

8 February 2024

Director
Climate Disclosure Unit
Climate & Energy Division
Treasury
Langton Cres
Parkes ACT 2600

By email: climatereportingconsultation@treasury.gov.au

Dear Sir/Madam,

Response to Climate-related Financial Disclosure Exposure Draft Legislation

We appreciate the opportunity to provide our comments on Treasury's *Climate-related Financial Disclosure Exposure Draft Legislation*.

Nexia Australia Pty Ltd represents the six independent chartered accounting firms comprising the Nexia Australia network with 80 partners servicing clients from small to medium enterprises, large private companies, not-for-profit entities, subsidiaries of international companies, and listed public companies.

We provide the following comments on the Exposure Draft legislation:

Item 23, Section 296D - Climate statement disclosures

We disagree with the entirety of subsection 296D(1).

In our opinion, the contents of a Climate Statement and any notes to the Climate Statement should be specified in Sustainability Standards issued by the Australian Accounting Standards Board and not additionally contained in legislation.

Modified director liability for scope 3 disclosures

The proposals seek to limit liability of directors for certain misleading and deceptive, and other, conduct in relation to the most uncertain parts of a climate statement prepared for financial years commencing between 1 July 2024 and 30 June 2027.

The policy intention is to ensure that during the transitional period, ASIC can undertake a role that promotes education about compliance with the new reporting regime and deter behaviour and reporting practice that is contrary to the policy position [Explanatory Memorandum, 1.119].

ASIC may still pursue actions under various sections, including section 1041E (false or misleading statements which include a fault element), but during the transitional period, the remedies available to ASIC are limited to declarations and injunctions [Explanatory Memorandum, 1.120].

We are not opposed to these proposals.

However, the proposals result in entity's auditors being exposed to a greater degree of enforcement and legal risks in respect of the climate statement than the company's directors, who have ultimate responsibility for the preparation of the sustainability report.

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In our opinion, such an outcome is inappropriate, unfair, and disproportionate to the respective roles and responsibilities of directors and auditors.

If the policy intention is to ensure that during the transitional period, ASIC can undertake a role that promotes education about compliance with the new reporting regime and deter behaviour and reporting practice that is contrary to the policy position [Explanatory Memorandum, 1.119] and allow ASIC to rectify these errors in reports during the transitional period to enable entities to understand and rectify errors, whilst ensuring that information made available in these reports is correct and complete [Explanatory Memorandum, 1.122], then in our opinion, a similar policy position should apply to auditors who are similarly coming to terms with the new reporting regime.

Item 23, subsection 296B(1) and Item 95, section 309A – Audit requirements where no material climate risks and opportunities

Item 95, Section 309A sets out reporting obligations by the auditor of the Sustainability Report.

The directors may determine that a company has no material climate-related risks or opportunities and identifies no matters to be reported in a Sustainability Report [Item 23, subsection 296B(1)].

In those circumstances, we are concerned that the auditor will be required to undertake their own analyses, scenario assessments, and business strategy and risk assessment procedures in order to form an opinion as to whether the auditor either concurs or disagrees with the directors' assessment.

In our opinion, there is a significant likelihood that the burden and responsibility for identifying material climate risks and opportunities will not reside with the directors but with the auditor.

We disagree with the proposal which could impose more onerous assessment obligations on the auditor than the directors of the auditee. We recommend that the audit and auditor's reports requirements [items 83 – 111] be amended so that an auditor is not required to form an opinion on the directors' assessment where subsection 296B(1) applies.

Appointment of separate Sustainability Auditor

Paragraph 1.72 of Part 2 of the Explanatory Memorandum states, in part, that "the sustainability disclosure report would be audited by the auditor of the financial report supported by technical climate and sustainability experts where appropriate."

However, the legislation is unclear:

- a) where the requirement that the auditor of the Financial Report is – or must be – the auditor of the Sustainability Report;
- b) whether, if an audit firm, or an audit company, conducts an audit or review of the Sustainability Report, the lead auditor is – or must be – the same person that is the lead auditor for the auditor of the Financial Report [refer Item 85, s307AC].

We are concerned that smaller audit practices that perform financial statement audits may not have the capacity, capability, or expertise – or for risk management purposes may choose not to – perform an audit of a Sustainability Report.

Requiring the same individual to be the auditor of the Financial Report and the Sustainability Report may preclude some smaller audit practices from the financial audit market and could reduce overall competition in the sector.

Furthermore, it would potentially preclude an audit firm or audit company utilising in-house expertise to enable one auditor to perform the audit of an entity's Financial Report and another auditor to perform the audit of its Sustainability Report.

In our opinion, the legislation should make clear that the auditor of the Sustainability Report need not be the same individual auditor, audit firm, or audit company that performs the audit of the Financial Report.

Pathway for assurance requirements

We note an apparent inconsistency between the policy intent described in paragraph 1.72 of Part 2 of the Explanatory Memorandum and the assurance requirements contained at Item 81, section 301B of the draft legislation.

We recommend that Item 81, section 301B of the draft legislation be amended so that the pathway for phasing in assurance requirements will be determined by the Auditing and Assurance Standards Board and not by legislation.

Other matters

We note that Treasury requested that submissions focus on whether the Exposure Draft legislation and explanatory materials appropriately reflect and give effect to the policy intent outlined in the Policy Statement. Nevertheless, we reiterate our following previous comments dated 19 July 2023 on Treasury's second Consultation Paper:

Transition planning and assurance

The Australian auditing profession has been beset by staffing shortages for a number of years, exacerbated by the Covid-19 pandemic affecting the number of inbound qualified professionals. Difficulties in attracting and retaining quality staff to the audit profession has been a concern that many have expressed to ASIC over the years.

We are concerned that the proposed staged timetable for implementation of the proposals will not provide sufficient time for mid-tier and smaller audit firms (that is, outside the Big 4 accounting firms) to upskill and develop the capabilities and capacity to provide climate-related assurance services to companies within the timetable proposed by Treasury.

Consequently, we recommend that Treasury extend each of the assurance transition periods by at least 12 months.

Reporting location, frequency, and timing

The draft legislation notes that climate-related disclosures will be included in a Sustainability Report which constitutes the fourth component of the annual financial reporting obligations and will be incorporated into an entity's annual report. Whilst the principal aim of integrating climate disclosures within the annual report is to foster consistency and mitigate redundant narratives across multiple reports, our previous concerns remain.

We maintain a preference for reporting climate-related information outside the annual report. We remain concerned that requiring significant additional non-financial information to be prepared and lodged as part of an entity's annual report will:

- i) Impose additional burden on financial report preparers by requiring them to provide climate-related information at the same time as resources are dedicated to the preparation of financial information;
- ii) Impose additional burden on auditors who are required to perform additional procedures on potentially material climate-related information included as part of the annual report at the same time as resources are dedicated to the audit of the financial information;

- iii) Delay an entity's planned finalisation and lodgment of its annual report due to the requirement to provide assurance over climate-related information before the entity can finalise and lodge its annual report; and
- iv) Audit firms, currently under significant industry-wide resourcing constraints, will be subject to further resourcing pressure because of the requirement to have the technical knowledge to be able to provide assurance over climate-related information even if that information has been prepared by an external subject matter expert.

Reporting entities and phasing

We acknowledge Treasury's proposal to address Group 3 entities that have no material climate-related risks and opportunities [Item 23, subsection 296B(1)].

However, we remain concerned that many proprietary companies are closely-held by family groups and often have no or few external stakeholders or users of their financial information. In many cases, their financial reports are prepared solely to meet their reporting obligations under the Corporations Act and, where relevant, are provided to external lenders.

Treasury has not indicated how Scope 1, Scope 2 and Scope 3 greenhouse gas data reported by entities is intended to be collated and used by either governments or others.

Extending mandatory climate reporting to large proprietary companies would impose significant time, cost, and resource burden of preparing and auditing such information without explaining to this cohort the purpose, usefulness, or expected benefits of doing so.

To more appropriately balance the actual regulatory cost and the potential benefits on Group 3 entities, we recommend that a more appropriate threshold is:

- Disclosing entities [as defined in subsection 111AC of the Act] required to report under Chapter 2M of the Corporations Act 2001 and that fulfill two of the three thresholds:
 - has over 100 employees;
 - The value of consolidated gross assets at the end of the financial year of the company and any entities it controls is \$25 million or more;
 - The consolidated revenue for the financial year of the company and any entities it controls is \$50 million or more.

Should you wish to discuss any aspects of this submission, please contact Martin Olde at molde@nexiaaustralia.com.au.

Yours faithfully

Nexia Australia Pty Ltd

Nexia Australia