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TO Climate Disclosure Unit
Market Conduct and Digital Division
Treasury
Langton Cres
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By email: climatereportingconsultation@treasury.gov.au

19 JULY 2023

Dear Climate Disclosure Unit

KWM – Submission on Climate-related Financial Disclosures: Second Consultation

We refer to Treasury's consultation paper on climate-related financial disclosures dated June 2023 (**Consultation Paper**).

The Consultation Paper seeks views on the proposed positions for the detail, implementation and sequencing of mandatory climate reporting in Australia. In particular, it seeks views on the proposed positions relating to coverage, content, framework and enforcement of the requirements.

We welcome the opportunity to comment on these issues. As stated in our first submission, we support standardised, internationally aligned requirements for climate-related financial disclosures. In the Annexure, we have set out comments for Treasury's consideration about the specific design proposal set out in the Consultation Paper.

We would be happy to discuss if you have any questions in relation to our submission.

Please contact one of us in the first instance.

Yours sincerely

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Annexure 1 KWM Submissions

#	PROPOSAL	SUBMISSION
1	That all entities that meet prescribed size thresholds and that are required to lodge financial reports under Chapter 2M of the *Corporations Act 2001* (Cth) (**Corporations Act**) would be required to make climate-related financial disclosures.	**Broad reach** The current proposal captures a broad range of entities, including proprietary companies. The reach is broader than many comparable jurisdictions which focus on "public interest entities". In designing the reporting regime, a balance needs to be struck between the benefits of reporting and the burden of reporting on entities. In our view, the focus of mandatory reporting should be on "public interest entities", including listed entities, large financial institutions, large superannuation funds and large emitters. Many public interest entities are already reporting in accordance with TCFD and have developed capability that will help them to meet the standards. As reported in our 2022 Climate Report, 96% of ASX50 entities are either fully or partially reporting against TCFD, or are in the process or aligning their reporting to the TCFD recommendations. We acknowledge that there are benefits in requiring a broad base of entities to report (such as ensuring that listed entities are not disadvantaged and creating transparency across the economy). However, we consider that these benefits need to be balanced with the burden of reporting on smaller entities. The phasing of reporting requirements assists with mitigating the burden of reporting on smaller entities. In addition to phasing, the Australian Accounting Standards Board (**AASB**) should consider implementing limited reporting requirements for other (non-public interest) entities (such as private companies in the third cohort) that focus on information that allows funders, insurers and other entities in their value chain to fulfil their reporting obligations. This approach would be in line with comparable jurisdictions which focus on "public interest entities" (for example, UK, US, Hong Kong and New Zealand): • In the UK, companies and limited liability partnerships (**LLPs**) that fall into certain public interest categories have to report (such as entities that are listed in a UK regulated market, banking companies, insurance companies and companies with securities admitted to AIM). Companies and LLPs that do not fall into a special public interest category only have to report if they have more than 500 employees and a turnover of more than £500,000,000. This threshold is significantly higher than the threshold in the proposed regime. • Similarly, in New Zealand, only entities that fall into similar public interest categories are required to produce climate-related disclosures. These entities include certain financial institutions, certain registered investment

		schemes, certain licenced insurers, certain listed issuers of quoted securities and certain listed issuers of quoted debt securities. In addition to these categories, the New Zealand regime also has size thresholds that entities must meet before having to report. • In the US and Hong Kong, mandatory climate reporting is being led by the local stock exchanges. Accordingly, the rules only apply to entities listed on those stock exchanges. They do not apply to private companies. The scope of the proposed regime is reasonably comparable to the EU Corporate Sustainability Reporting Directive (**CSRD**). Like the proposed regime, the CSRD in its end-state will require companies of a certain size to report on sustainability, even if they are privately owned. The size thresholds in the CSRD are comparable to the thresholds in the proposed regime.[1] **Funds** Currently, registered schemes are required to report under Part 2M of the Corporations Act. As noted in the Consultation Paper, registrable superannuation entities (**RSEs**) will also have to report under Part 2M of the Corporations Act from 1 July 2023 when the *Treasury Laws Amendment (2022 Measures No. 4) Act 2023* (Cth) comes into effect. Further consideration will be required in relation to the reporting obligations of funds. In particular: • The relevant reporting entity will be the trust, but the reporting obligations will need to apply to the responsible entity (in the case of a registered scheme) or the RSE licensee (in the case of an RSE). Currently, under s 285(3) of the Corporations Act, for the purposes of applying Chapter 2M to a registered scheme, the scheme's responsible entity is responsible for the performance of obligations in respect of the scheme. A similar provision (s 285(3A)) will be inserted in respect of RSE licensees by the *Treasury Laws Amendment (2022 Measures No. 4) Act 2023* (Cth) which makes RSE licensees responsible for the performance of the RSE's obligations. It will be necessary to ensure that these provisions apply to climate reporting (as we expect will be the case). • Some funds invest in real assets, but most invest in shares and other financial instruments issued by third parties. Where relevant, the Australian-specific standards should provide guidance specific for funds and similar entities that invest in financial products (rather than real assets). For example, in relation to the measurement of scope 3/financed emissions and scenario analysis. • Further, consideration should be given to the fact that funds and other financial institutions rely on third-party information of the companies they invest in for their reporting. This affects the timing and quality of disclosures for these entities. Accordingly, adjustments should be made in acknowledgment of the entity's reliance on third-

[1] Under the CSRD, entities are considered "large undertakings" if they meet at least two of the following criteria balance sheet total: EUR 20,000,000; net turnover: EUR 40,000,000; or average number of employees during the financial year: 250. "Large groups" are also required to report if they exceed at least two of these three thresholds on a consolidated basis.

		party information (such as guidance on the meaning of "reasonable grounds" when relying on third-party disclosures). • The proposal states that as industry-specific metrics develop, entities will be required to disclose against industry-specific metrics. The Australian-specific standards should consider how this will work for reporting entities that invest in a variety of sectors. We also note that the proposal does not capture funds that are not required to report under Chapter 2M. This will include a large number of substantial wholesale funds with investments of hundreds of millions if not billions of dollars. The exclusion of these funds from the proposed reporting regime, and the exclusion of large charitable not-for-profits, highlights the inconsistency of requiring smaller private companies to report. We are not advocating that the regime be expanded, but we do reiterate our submission that reporting requirements for private entities in the third cohort of reporting entities should be limited. **Not-for-profits** We note that not-for-profits registered with the Australian Charities and Not-for-profits Commission (**ACNC**) do not report under the Corporations Act and will not be caught by the proposed mandatory reporting scheme. However, not-for-profits that are not registered with the ACNC and are required to report under Chapter 2M, will be caught by the scheme if they meet the size thresholds. This will place a significant burden on sporting clubs and similar organisations who rely on member subscriptions, donations and volunteers to operate on a not-for-profit basis, for very little utility or benefit to stakeholders. There is no consistency in requiring a smaller sporting club to report, but not huge charitable organisations like the Red Cross, the Salvation Army, hospitals, aged care providers and large educational institutions. We submit that for consistency, efficiency and utility, the scheme should not apply at all to not-for-profits, or at least not to not-for-profits in the third cohort.
2	Principles of financial materiality would apply.	The proposed materiality threshold is "climate-related financial information would be material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial reports (existing and potential investors, lenders and other creditors) make on the basis of the reports". This definition is aligned with the materiality threshold in the standards developed by the International Sustainability Standards Board (**ISSB**) and the materiality threshold in AASB Standard 101. In our view, this is preferred as it allows for comparability of climate disclosures across jurisdictions.
3	To maintain alignment with existing corporate reporting practices, climate disclosures	**Directors' declarations** Information included in a financial report is subject to the directors' declaration (and a CEO and CFO declaration for listed companies) that the disclosures give a true and fair view and comply with applicable standards. Given assurance of

	would be required to be published in an entity's annual report.	climate reporting will be phased in, under the current proposal, directors, CEOs and CFOs will be asked to give declarations covering elements of the climate disclosures that are not assured. This will impose significant risks on directors, the CEO and CFO, given not only the lack of assurance but also the evolving nature, the development of internal and external expertise on which the certifiers will rely, and the inherent uncertainties involved in climate reporting. For consistency, we consider it would be appropriate that the declarations required by directors, CEOs and CFOs in relation to climate reports are only required to the extent that reasonable assurance has been given in relation to the report. We also note that the directors' report is not subject to the same declaration and assurance requirements as the financial report. Accordingly, it matters whether disclosures are contained in the directors' report or the financial report. In designing the legislation, the difference between the two reports should be considered and guidance should be provided about what information goes in which report. **Remuneration reporting** The final standards developed by the ISSB require that entities disclose whether and how climate-related considerations are factored into executive remuneration and the percentage of executive management remuneration linked to climate-related considerations. It would be helpful if guidance was provided in relation to the Australian-specific standards around the expectations and level of detail required in this disclosure – is it sufficient to say that this is an element of operational risk considered in assessing variable remuneration? Or does this reporting requirement imply that yet more elements are to be imposed on remuneration structures? **Half-year reports** It would also be helpful to confirm that climate reporting (including updates to climate reporting required to be included in annual reports) is not required to be included in half-year financial reports under Chapter 2M.
4	The application of misleading and deceptive conduct provisions to scope 3 emissions and forward-looking statements would be limited to regulator-only actions for a fixed period of three years.	Currently, it is proposed that the three-year modified liability regime will commence from 1 July 2024 (when the mandatory reporting regime commences). Assuming that the modified liability regime will only apply to reports published in the three-year period ending on 30 June 2027, rather than reports published with respect to years commencing during that three-year period, the modified liability regime will only apply to two reports. Further, it will apply to only one report that includes scope 3 emissions. To ensure the regime actually has effect for three reporting periods (as we assume is intended), it should at least apply to all reports made with respect to financial years commencing in the three-year period to 30 June 2027. We submit that consideration should also be given to applying the modified liability regime to the first three years' climate reports for each cohort.

		Further, given the short timeframe between the release of the AASB standards and the commencement of mandatory reporting, we consider it would be appropriate for the modified liability regime to be broader. This would allow entities to build internal capability and embrace continuous improvement. We remain concerned that the requirements under the ISSB standards for forward looking statements about the financial impact of climate-related issues will not be able to be made on reasonable grounds and will therefore breach Australian laws concerning misleading statements. Broadening the modified liability regime during a transition period will enable practice and guidance to be developed if, as appears to be the case, Treasury intends that this risk will be imposed on the corporate and director communities without safe harbours. For example, Treasury should consider some (or all) of the following extensions to the safe harbour regime: • limiting regulatory actions during the three year period to declarations, injunctions and infringement notices (i.e. no civil penalties or disqualification of officers); • applying the modified liability regime to all climate disclosures that rely on information from third parties, in addition to scope 3 emissions and forward-looking statements; • extending the timeframe of the regime for disclosures of scope 3 emissions given the deferral of scope 3 reporting and various uncertainties in reporting scope 3 emissions; • extending the regime to climate-related disclosures in other disclosure documents required under the Corporations Act, including fundraising documents, scheme documents and takeover documents; and • extending the regime to statements made under continuous disclosure rules to amend or augment information in an annual climate report, and to breaches of continuous disclosure rules for failing to amend or augment information in an annual climate report. Further, guidance on what constitutes “reasonable grounds” for forward looking statements in climate disclosures would be helpful given the inherent uncertainty of physical and transition risks. Particular guidance that addresses what constitutes “reasonable grounds” in the context of reliance on third-party information would be valuable for entities when preparing disclosures that rely on third-party information (such as scope 3 emissions).