AIRA
AUSTRALASIAN INVESTOR RELATIONS ASSOCIATION

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ABN 66095554153
[redacted]

21 July 2023

Director
Climate Disclosure Unit
Market Conduct and Digital Division
The Treasury
Langton Crescent
PARKES ACT 2600

By email: climatereportingconsultation@treasury.gov.au

Dear Sir/Madam,

Submission to the second Treasury consultation on climate-related financial disclosures

The Australasian Investor Relations Association (AIRA) is pleased to submit this response to the Department of Treasury's Second consultation paper on Climate-Related Financial Disclosure, issued on 27 June 2023.

AIRA is the peak body representing investor relations practitioners in Australia and New Zealand. The Association's 160 corporate members now represent over A$1.2 trillion of market capitalisation, over 80% of the total market capitalisation of companies listed on ASX.

We exist to provide listed entities with a single voice in the public debate on corporate disclosure and to improve the skills and professionalism of members. Our vision and purpose is that investor relations enables and creates sustainable value for all capital market stakeholders by building and strengthening market confidence in listed and unlisted entities.

Overall Comments on Consultation Paper Proposals and Objectives

AIRA wishes to place on record its strong support for the underlying goals underpinning the discussion paper and the Australian Government's approach to disclosure of financial risks and opportunities relating to climate change. In particular, we agree that:

- Disclosure of financially-material climate risks and opportunities should be mandated and, as far as practicable, made consistent, comparable and decision-useful across different industry sectors, frameworks and jurisdictions, building on the foundations established by initiatives such as the TCFD and ISSB.

- The focus of the mandatory disclosure regime should be on the specific information needs of the providers of investment capital (including debt as well as equity) and on financial materiality. This of course should not inhibit any communications from reporting entities targeted at other key stakeholders such as non-government organisations, local communities and society at large; however, we agree that the 'single materiality' financial focus proposed in the consultation paper is the correct one for the mandatory reporting aspect.
- The coverage of the mandatory rules should be broad, including private as well as public and listed entities of comparable size, and with government-owned business enterprises also being included under suitable legislative requirements.
- The degree of uplift to existing financial reporting requirements and practices will be significant, even among organisations such as AIRA's members which, as larger ASX-listed entities, are generally some way down the path of meeting the new requirements through voluntary adoption of frameworks such as the TCFD, CDP, SASB etc – as well as mandatory emissions reporting through the existing NGER framework. Whilst this will require significant additional resources from our members, subject to our comments below our members accept this additional burden given the urgency of the climate crisis and the need for Australian issuers to respond and keep pace with global developments.
- A graduated phasing in of the mandatory disclosure requirements to three broad categories of entities, based on their size, over the coming 5 financial years from 2024/25 to 2028/29 is an appropriate and practical means of implementing the new framework (again subject to our comments below).
- It is appropriate that reporting entities be expected to undertake at least a baseline level of best practice climate disclosure and measurement, including scenario planning against at least two plausible scenarios (one of which is aligned with the Australian Government's current legislative objective), transition planning, Scope 3 emissions reporting (eventually moving from a qualitative to a more quantitative format), and in accordance with industry-specific standards as they evolve.
- Disclosure of any exclusions in calculating scope 3 emissions and the estimations used to calculate these emissions should be mandated. This level of transparency will provide comparability and consistency when comparing like for like reporting entities.

Specific Comments on Implementation

In summary, AIRA believes that the public policy and key proposals put forward in the Consultation Paper are fundamentally sound and should be formalised through necessary legislative amendments and/or incorporation into Australian Accounting Standards in tandem with the recent global reporting standards S1 and S2 issued by the ISSB, as required.

Our only significant concerns with the proposals put forward in the consultation paper relate to *practical implementation* and *cost* issues in the early phase of adoption of the new requirements, particularly with regard to the proposed assurance requirements.

As investor relations and ESG professionals in major listed companies, AIRA's members have had significant experience in the practicalities of expanding the scope of corporate reporting beyond its traditional scope of financial accounts reporting to broader sustainability and ESG reporting, and in many cases to very detailed reporting against existing climate disclosure frameworks such as the TCFD and CDP. For these companies, the transition to this more comprehensive disclosure suite has generally been a progressive, multi-year project, even in cases where there was a strong Board and Executive conviction and substantial resources allocated to expediting the process as much as possible.

Against this background, anecdotal feedback we have received from certain of our members who are the most advanced in their climate disclosure, when reviewing the Treasury consultation paper, has been along the lines of "*This is going to be hard enough for us to do. But it's hard to imagine how anyone who was just starting out now could possibly get there by 2024/25.*"

On further unpacking this reaction, the main concern our members are expressing is not around any lack of conviction around the urgency of improved climate risk reporting or the willingness of companies to provide it – concerns that we agree would be rendered less relevant in a mandatory reporting system in any case. Instead, the concern was squarely focused on *the availability, long lead times, scope and costs of engaging external assurance providers to review disclosure material*.

We would strongly urge Treasury to consider this feedback from experienced corporate reporting practitioners from the 'top end' of the listed market and be mindful of potential challenges in its ongoing rollout of the new mandatory reporting requirements. We do not suggest that these concerns necessarily warrant a delay in the Treasury's proposed phase-in timetable across the three groups of issuers, or the scaling back of the more ambitious requirements in areas like scenario planning, transition management and Scope 3 disclosures. Rather, **we suggest the key area in which Treasury may wish to 'flex' its proposals is in the nature and extent of assurance requirements that reporting entities will need to adhere to** (even recognising the leeway that has already been foreshadowed in the paper around the phasing from 'limited' to 'reasonable' assurance, and the need for more granular assurance standards to emerge in areas like scenario planning and Scope 3).

Some specific considerations

Some specific considerations that we would suggest Treasury might consider in this regard are:

Exponential increase in the number of reporting entities.

The consultation paper notes (but does not quantify) the significant expansion in the number of Australian entities that will be required to undertake mandatory climate disclosure. It also notes the relative dearth of expertise, standards and accreditation in the specific specialisation of climate risk assurance, with the most relevant locus of expertise being some 76 individuals currently registered by the Clean Energy Regulator as Greenhouse and Energy Auditors under the NGER reporting framework.[1]

Whilst we are unaware of the exact numbers in each Group, one estimate we have seen of the total coverage of the new reporting requirements once all three Groups are covered from FY2027/28 is 13,000 entities[2]. This compares to around 900 entities currently covered by the closest mandatory reporting standard, NGER. [3]

[1] Discussion Paper, p.24 and https://www.cleanenergyregulator.gov.au/Infohub/Audits/register-of-auditors
[2] Source: KPMG
[3] As an aside, AIRA suggests that Treasury and other relevant Government agencies consider the potentially conflicting or duplicated timeframes for submissions and limited assurance under the NGERs requirements (currently due at the end of October), and the proposed alignment of the new mandatory climate-related financial disclosures in line with financial reporting deadlines. To avoid confusion, a clarification on the process around the future of NGERS reporting timeframes would be appreciated.

It is of course expected that there will be a significant uplift in skills development and resources in the audit and assurance profession in anticipation of the introduction of mandatory climate reporting from 2024/25. The main question, however, is whether this uplift can in fact keep pace with the level of demand. Some obvious further questions arise as to the potential risk of slippage in audit and assurance quality that may stem from this situation.

An additional concern is the significant cost impacts on reporting entities, including AIRA members, stemming from the sudden emergence of a growing captive market of reporting entities having to compete for increasingly scarce high-quality assurance and advisory services within tight time-frames of financial reporting periods.

Overlap with other new Australian and international ESG disclosure requirements

It is understood that the current proposals only relate to the topic of climate-related financial disclosures, and we agree that this is the most urgent area of enhanced ESG disclosure for policymakers to address, both in Australia and overseas.

Nevertheless, it is also clear that there are a number of other significant new ESG disclosure initiatives in the pipeline, and that these are likely to be implemented within an overlapping timeframe as per the requirements envisaged in the consultation paper. These include:

- whatever adaptation of Australian accounting standards are adopted by the AASB in its review of the IFRS S1 and S2 standards,
- more granular reporting and accountability requirements following the recent review of the Modern Slavery Act, and
- expected new global standards to be developed by the TNFD in the areas of biodiversity and nature-related risks.

In addition to the above, even within the confines of climate risk reporting alone, many Australian entities including AIRA members which have offshore operations will be required to navigate the emerging disclosure frameworks being developed in other jurisdictions, such as the CSRD in Europe and the proposed SEC requirements in the US.

Despite all the progress that has been made in harmonising disclosure frameworks across jurisdictions over recent years, the global reporting landscape is still quite fragmented, and we are some way off having mutual recognition or interoperability between all these different reporting frameworks. This situation poses significant additional practical challenges to reporting entities, no matter how strong their conviction to be leaders in this area.

Nature of intended disclosure recipients

As noted above, AIRA strongly supports the focus of Treasury’s proposed disclosure requirements being on the information needs of the providers of financial capital.

By its nature, however, it should be noted this cohort of disclosure recipients generally comprises a highly sophisticated, professional investor audience. Investors (and their own advisers) are generally better placed than other stakeholder groups to make their own assessment of the quality of disclosure, conformance with recognised industry standards, and extent of governance oversight.

In this regard, investors may not require the same level of external assurance of all aspects of climate disclosure – for example those relating to the Strategy and Governance pillars of the TCFD/ISSB frameworks, which are generally in the domain of oversight issues on which investors expect directors to have adopted distinct approaches that are specific to the reporting entity's unique circumstances. By contrast, Risk Management and Metric & Targets pillars may be considered more important for external assurance requirements and to greater standardisation across industries.

We would also urge Treasury to consider the inverse of the above point about the primary focus being on the information needs to providers of investment capital. That is, reporting entities (most particularly listed companies operating under the ASX Corporate Governance Principles) still need to cater to the legitimate information and disclosure needs of their *non-professional investor* stakeholders – communities, employees, NGOs, media, regulators and so on. Many companies have made very significant progress in this area using adjacent frameworks to the TCFD/ISSB – such as the Global Reporting Initiative (GRI), Integrated Reporting and United Nations Sustainable Development Goals (SDGs), which remain the pre-eminent frameworks for broader ESG disclosure globally.

In this regard, the potential detriment that may be seen is essentially one of skewed allocation of scarce resources – will/might the quality of generic ESG disclosure decline as companies naturally turn their priority to the mandatory reporting and assurance requirements?

Or more fundamentally still, might the mandatory requirements instill a minimalist compliance approach as opposed to a more candid, fulsome approach to disclosure across the market?

Recommendations

As noted repeatedly in this submission, AIRA does not wish to advocate any delay or diminution on scope of the mandatory climate reporting framework proposed in the Second Consultation Paper.

Rather, our goal is to suggest consideration of a more flexible approach to implementation of the new rules, commensurate with the level of 'real-world' impact it will likely have on the practices and priorities of reporting entities.

Some specific measures we suggest that Treasury may wish to further consult on and consider include:

1. **Permitting a limited level of assurance over qualitative disclosures**

   Whilst obtaining reasonable assurance is appropriate for quantitative metrics such as scope 1, 2 and 3 emission disclosures, we suggest allowing entities to obtain a limited level of assurance over other qualitative climate disclosures, with a move to reasonable assurance at a later date.

Furthermore, the Governance and Strategy pillars that are being adopted from the TCFD framework are essentially more qualitative in nature and are areas in which investors might reasonably expect company directors to have adopted very specific oversight practices that are aligned to the entity's unique circumstances (rather than being framed by broader industry assurance standards at the outset). Moreover, these are areas in which investors already have significant resources at their disposal to evaluate companies' practices (including ASX Principles, investment stewardship policies, investor collaborations like ACSI and IGCC, proxy advisers, sustainability research providers and the like).

Greater flexibility in this regard should still provide transparency and accountability to all stakeholders while allowing greater scope for innovation by reporting entities and for existing resources such as ASX Principles, investment stewardship policies, ACSI, IGCC to align to the proposed standards.

2. ***Retain 'limited' assurance for individual industries until sector-specific standards have been finalised and adopted, before escalating to 'reasonable' assurance***

The implementation roadmap in the discussion paper recognises that time will be needed for assurance standards to progress from a 'limited' to a 'reasonable' level, but there appears to be no recognition of that transition taking longer in some sectors than in others.

Whilst recognising that sector-specific transitions would complicate the implementation timetable envisaged in the consultation, we suggest this would be manageable if handled appropriately, and would be more reasonable in terms of expectations of reporting entities.

3. ***Retain flexibility to adjust the assurance roadmap and timetable in light of market experience***

This recommendation essentially calls for a periodic stocktake of the actual market experience (progress of reporting standards, availability of assurance expertise, addition of new ESG requirements etc), and decisions being made at those intervals about the next implementation phase.

Counterbalancing this, of course, is the need for sufficient certainty as to the timing of enhanced assurance requirements, towards which both audit firms and reporting entities can plan. We appreciate that this is precisely the balancing act that the Consultation Paper has sought to undertake. However, at this very early stage, the unknown factor is whether the fixed timing schedule proposed will in fact turn out to be feasible in practice.

At minimum, we suggest, this would require the timetable and roadmap from Day 1 to be expressed as strongly aspirational, and only embedded in soft regulation or guidance, not hard coded into legislation.

Conclusion

AIRA welcomes the opportunity to contribute to Treasury's consultation on this topic. We believe the intent and impact of the measures being proposed are overwhelmingly positive for the Australian economy and look forward to their successful implementation.

Our submission does, however, raise a number of questions of practical implementation effects that we believe need to be addressed to ensure the overall policy measures are successful. We trust that our comments are understood in this light.

AIRA would be delighted to expand on this submission in discussion with Treasury, and to make available expert resources from our newly-established ESG Chapter to provide individual case studies and experiences from our membership.

Please do not hesitate to contact me on [redacted] if you would like to take up such a discussion or require any further information.

Yours sincerely

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Chief Executive Officer