 14% disclosed all Scope 3 emissions.³⁴ For entities already disclosing Scope 3 emissions, the Draft IFRS S2's requirements will standardise leading practices in this regard. For entities not already disclosing Scope 3 emissions, it will prompt better understanding of climate-related risks and opportunities, and their ability to manage a range of physical, transitional, regulatory, reputational and other risks. The Association acknowledges that there is difficulty and uncertainty in reporting Scope 3 emissions, but believes that this is already accommodated within Australian legal norms: see further below.

43. As mentioned above, if adopted, the ISSB Draft Standards will become a baseline, which will improve the consistency, comprehensiveness, and comparability of emissions disclosures. Derogation from this baseline, particularly in relation to such a significant aspect, would not be in line with the Treasury's stated reform principles and could be detrimental to Australia's integration into international markets.

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

44. The Association considers that it is desirable to have consistency between disclosures, including industry-specific metrics, and that the ISSB Draft Standards, and the industry-specific requirements in Appendix B to Draft IFRS S2 that are based on SASB Standards, provide appropriate common baseline metrics to ensure consistency and comparability of emissions disclosures.

45. In particular, Draft IFRS S2 and the industry-specific Sustainability Accounting Standards Board Standards (**SASB Standards**) appropriately require entities to:

- a. disclose absolute Scope 1, 2 and 3 greenhouse gas emissions;
- b. measure emissions in accordance with the GHG Protocol, which provides clear guidance on boundary-setting for corporate emissions accounting, amongst other things;
- c. express emissions as metric tonnes of CO₂ equivalent (**CO₂e**), meaning that entities' emissions disclosures must account for all seven greenhouse gas emissions covered by the Kyoto Protocol, and not just CO₂; and
- d. calculate the CO₂e of different greenhouse gases in accordance with the global warming potential values in the 2014 Fifth Assessment Report of the Intergovernmental Panel on Climate Change (**IPCC**).

46. However, the Association is of that view that the consistency and comparability of emissions disclosures could be improved by covered entities being required to use the same emissions accounting method in

³⁴ PWC, *ESG Reporting in Australia* (2022) p 14.

the GHG Protocol. Covered entities being able to choose whether they report operational or equity emissions impedes an easy comparison of those emissions.

47. The Association considers the reporting of equity emissions to be the most decision-useful information for investors and other stakeholders.

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

48. The Association believes that alignment with the 1.5°C temperature goal of the Paris Agreement and Australia’s legislated net zero emissions by 2050 target³⁵ should be a central consideration for climate-related risk management disclosures. This would help ensure that Australia fulfils its international and statutory climate-related commitments, and that Australia’s climate-related disclosure regime is scientifically-sound and aligned with international best practice.

49. The Association welcomes Draft IFRS S2’s requirements regarding covered entities’ disclosure of climate-related risk management, including the use of offsets³⁶ and whether climate-related targets align with the Paris Agreement.³⁷ The Association considers the adoption of these requirements would provide greater certainty regarding covered entities’ disclosure obligations, improve transparency regarding covered entities’ transition plans, and help rectify current deficiencies in Australian climate-related disclosures. This would in turn help reveal bad or substandard practice, facilitate more informed decision-making by investors and other stakeholders, and minimise the risk of misleading information that may expose investors and markets to unexpected losses.

50. For example, ongoing proceedings in the Federal Court of Australia allege that Santos Ltd misled investors when it claimed to have a “clear” and “credible” plan to achieve net zero emissions by 2040, in part because it purportedly failed to disclose the extent to which portions of the plan relied on offsets.³⁸ Such issues could be avoided by requiring covered entities to disclose the extent to which their climate-related targets rely on the use of carbon offsets and the type(s) of carbon offsets being used, in accordance with paragraph [13](b)(iii) of Draft IFRS S2.

51. However, in one respect, the Association considers that the requirements of Draft IFRS S2 could be clarified to reflect Australia’s international and statutory climate-related commitments. The Draft IFRS S2 requires covered entities to disclose whether their climate-related scenario analysis³⁹ and climate-related targets⁴⁰ are aligned with the Paris Agreement. However, it does not specifically require covered entities to conduct climate-related scenario analysis aligned with the 1.5°C temperature goal of the Paris

³⁵ *Climate Change Act 2022* (Cth) s 10(1)(b).

³⁶ Draft IFRS S2 paragraph 13(b)(iii).

³⁷ *Ibid* paragraph 23(e).

³⁸ *Australasian Centre for Corporate Responsibility v Santos Ltd* (NSD858/2021).

³⁹ Draft IFRS S2 paragraph 15(b)(i)(4).

⁴⁰ *Ibid* paragraph 23(e).

Agreement or to disclose transition plans compatible with limiting warming to 1.5°C. This is at odds with international standards regarding net zero emissions targets and international best practice:

- a. The EU requires “large undertakings” and “small and medium-sized undertakings, except micro undertakings, which are public-interest entities” to describe their plans, including implementing actions and related financial and investment plans, to ensure that their business model and strategy are compatible with limiting warming to 1.5°C and achieving the EU’s target of carbon neutrality by 2050, and, where relevant, their exposure to coal-, oil- and gas-related activities.⁴¹
- b. The Science Based Targets Initiative’s (SBTi) Corporate Net Zero Standard, which was the first international standard for corporate net-zero target setting aligned with the Paris Agreement, requires that, at a minimum, corporate Scope 1 and 2 emissions targets must be consistent with the level of decarbonisation required to keep warming to 1.5°C,⁴² and Scope 3 emissions targets must be consistent with well below 2°C of warming.⁴³
- c. The United Nations’ High-Level Expert Working Group on Net Zero Emissions Commitments of Non-State Entities concluded that non-state entities can only claim to be “net zero-aligned” if their transition plan is in line with the IPCC or IEA net zero emissions modelled pathways that limit warming to 1.5°C.⁴⁴

52. The Association submits that, as in the EU, covered entities should be required to disclose transition plans consistent with the IPCC and IEA modelled pathways that limit warming to 1.5°C. The transition plan disclosures required by Draft IFRS S2 otherwise appropriately balance the need for certainty regarding covered entities’ disclosure obligations and decision-useful information for users, on the one hand, and flexibility to accommodate covered entities’ varying circumstances and evolving market expectations, on the other. Statutory norms regarding corporate disclosures and misleading or deceptive conduct provide adequate controls on those baseline disclosure requirements.

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

53. The Association considers it sufficient that covered entities be required to disclose transition plans and scenario analysis aligned with the IPCC and IEA modelled pathways and scenarios that limit warming to 1.5°C (see response to Question 11 above). These pathways and scenarios reflect the best available science, and underpin international standards regarding emissions reduction targets aligned with the Paris Agreement, such as the SBTi’s Corporate Net Zero Standard and the UN Report. The provision of separate supporting information would, in our view, create unnecessary fragmentation and impose additional regulatory burdens and costs.

⁴¹ EU Directive, arts 19a(2)(iii), 29a(2)(iii).

⁴² SBTi, *SBTi Criteria and Recommendations* (Version 5.0, October 2021) criteria 15 and 16.

⁴³ SBTi, *SBTi Criteria and Recommendations* (Version 5.0, October 2021) criterion 18.

⁴⁴ United Nations, *Integrity Matters: Net Zero Commitments by Businesses, Financial Institutions, Cities and Regions* (November 2022) (UN Report), Recommendation 1.

54. To mandate that a particular entity or entities provide and govern that information may have a benefit in encouraging standardisation, and would be underpinned by the *competence* consideration outlined above. However, it would also add to regulatory burden and risks creating a “cottage industry” to which companies may then become beholden. The Association therefore believes that the existing audit assurance framework, combined with misleading and deceptive conduct laws, will create an adequately layered system for monitoring the competence, materiality and reliability of required disclosures.

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

55. The Association considers that the “reasonable grounds” requirements are appropriate and sufficiently flexible to accommodate uncertainties or assumptions in the context of climate reporting. The Association does not support the adoption of other tests or measures, such as the US “safe harbour” provisions, which would introduce unnecessary fragmentation of statutory norms.

56. Before commenting on the appropriateness of the “reasonable grounds” requirements, it may assist if we first seek to explain how these requirements operate.

57. Misleading or deceptive conduct is prohibited for example by the *Corporations Act 2001* (Cth), *Australian Consumer Law (ACL)* and the *Australian Securities and Investments Commission Act 2001* (Cth) (**ASIC Act**).⁴⁵ Where a representation is made about a future matter, it will be “taken to be misleading” if the person making the representation “does not have reasonable grounds for making the representation”.⁴⁶ Although this requirement does not shift the ultimate burden of proof, a finding that an entity has made a representation concerning a future matter places an evidential burden on the entity to adduce evidence that there were reasonable grounds for making that representation.⁴⁷ For there to have been “reasonable grounds”, there must have existed “facts sufficient to induce that state of mind in a reasonable person”⁴⁸ at the time the representation was made.⁴⁹

58. The Association considers the legal requirement that there must be “reasonable grounds” for making forward-looking statements is sensitive to the fact that some matters that are required by climate disclosure requirements are inherently uncertain. To the extent that there is inherent uncertainty in the scope, distribution, impacts and timing of the impacts of climate change, and to the extent that matters of that kind are required by climate disclosure requirements to be considered and disclosed, the “reasonableness” standard does not require the introduction of certainty where the subject matter makes that impossible. Each representation will be judged in its context, which will include any assumptions or other qualifications made at the same time. Reasonableness will then fall to be assessed in that context. So, where disclosures are made with appropriate disclosure of assumptions, methodologies

⁴⁵ *Corporations Act 2001* (Cth) s 1041H; ACL s 18; ASIC Act s 12DA.

⁴⁶ *Corporations Act 2001* (Cth) s 796C; ACL s 4(1); ASIC Act s 12BB(1).

⁴⁷ *Australian Competition and Consumer Commission v Woolworths Limited* [2019] FCA 1039 at [113] (this finding was not disturbed on appeal).

⁴⁸ *Prior v Mole* (2017) 261 CLR 265 at [98] (Gordon J); *Australian Competition and Consumer Commission v Dateline Imports Pty Ltd* [2015] FCAFC 114 at [100]; *George v Rockett* (1990) 170 CLR 104, 112.

⁴⁹ *Sykes v Reserve Bank of Australia* (1998) 158 ALR 710, 712 (Heerey J).

and uncertainties, the assessment of reasonableness will take into account those assumptions and disclosed uncertainties.⁵⁰

59. As an example of this, in *Bell Resources Ltd & Anor v BHP Co Ltd & Ors* (1996) ATPR 40-702, the Court considered forecasts of the company's profitability communicated to shareholders. The Court held that the profit forecasts were balanced and, under the circumstances of the case, supported a conclusion that the shareholders would understand them in the context of assumptions to which management had applied reasonable professional judgment. The shareholders could therefore be assumed to understand the disclosures to be the opinion of the company, not incontrovertible truths about the future.

60. In *TPT Patrol Pty Ltd v Myer Holdings Ltd* [2019] FCA 1747 at [1320]-[1322], Beach J said:

In determining whether a person held reasonable grounds for a representation of opinion, the relevant inquiry is into whether the facts possessed by him were capable of supporting the opinion that he held.

A person will have had reasonable grounds for making a representation with respect to a future matter if there are facts which are sufficient to induce that state of mind in a reasonable person.

The question whether there were reasonable grounds for the making of a profit forecast is to be resolved by looking at whether the relevant director had made a genuine assessment as to the appropriateness of the forecast. If such a genuine assessment had been made, there would be reasonable grounds to support the making of the forecast.

61. The Association does not believe that the "reasonable grounds" requirements operate unfairly or inefficiently. It is appropriate and efficient that entities be required by law to consider whether they have reasonable grounds for making forward-looking statements, and there is no principled reason to depart from this statutory norm merely because forward-looking statements concern climate-related matters.

62. In *Guidance 247, Effective Disclosure in an Operating and Financial Review*, ASIC states:

"In our view, the risk of being found liable for a misleading or deceptive forward-looking statement is minimal, provided:

- a. the statements are properly framed in the operating and financial review as, for example, being based on the information available at this time;*
- b. the statements have a reasonable basis, which involves good governance at board level for signing off on the statements; and*

⁵⁰ See, for example, *ASIC v Macdonald (No 11)* (2009) 256 ALR 199 at [373]-[374] (the actuarial reports relied upon were "inherently uncertain"). See also [79]-[83] of the General Requirements Exposure Draft, including the statement at [79]: "The use of reasonable estimates is an essential part of preparing sustainability-related metrics and does not undermine the usefulness of the information if the estimates are accurately described and explained".

c. *there is ongoing compliance with continuous disclosure obligations when events or results overtake forward looking statements in the OFR.*

63. As a consequence of these matters, the Association considers the “reasonable grounds” requirements are well-adapted to the uncertainties and assumptions inherent in some climate-related disclosures, such as climate-related scenario analysis. If a concern about legal liability sometimes means that a desired forward-looking statement *cannot be made* (i.e. because it lacks reasonable assumptions and therefore reasonable grounds), we do not perceive that to be a bad thing. In our experience, an important and valid concern of entities is that they lack precisely the guidance about processes and disclosures which the ISSB Draft Standards are intended to assist in providing. The ISSB Draft Standards appear likely to assist in exposing existing bad practice, in improving substandard practice (by providing a consistent framework against which substandard practice can be improved), and in standardising the reporting and disclosure which accompanies good practice.
64. The Association considers that a “safe harbour” insulating directors or companies against liability for statements lacking a reasonable basis would not support the goals of certainty, materiality and competence. They would risk undermining the beneficial effects of the ISSB Draft Standards by removing the effective incentive (liability risk) that will actuate companies to act carefully in adopting them.
65. A justification which has been proffered for a “safe harbour” is that scientific understanding, and methodologies for the measurement and quantification of risk, are constantly evolving. The Association suggests this is not a secure policy basis to create such a defence. That is because, under existing law, a forward-looking statement is not misleading merely because it later turns out to be wrong,⁵¹ or based on science or methods that were later overtaken. A forward-looking statement which later turns out to be wrong might be found to have been made on a reasonable basis at the time, if, for example, it was consistent with the best available science at the time. Investors and courts do not expect entities to predict the unpredictable, but instead to make sensible disclosures on a reasonable basis, and to update earlier disclosures if they become misleading by reason of later events.⁵²

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

66. The Association believes that this is an important consideration that should inform Australia’s new climate-related reporting framework, given rapidly evolving regulatory and market expectations regarding environmental, social, and governance matters. As detailed in our response to Question 5 above, the Association considers the first regulatory framework proposal in the Consultation Paper would allow sufficient flexibility to accommodate subsequent developments, such as the forthcoming recommendations of the Taskforce on Nature-related Financial Disclosures.

⁵¹ *Bonham atf Aucham Super Fund v Iluka Resources Ltd* (2022) 404 ALR 15 at [698].

⁵² See *Ambergate Ltd v CMA Corporation Ltd* (2016) 110 ACSR 642 at [36]-[37].

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

67. The Association supports reporting systems that increase transparency and the accessibility of decision-useful information, but otherwise has no comments in relation to this question.

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

68. Of the potential structures presented in the Consultation Paper, the Association considers that the ***first*** potential structure is the most appropriate.

69. That is, confirming the AASB as the entity responsible for developing, making, and monitoring climate- and sustainability-related disclosures. This would allow Australia to leverage the AASB's existing expertise in climate-related disclosures in its design and implementation of a new climate-related reporting framework, as well as its existing relationships with international standard-setting bodies.

70. The Association is concerned that the second potential structure could lead to further fragmentation of the regulatory landscape, and resulting confusion for users. The third potential structure risks further delaying the implementation of a mandatory climate-disclosure framework at a time when Australia is already experiencing regulatory lag, and investors and other stakeholders have expressed an “urgent need for disclosure standards on climate change”.⁵³

Conclusion

71. The Association thanks you for considering this submission. Should you wish to discuss, or if the Association may be of further assistance, please contact Lucy Kelley, Policy Lawyer, at lkelly@nswbar.asn.au.

Yours sincerely,



Gabrielle Bashir SC

President

⁵³ Draft IFRS S2, p 7.