ACSI
Level 23, 150 Lonsdale St, Melbourne VIC 3000 | **T** +61 3 8677 3890 | **E** info@acsi.org.au | **W** www.acsi.org.au

20 February 2023

The Treasury
Langton Crescent
Parkes ACT 2600

Submitted via email: climatereportingconsultation@treasury.gov.au

Dear Sir/Madam

CLIMATE-RELATED FINANCIAL DISCLOSURE: CONSULTATION PAPER

On behalf of the Australian Council of Superannuation Investors (ACSI), thank you for the opportunity to make a submission to the Climate-related Financial Disclosure Consultation Paper (the Paper).

About ACSI

Established in 2001, ACSI exists to provide a strong voice on financially material environmental, social and governance (ESG) issues. Our members include 26 Australian and international asset owners and institutional investors with over $1trillion in funds under management.

Through research, engagement, advocacy and voting recommendations, ACSI supports members in exercising active ownership to strengthen investment outcomes. Active ownership, including the management of climate related risk, allows institutional investors to enhance the long-term value of retirement savings entrusted to them to manage.

This submission draws on ACSI's long-standing practice of detailed engagement with listed companies in relation to climate-related risks and opportunities, as well as detailed research into market practice. Our expertise is primarily in respect of Australian listed equities, with the focus on the ASX300, and our comments reflect that perspective.

Summary of ACSI position

ACSI welcomes the proposed introduction of mandatory climate-related financial disclosures. Adopting mandatory climate reporting would see Australia follow other jurisdictions around the world, such as the UK, US and New Zealand, and is a logical step towards a global baseline for sustainability reporting. As long-term investors, sustainability risks, including climate-change related risks, are financial in nature and deeply embedded across the economy. They are a significant challenge for Australian companies and investors, including superannuation funds. ACSI members need information on their investee companies' exposure to physical and transitional risks related to climate-change. Such information is integrated into investment processes and is used by investors in investment analysis, risk assessment, stewardship activities and investment due diligence. Given our members invest across global markets, there is a strong appetite for consistency and comparability in the approach to disclosure.

The lack of a standardised approach to climate reporting means the quality of reporting varies widely across companies. Mandatory disclosure of climate data, including emissions, targets, strategy and risk management processes, would enable investors to identify the adequacy of responses to climate risk and opportunity. The introduction of mandatory reporting would also provide an important signal to investors, companies and regulators about market level risks associated with the transition to net zero. Mandatory reporting would act to lift the market as whole – improving disclosure by laggard companies and driving transparency on climate change strategies for Australia's largest companies.

Answers to the consultation questions are included in Attachment 1. ACSI's positions on key issues are summarised below:

The ISSB standard should be adopted

ACSI welcomes the adoption of mandatory, internationally aligned climate reporting standards that will enhance the comparability and credibility of climate reporting from Australian companies and other relevant stakeholders. Capital markets are global, resulting in strong investor appetite for consistency and comparability across jurisdictions. At the same time, climate change is a global issue, requiring an international response to systemic risk. Internationally aligned climate reporting standards will facilitate the provision of comparable and consistent information about climate risks exposure at the company level.

ISSB Draft Standards represent minimum standards on which an Australian approach to mandatory climate reporting can be built. ISSB Draft Standards are consistent with existing requirements that apply to listed companies in Australia. ACSI, in conjunction with other institutional investors, sought a legal opinion on whether the requirements in the ISSB Draft Standards in relation to forward-looking statements present heightened liability risks to company directors. As part of answering this question, the Hartford Davis and Dyon Legal Opinion ('the Legal Opinion'), provided in full in Attachment 2, compared the ISSB Draft Standards to existing obligations for listed companies in Australia. The Legal Opinion found that the ISSB Draft Standards are 'broadly consistent with existing requirements that apply to listed companies in Australia, and requires disclosure of things which company directors should already be considering in the proper discharge of their duties as directors.' Adopting the ISSB standards as base reporting requirements would also ensure that Australian reporting requirements align with international practice.

Timebound phased introduction of mandatory climate reporting

Large listed entities (ASX300), large unlisted entities and financial institutions with revenues of over $100 million, and entities already reporting to the National Greenhouse and Energy Reporting Scheme (NGERS) should be the first group to be subject to mandatory requirements, with reporting to begin in 2024-25 financial year. At the end of the transition period, mandatory climate reporting should apply economy-wide. While ACSI research indicates that just over half (103) the ASX200 are making climate-related disclosures[1], we recognise that less mature market participants may require time to scale up their reporting capabilities. Consequently, we support a phased-in transition period for coverage of 2 to 3 years.

The design of mandated disclosures should focus on the outcomes of reporting, namely that users of the reporting are able to access easily understandable and credible information on an entities' exposure to climate change risks and opportunities. This requires the disclosure of both backward-looking data (scope 1, 2 and 3 emissions levels) and forward-looking information (such as an entity's strategy, risk management framework, metrics and targets). Reporting design should also acknowledge that there will be data gaps in the early years of disclosure. Large investors with diverse portfolios in particular rely on information sourced from their investees and this data is currently unavailable for many assets. There will be a time lag sourcing data as portfolio companies begin mandatory climate reporting in coming years. These challenges should be acknowledged and incorporated into disclosure design.

Starting the reporting period in 2024-25 will allow time for regulators to develop reporting guidance (e.g. scope 3 emissions, Australian specific scenarios), and for entities and service providers, including auditors, to develop the expertise required to meet expected demand. This length of transition period will ensure that Australia does not lag behind market practices, given that many markets have already introduced mandatory reporting. Any arrangements within this 2 to 3 year transition period should also encourage consistent improvement across the market, such that where companies have adopted current 'good practice' standards, they are encouraged to continue to progress.

[1] ACSI, 2022, [Promises, pathways and performance. Climate change disclosure in the ASX200](#).

Include Scope 3 emissions reporting requirements

Consistent with the ISSB approach, mandatory reporting should incorporate scope 3 emissions. There is growing consensus that scope 3 emissions represent significant market risk, with products and services that may be impacted by the transition to a low-carbon economy. In many cases, scope 3 emissions disclosure may require an entity to estimate or rely on members of its value chain to report their emissions correctly. While we agree there are challenges in reporting scope 3 emissions, ACSI research has shown that scope 3 reporting is becoming more common and improving in quality.[2] The challenges in scope 3 reporting should be managed through the appropriate disclosure of data gaps and the methodology used, and with updates as methodologies progress.

One concern around the disclosure of scope 3 emissions data is that a company may need to rely on disclosures by others. This issue was considered in the Legal Opinion ACSI and other institutional investors sought from Hartford Davis and Dyon. The Legal Opinion found that, '(g)enerally speaking, the company is permitted to rely on disclosures by others, and on the best available information. To use a suppliers' reported Scope 1 and 2 emissions as a basis for reporting a company's own Scope 3 emissions likely would furnish a reasonable basis, provided that there was not some reason to mistrust the reporting on emissions by others, and provided that it is accompanied by adequate disclosures regarding the reliability of the data or necessary proxies on which that information had been based.' In addition, the Government should work with industry in order to better define and address scope 3 reporting challenges over time. Part of this work should address and provide guidance on the challenges in defining clear value chain boundaries for scope 3 emissions.

Align with ISSB materiality definition

Applying materiality judgements to reporting requirements ensures that the information reported is comparable, decision-useful and that the reporting burden for reporting entities is reasonable and pragmatic.

ACSI supports the approach of the ISSB to materiality which now uses the IFRS Accounting Standard definition. We consider that the materially definition applied should be internationally aligned, to ensure reporting information and requirements are broadly similar, and investor focused. We caution against creating a false distinction between investors and the interests of other stakeholders. Over the long-term, where entities have effective and mutually beneficial relationships with their stakeholders, they are more likely to be successful. As noted by Justice Hayne in the Australian Financial Services Royal Commission, 'The longer the period of reference, the more likely it is that the interests of shareholders, customers, employees and all associated with any corporation will be seen as converging on the corporation's continued long-term financial advantage.'[3]

Guidance to support forward-looking statements

ACSI notes that disclosure of forward-looking information reflects existing practice of many companies,[4] both in respect of sustainability related information, but also in respect to financial information such as a provision or earnings guidance. The disclosure of forward-looking statements is also addressed through existing regulatory guidance, such as ASIC Regulatory Guidance 170 Prospective Financial Information which provides guidance on the use of prospective financial information in a disclosure document.

The Legal Opinion considered whether Australian company directors have heightened liability risks due of the requirement to establish reasonable grounds for any forward-looking statements. In summary, the Legal Opinion found that the legal requirement for forward-looking statements to be based on reasonable grounds, 'is capable of being sensitive to the inherent uncertainties in the scope, distribution, impacts and timing of the impacts of climate change.'[5] Nonetheless, we recognise that there is uncertainty in the market, which could be addressed by additional guidance on frameworks and strategies to support preparers. For example, further

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[2] ACSI, 2022, Promises, pathways and performance. Climate change disclosure in the ASX200.

[3] Justice Hayne in the Final Report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, February 2019 Volume 1 at page 403

[4] For example, Australian companies reporting against the TCFD include forward-looking statements.

[5] Hartford Davis and Dyon Legal Opinion

guidance on what constitutes reasonable grounds, and examples of fulsome disclosure.[6] Disclosure guidance should be formed through consultation with industry.

I trust our comments are of assistance. Please contact me, Kate Griffiths, Executive Manager – Policy and Research (kgriffiths@acsi.org.au), should you require any further information.

Yours faithfully

Louise Davidson AM
Chief Executive Officer
Australian Council of Superannuation Investors

[6] Section E of the Legal Opinion provides an indication of issues that could be covered in such guidance, to provide comfort to directors

Attachment One: Specific comments on Climate-related Financial Disclosure Consultation Paper

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?

The approach set out in the ISSB Draft Standards is consistent with existing requirements that apply to listed companies in Australia. In particular, a listed company in Australia is required by the *Corporations Act* to include in its directors' report information that shareholders would reasonably require to make an informed assessment of the entity's operations, financial position, business strategies and prospects for future financial years.[7] The ISSB Draft Standards 'requires disclosure of things which company directors should already be considering in the proper discharge of their duties as directors.'[8]

Relevant regulatory guidance effectively requires a company to disclose material business risks, which include environmental, social and governance (ESG) risks, where those risks could affect the entity's achievement of its financial performance or outcomes, taking into account the nature and business of the entity and its business strategy.[9] Therefore, listed companies effectively have an existing requirement to discuss material ESG risks in their annual disclosures, although there may be clearer ways of expressing this requirement directly in the Corporations Act. The ISSB Draft Standard provides further guidance on how to disclose these material ESG risks. Consequently, given the focus on material risks, adopting international practice on climate-financial risk disclosures should present an evolution for listed companies.

Good disclosure increases investor confidence and promotes open markets that can more accurately price risk and potentially lower the cost of capital, and arguably therefore can be expected to lower the cost of capital. The current lack of clarity and comparability in climate disclosures causes unnecessary expenditure by companies and investors in attempting to assess an entity's exposure to climate risks and opportunities. In addition, adoption of a global baseline will reduce the risk of market fragmentation and encourage those companies at the less mature end of the market to improve both their practices and disclosures, leading to more sustainable outcomes over the long-term.

Our view is that the costs of not adopting the global baseline outweighs the costs of adoption. Not adopting the Standards will create a disclosure gulf between Australian reporting and global best practice. As our members invest across global markets, there is strong investor appetite for consistency and comparability across disclosures. Substandard information on climate risks and opportunities in the Australian context will not only frustrate investors' ability to obtain decision-useful information, but it is also likely to create barriers to investment in low carbon emissions technologies. Competition for international capital will remain intense through the transition and every effort should be made to ensure consistent comparable disclosures are provided to the market.

Question 2: Should Australia adopt a phased approach to climate disclosure, with the first report for initially covered entities being financial year 2024-25? 2.1 What considerations should apply to determining the cohorts covered in subsequent phases of mandatory disclosure, and the timing of future phases?

ASX listed company climate-related disclosures are increasing. Around half of the ASX200 (103) align climate disclosure to the TCFD framework. There are examples of good practice within in the Australian market that provide a sound basis for the adoption of mandatory climate reporting.[10] However, the lack of a standardised approach to climate reporting means the quality of reporting varies widely across companies. While there is a strong need for improved consistency and clarity in reporting, the adoption of economy wide mandatory climate reporting will require a transition period to allow areas of the market that are less mature to scale up their reporting capabilities. In addition, sufficient time must be given to both finalise reporting standards (ISSB standards are due to be finalised in mid-2023) and allow organisations the time to integrate these requirements into their reporting arrangements. In particular, large investors with diverse portfolios will be relying on data from their investees, which will create a lag between the onset of reporting and the consolidation and aggregation of portfolio company emissions and investment data. This is discussed further in Question 13. The timing of the phased approach should seek to ensure that Australia does not fall further

[7] Corporations Act (Cth) 2001 section 299A (1)

[8] Hartford Davis and Dyon Legal Opinion

[9] ASIC Regulatory Guide 247 paragraphs 61-64

[10] For example, the 2022 ACSI report, Promises & Pathways. Climate reporting in July 2022, found that the majority of the ASX200 is partially or full reporting against the TCFD.

behind other jurisdictions that are more advanced in their implementation of mandatory climate reporting.

Accordingly, ACSI supports a 2 to 3 year transition period with reporting for the first phase of covered entities to start in the financial year 2024-25. At the same time, we recommend that any arrangements within this 2 to 3 year transition period encourage consistent improvement across the market, such that where companies have existing good practice, they are encouraged to continue to progress. This could be achieved through the development of best practice guidance that provides support for the next stage of reporting development. As part of this encouragement, Government should clearly flag the timeline in which mandatory reporting will be rolled out to encourage early adoption.

Ideally at the end of the 2 to 3 year transition period coverage of mandatory climate reporting will apply economy-wide. This will ensure that reporting captures economy-wide climate risks and opportunities. Extending this transition period would be out of step with international practice and limit the information investors require to assess market level risks caused by climate change.

ACSI acknowledges that some areas of reporting, such as scope 3 emissions, are likely to have data gaps or challenges at the commencement of reporting requirements. It may be appropriate to phase in disclosure requirements within the 2 to 3 year transition period. Phasing in of reporting requirements would need to be carefully considered. One option could be to allow the provision of incomplete data in identified topic areas, such as scope 3, in the first phase of reporting if the information is accompanied with a clear description of the data's limitations, the use of estimated data, and the underpinning methodologies and assumptions. For example, large investors with diverse portfolios will be dependent on the information provided by their investees. As data in the investment portfolio is aggregated over time, there will need to be consideration that some data will be missing or estimated in the early years of reporting. The 2 to 3 year transition period will also allow time for regulators to develop reporting guidance (e.g. scope 3 emissions, Australian specific scenarios). Any arrangements within this 2 to 3 year transition period should also encourage consistent improvement across the market, such that where companies have good practice, they are encouraged to continue to progress.

Question 3: To which entities should mandatory climate disclosures apply initially? 3.1 What size thresholds would be appropriate to determine a large, listed entity and a large financial institution, respectively? 3.2 Are there any other types of entities (that is, apart from large, listed entities and financial institutions) that should be included in the initial phase?

The introduction of mandatory climate reporting internationally has applied requirements to large entities in the first instance, with reference to revenues, number of employees, and/or assets under management (AUM). ACSI research has found that an increasing proportion of companies has started reporting on emissions reduction and setting net zero and emissions targets over time. The standard of reporting tends to improve as market capitalisation increases.[11]

Initial coverage should be targeted where it will apply to entities that have material exposure, or make a significant contribution, to systemic climate change risks. ACSI recommends that the following types of entities are captured in the first phase of coverage:

- **Large listed companies,** defined as members of the S&P/ASX 300. Incorporating large listed companies in the first phase of coverage aligns with international approaches to mandatory climate reporting. As noted above, over half of the ASX200 already disclose TCFD aligned reporting.
- **Large unlisted non-financial companies**, defined as companies with annual consolidated revenues of $100 million or more.
- **Large financial institutions**, defined as banking, superannuation, asset management and life insurance companies with either annual consolidated revenues of $100 million or more, or total Assets Under Management (AUM) of $5 billion or more. Setting threshold limits based on AUM aligns with the approaches taken in the UK and New Zealand.
- **Companies that already report to NGERS.** Incorporating companies that report to NGERS and are not captured in the first three categories of entity will ensure that the largest share of emissions is captured in the first stage of reporting. Companies reporting under NGERS will also have some existing expertise in reporting emissions.

Question 4: Should Australia seek to align our climate reporting requirements with the global baseline envisaged by the International Sustainability Boards? 4.1 Are there particular considerations that should apply in the Australian context regarding the ISSB implementation of disclosures relating to: governance, strategy,

[11] ACSI-Chasing-1.5C-PUBLIC-FINAL.pdf

risk management and/or metrics and targets? 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?

As outlined above, ACSI considers that adopting the ISSB standards would best serve Australia's economic competitiveness. Investment markets are global in nature and failure to adopt a global reporting baseline could see investment move offshore or be attracted to other markets.

ACSI considers that while the ISSB standards could be used for the base reporting requirements, there will be a need to develop guidance and further define requirements for an Australian context. One example is the provision of industry specific metrics that are published in separate volumes from the ISSB Climate-Related Disclosure Standard. The Australian Government has committed to the development of sector specific pathways to net zero in the Australian context.[12] These pathways should be used to set industry specific metrics in the Australian adoption of the ISSB Standard. Government and regulators should work with the market to develop standards, auditable data and scenarios for the disclosure of climate risks by Australian reporters. This would align the Australian approach with other jurisdictions that have provided additional guidance and/or requirements over and above the base standards outlined in the draft ISSB Standards. For example, the New Zealand arrangements provide extensive guidance on, and resources for, scenario analysis disclosures.[13] Developing similar guidance for Australian entities that take into account physical and transition risks specific to the Australian economy would assist entities when they are preparing their reporting. This is discussed further in Question 14.

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)?

ACSI considers that the first regulatory framework design option highlighted in the consultation paper that will 'incorporate the overarching obligations for climate disclosure (governance, strategy, risk management, targets and metrics) into legislation and build out the detail of those obligations through standards or guidance' is optimal. This design would both ensure the mandatory obligations are set out in legislation, and so support compliance by reporting entities. ACSI recommends that the detailed requirements are outlined in mandatory standards, as this aligns with the design of financial reporting requirements.

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?

Climate reporting requirements should be included in the annual report and integrated into the financials, whether by cross referencing or other methods. As one of the aims of the introduction of mandatory climate reporting is global comparability and integration with financial reporting, our view is that the disclosures should be presented in a manner that is efficient for preparers while also providing the information required by users including investors. The phasing in of assurance requirements should also be considered when deciding the location of climate reporting requirements. Temporary locations may be required as assurance requirements are ratcheted up over the transition period.

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)?

ACSI considers that the reference point for materiality should be internationally aligned, investor-focused, and considered over the short, medium and long-term. Materiality judgements allow entities to adopt an approach and disclose information that is proportionate to their particular circumstances and should apply across climate reporting requirements. It is important that the information provided is true and correct and reflects the goal of providing decision-useful information to assess the exposure of entities to Australia's transition to net zero, provide greater transparency that will improve information flows to investors and regulators in their management of risk, and have in place disclosure requirements that are proportional to the risks they represent.[14]

Accordingly, we support the adoption of the ISSB reference point for materiality. While the ISSB is developing guidance for the application of materiality, it uses the investor-focused definition used by the IFRS as a starting

[12] Annual Climate Change Statement 2022 (dcceew.gov.au)

[13] Resources » XRB

[14] Reform principles cited in The Treasury, Climate-related financial disclosure Consultation paper, December 2022, p.6.

point. Materiality is defined by the IFRS Accounting Standard as, 'information is material if omitting, misstating, or obscuring 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, which provide financial information about a specific reporting entity.'[15]

We note that the UK and New Zealand mandatory climate reporting frameworks have also aligned with the ISSB approach to materiality. It may also be appropriate for the Government to develop further guidance and examples of how to apply the concept of materiality in the context of climate-related disclosures.

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?

ACSI considers that, like reporting requirements, assurance should be phased in as the reporting market matures and be subject to a materiality assessment. The principle that any phasing-in arrangements encourage consistent improvement, should be maintained for assurance as well as reporting requirements. Many companies already have their existing disclosures assured (although the standard of assurance may vary), however development of capability across the market, including a shortage of people with the necessary skills, pose short-term issues.

The International Auditing and Assurance Standards Board (IAASB) has undertaken a project to develop an overarching standard for assurance on sustainability reporting. The project is expected to be completed in late 2024 or early 2025,[16] and could provide a framework to guide an expansion of assurance requirements over the 2 to 3 year transition period. ACSI recommends that any Australian approach to climate-related disclosures assurance is aligned with the IAASB Standard when complete.

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?

ACSI recognises the challenges involved with scope 3 reporting. We also note there is guidance available, including forthcoming guidance from the ISSB[17] and the Scope 3 Calculation Guidance from the Greenhouse Gas Protocol.[18] The ISSB will develop a framework for the measurement of scope 3 emissions that will 'require the use of reasonable and supportable information that is available without undue cost or effort and incorporates the use of estimation. Disclosures should be accompanied by information to enable investors to understand the basis for measurement of Scope 3 GHG emissions.'[19] There is a growing consensus that Scope 3 emissions represent significant market risk, with products and services that may be impacted by the transition to a low-carbon economy. In addition, scope 3 reporting is becoming more common, with improved quality. In this context, in 2022 ACSI found that 27 companies disclosed scope 3 targets and milestones across the ASX200 and 93 of the ASX200 reporting their Scope 3 emissions.[20]

Our view is that well-framed disclosure will acknowledge and detail the challenges and explain the methodologies used, to allow investors to understand and take into account measurement uncertainty. As explained in the Legal Opinion, the reasonable grounds legal requirement 'does not require the introduction of certainty where the subject-matter makes that impossible.' Rather if disclosures are accompanied by information outlining the assumptions, methodologies, estimations, and uncertainties underpinning that information, any assessment of reasonable grounds will take these uncertainties into account. Nonetheless, we acknowledge that a phasing in of the levels of data disclosure for Scope 3 emissions (ie. allowing data gaps in the first reporting period when accompanied by methodology, assumptions, and plans to improve data disclosure) may be appropriate here, particularly for entities at the smaller end of the market or with particularly complex financed emissions. Large investors with diverse portfolios, for example, will be incorporating data as it becomes available from their investees. This means that disclosures will need to be aggregated over time, with an increasing percentage of the portfolio covered in subsequent years of reporting.

The established reporting requirements for scope 1 and 2 emissions in the National Greenhouse and Energy Reporting Scheme could be a useful base template for designing reporting requirements for scope 1, 2 and 3 emissions by Australian entities, particularly entities who have not reported their emissions before. Extending NGERS reporting requirements to include scope 3 emissions, and aligning reporting obligations to mandatory

[15] IFRS, *International Accounting Standards* (IAS) 1.7

[16] Assurance on Sustainability Reporting | IFAC (iaasb.org)

[17] IFRS - ISSB announces guidance and reliefs to support Scope 3 GHG emission disclosures

[18] Scope 3 Calculation Guidance | Greenhouse Gas Protocol (ghgprotocol.org)

[19] IFRS - ISSB announces guidance and reliefs to support Scope 3 GHG emission disclosures

[20] ACSI, 2022, Promises, pathways and performance. Climate change disclosure in the ASX200.

climate disclosure timing, would provide both guidance for entities newly reporting and reduce duplication for entities covered by both the NGERS and mandatory climate reporting obligations. As noted in the IGGC submission to this consultation, it will also be important to ensure that emissions are reported on both an equity share and operational control basis. This will allow users of the reporting to both assess overall risk (equity share) and track performance (operational control).

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

A key goal of mandated climate reporting is comparability, which is currently missing in the climate reporting disclosed. Consequently, ACSI supports the production of a common baselines of metrics, including industry-specific measures, in order to ensure that there is a degree of consistency between disclosures. The ISSB work on industry metrics can be used as a template on which to develop Australian specific metrics and guidance.

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?

Investors are seeking credible, timely and comparable disclosures that will enable them to assess the adequacy of an entity's approach to climate risk and opportunity and progress achieved to date. Transition plan disclosures are critical to helping investors understand the steps companies are taking to transition to a net zero economy. Consequently, an Australian climate reporting standard should provide guidance around the management of transition risks and the development of transition plans. Further consultation with industry will be required to develop sector specific transition plans, such as guidance on transition plans for large investors with diverse portfolios. For example, the Glasgow Financial Alliance for Net Zero (GFANZ) separates guidance for transition plans between real-economy organisations and financial institutions.[21]

ACSI research[22] found that the information investors require to assess the adequacy of a transition plan, which is an extension of climate disclosure, includes data that supports the credibility, ambition and action underpinning any plan. Such information includes:

- How the plan addresses a companies' sector-appropriate material emissions.
- Short, medium and long-term decarbonisation targets that are Paris-aligned.
- A roadmap and long-term strategy for its resilience or transformation, including key levers and sector-specific leading indicators that the company can use to demonstrate progress and investors can use to assess it.
- Information outlining how decarbonisation and climate change is being integrated into corporate decision-making.
- Targets that can then be used to assess a company's progress against their transition plan over time. Targets may include decarbonisation targets, capital allocation, alignment with a company's net zero transition plan, and investment milestones.

Other relevant disclosures in transition plans that ACSI considers to be relevant in an assessment of a company's management of climate risks include:

- Integration of climate change factors into capital allocation frameworks.
- Alignment of company targets and strategy to 1.5°C outcomes.
- Investment in technology solutions (where required) and disclosure of research and development.
- Management of physical risk, including an assessment of exposure and resilience plans.
- Plans for an equitable transition where relevant.

There is also substantial international guidance available on key elements to be included in a transition plan. For example, the UK's Transition Plan Taskforce Disclosure Framework and Implementation guidance[23] provides a comprehensive guide to assist companies in the creation and disclosure of transition plans.

Disclosure on the use of offsets is also a key element in understanding a company's transition plan. There is currently limited public information provided on the use of offsets by Australian companies. The extent to

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[21] Glasgow Financial Alliance for Net Zero (gfanzero.com)

[22] ACSI, 2022, Promises, pathways and performance. Climate change disclosure in the ASX200.

[23] Transition Plan Taskforce | Setting a robust standard (transitiontaskforce.net)

which offsets support a company's emission reduction target is often unclear. Mandatory reporting should require companies to disclose the use of offsets in their transition plans. The Oxford Offsetting Principles, a widely accepted framework guiding the use of offsets, should be used to frame disclosures.[24] For example, disclosure should start from the principle that offsets should only be used when emissions cannot be avoided and explain why the company is using offsets.

In addition, data on the offsets themselves should be provided to allow an assessment on the credibility of the offsets used, including whether they actually represent a reduction in emissions. Data that can support an assessment of the credibility of offsets includes:

- Type of offset used (e.g., nature or technology based).
- Verification or certification scheme used.
- Does the offset represent carbon removal or avoidance.
- The level of additionality represented by the offset.
- The permanence of the offset.
- The robustness of the governance and accounting frameworks that manage the offsets.

Question 12: Should particular disclosure requirements and/or assurance of those requirements commence in different phases, and why?

Phasing in of particular disclosure requirements and/or assurance of those requirements may be appropriate in some circumstances, particularly for smaller entities scaling up their reporting capability and to allow the development of expertise by service providers. A phased-in approach to reporting requirements should be clearly timebound within a 2 to 3 year transition period. This approach would acknowledge there may be data gaps that may be addressed over the 2 to 3 year transition period or be the subject of consistent improvement across the market. Such an approach would not excuse poor data disclosure, but rather would allow the provision of incomplete data that was accompanied by clear references to the assumptions, methodologies, and uncertainties associated with that data and a plan for improving data provision in the future.

ACSI also considers that there should be a phased approach to assurance requirements, to allow service providers (e.g. auditors) to develop the expertise to meet a likely significant increase in demand. The implementation of mandatory climate reporting in other jurisdictions provides helpful templates for the phasing in of assurance. For example, the New Zealand approach is to limit assurance to emissions levels in the first year, with further assurance areas to be developed over the transition period.

Question 13: Are there any specific capability or data challenges in the Australian context that should be considered when implementing new requirements? 13.1 How and by whom might any data gaps be addressed? 13.2 Are there any specific initiatives in comparable jurisdictions that may assist users and preparers of this information in addressing these challenges?

ACSI's expertise is in large listed companies. Our research has found that management and disclosure of climate-related risks and opportunities has continued to improve, albeit at different rates. Challenges also remain, such as incomplete, unverifiable and incomparable information provided on scenario analysis and gaps in the quantification of physical risk.[25] We acknowledge that smaller entities may be less developed in their assessment of climate related risks and opportunities.

As discussed in Question 12, ACSI acknowledges that there will be data gaps at the commencement of any mandatory reporting requirements. For example, large financial institutions may have incomplete data at the start of mandatory reporting as they are sourcing information from the many entities in which they invest who have also not reported before. These would include public and private assets across the globe, many of which do not report any climate data. Disclosure should explain these challenges and gaps, estimation methods used, and how they are proposed to be addressed in future. ACSI would also recommend embedding in the reporting rules an ability to disclose retrospectively for the preceding financial year. A staggered approach to reporting would also allow disclosures to be aligned with other reporting obligations, such as the December release of the APRA Heatmap.

At the same time, it is important to recognise that data gaps should not justify poor disclosure. Reporting entities should be required to be transparent about the data used, its limitations, the level of uncertainty associated with the data, and any assumptions that have been made. This will both provide improve the

[24] The Oxford Offsetting Principles | Smith School of Enterprise and the Environment

[25] WEBSITE-VERSION-ACSI-Climate-Change-Disclosure-in-ASX200-designed-1.pdf

information available to investors and encourage improvement in reporting standards over time. Disclosures do not require certainty when there is none. Rather, the assumption of reasonable grounds will be assessed in the context of both the data and the assumptions, methodologies and uncertainties disclosed alongside the data.[26]

Consequently, ACSI recommends that the Government develop guidance that outlines what is a considered reasonable grounds for:

- statements made in disclosures; and
- the disclosure on the methodologies and assumptions that underpin those statements.

This guidance should reflect the needs of the users of disclosures and address data gaps (while they remain). For example, superannuation fund members may need a different approach to disclosure than institutional investors.

The New Zealand Government, for example, has released a range of resources for reporting entities at the same time as the Aotearoa New Zealand Climate Standards were released.[27] Government guidance will provide more certainty to in-scope companies on their obligations, particularly those at a less mature stage of reporting.

In addition, the Government should provide sector specific guidance for reporting that reflect the different disclosure needs and transition arrangements in individual sectors. For example, different approaches to reporting will be required for companies in the real economy compared to financial institutions.

Specific provisions should be considered to reflect the activities of superannuation funds. A key example where additional guidance will be required will be where the organisations in which funds invest (which in many circumstances will not be bound by Australian legislation) do not provide the information needed to comply with the Australian disclosure obligations. As part of this guidance, it should address the concept of reasonable grounds in the context of using data obtained by a third-party provider and reasonable estimation methods.

In addition, consideration should be given to interaction between other provisions applicable to superannuation funds. For example, the provision of regulation or guidance should be considered on the level of information that should be provided by funds in their reporting to satisfy retail members and their general right to information reasonably required to understand their interest in the fund. Regulation or guidance should make it clear that compliance with the desired climate related financial reporting should serve to provide comfort to funds on how a trustee can fulfil its duty to provide members with the information reasonably required to understand their interest in the fund.

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?

Scenario analysis is an important tool for understanding a company's resilience to low carbon scenarios by highlighting key potential risks and opportunities such as how the company might absorb impacts from changes in demand or address increased carbon costs. While increasing numbers of ASX200 companies are disclosing climate scenario analysis (88 in 2022 compared to 62 in 2021), the quality of those disclosures is variable. Less than half of the scenario analysis reporting entities in 2022 used a Paris-aligned 1.5° model and ACSI research also found that 105 different scenarios were used by ASX200 companies, making comparability a challenge.[28]

Varying levels of information provided in scenario analysis disclosures suggests that there is a role for the provision by Government of scenario analysis models that companies can use to test their resilience to low carbon scenarios. The provision of scenario analysis models would also assist entities that have not yet used scenario analysis to report on their climate risk by potentially resolving data challenges and associated costs.

ACSI recommends that Government develop a set of science-based, internationally aligned climate scenarios that have been adapted where necessary for the Australian environment. As noted in ACSI research,[29] key elements in climate scenario analysis include:

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[26] Hartford Davis and Dyon Legal Opinion

[27] Resources » XRB

[28] ACSI, 2022, Promises, pathways and performance. Climate change disclosure in the ASX200.

[29] ACSI, 2022, Promises, pathways and performance. Climate change disclosure in the ASX200.

- Disclosure against a 1.5°C scenario, including the underpinning assumptions.
- A mix of qualitative discussion and financial impact quantification.
- Quantification at a portfolio level, as well as at an asset specific level when a specific asset or operation is highly exposed to climate change risk. Where possible analysis should be done on core assets whilst also considering the opportunities presented by the transition to a net zero economy.
- Information on how cashflows could be impacted by demand and supply changes, abatement and carbon costs, and how these would affect specific projects and business divisions is useful to understanding the company's strategic risks.

Any reporting framework and regulatory should be clear that such scenarios are possible outcomes only, and not an endorsed trajectory. Reporters should be free to supplement with additional scenario analysis if they see fit. ACSI recognises that scenario analyses are stress tests, not a prediction of future events. Consequently, scenario analysis disclosures should be appropriately framed as such and accompanied by relevant context that explains the scenario analysis and purposes, so that disclosures are not confused with forward-looking predictions.

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?

The Legal Opinion (refer Attachment 2) provides assurance that the 'reasonable grounds' requirements and disclosures of uncertainties or assumptions in the context of climate reporting are suitable. . In summary, the Legal Opinion explains that:

- The ISSB Draft Standards 'require disclosure of material information about sustainability risks in a manner which is broadly consistent with existing requirements that apply to listed companies in Australia and requires disclosure of things which … company directors should already be considering in the proper discharge of their duties as directors. In this sense, although the ISSB Draft Standards increase the number and kinds of forward-facing matters that directors are required to disclose, for diligent company directors properly support by competent management, the ISSB Draft Standards should not increase directors' exposure.'
- 'The legal requirement to have a 'reasonable basis' for the making of forward-looking statements is capable of being sensitive to the inherent uncertainties in the scope, distribution, impacts and timing of the impacts of climate change. Directors must make a genuine assessment as to the appropriateness of the forward-looking disclosures at the time it is made, but they will not face liability merely because their assessment later turns out to be incorrect.' Therefore, for example, where methodologies are updated, or new information comes to light, liability concerns should be limited, so long as the statements were reasonable when made, and that updates are provided when the new information is known.

The Legal Opinion also addresses the issue of safe harbour, finding that:

- 'A specific 'safe harbour' aimed at climate and/or sustainability-related disclosures is not necessary or desirable.' A safe harbour would only undermine the beneficial effects of the ISSB Draft Standards, such as exposing bad practice, improving sub-standard practice and standardising the reporting and disclosure which accompanies good practice.
- There are a number of practical steps that can be taken to minimise liability concerns without resorting to the provision of a safe harbour, including:
    - Individuals and committees within the organisation and at board-level should be specifically tasked with governance responsibilities and with assembling information to provide directors with assurance that there is a reasonable basis for forward-looking statements,
    - Processes should be put in place to assess, measure and report on climate-related risks and opportunities on a continuous basis,
    - Disclosures of forward-looking climate-related information and scenario analysis of physical and transitional risks should be accompanied by a description of the assumptions and methodologies used to develop the information, as well as the time periods covered and risks that the predictions will not materialise.

ACSI notes that the release of the ISSB Draft Standards and this consultation on the introduction of mandatory climate reporting in Australia has raised questions in respect of forward-looking statements. The disclosure of forward-looking statements also reflects existing practice, as many Australian listed companies make and manage forward-looking statements in disclosures such as TCFD reports and other climate change-related reporting. Other forward-looking statements are widely made across the market, such as earnings estimates and for example, provisions in financial statements. Existing regulatory guidance makes it clear that preparers are unlikely to be found liable for misleading or deceptive forward-looking statements provided the statements are properly framed, they have a reasonable basis (which includes good governance at board level to sign off the statements) and there is ongoing compliance with disclosure obligations when circumstances change. Nonetheless, it is clear that there is a case for additional guidance which could provide comfort to preparers. Such guidance should cover the elements of systems and frameworks that support good practice and therefore limit liability, examples of what constitutes a reasonable basis and examples of disclosure of methodology, gaps and uncertainty.

In summary the disclosure of forward-looking statements reflects existing practice within the market and is already supported by the provision of regulatory guidance. Climate-related disclosures, such as that outlined in the ISSB Draft Standards, should not increase directors' exposure for diligent company directors properly supported by competent management. Consequently, reasonable grounds requirements and the disclosures of uncertainties or assumptions remains appropriate in the context of climate reporting. The provision of a safe harbour may only serve to undermine the expected benefits of mandatory climate reporting, such as improving sub-standard practice, nonetheless additional guidance may be useful.

Question 16: Are there particular considerations for how other reporting obligations (including continuous disclosure and fundraising documents) would interact with new climate reporting requirements and how should these interactions be addressed?

Other reporting requirements, such as the continuous disclosure regime, provide a framework to keep the market informed outside of periodic reporting cycles. In summary, where material information becomes known, an entity is required to notify the market. Continuous disclosure obligations support markets being well informed and priced accordingly. Where information changes, it is appropriate to update the market.

Many organisations manage these requirements already through internal systems and reporting of information to support compliance with continuous disclosure obligation. Climate related reporting requirements should be no different and integrated into entities' internal compliance systems. As with existing disclosures, information should be monitored, and where new information means that a disclosure requires updating, that disclosure can be updated or withdrawn. From a practical perspective the nature of climate-related disclosure means that annual review and update is likely to be sufficient, supplemented by disclosure of any material information that arises in the interim. This would mirror the approach to reporting of financial information, where assumptions are re-tested as part of the regular financial reporting process, with any information that arises in the interim disclosed where it is material. Companies already reporting under the TCFD have integrated this into their existing internal compliance systems.

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?

Climate-related reporting disclosure is the first in a series of planned ISSB Standards. The ISSB are also preparing to release disclosure standards on topics such as Nature and Biodiversity, which is intrinsically linked to climate and is already under consideration by many investors. Incorporating these sustainability standards into Australia's mandatory reporting requirements in time will provide investors with more decision-useful information as well as align Australia with global practice.

Consequently, it will be important to create a flexible rule design to support international alignment by allowing for the introduction of further sustainability standards as they develop.

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

No comment

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?

ACSI does not have a position on which of the three options is optimal. When designing the financial reporting system, it is important that the body that has carriage of the reporting standards:

- Has sufficient resourcing to undertake the development of the climate and sustainability standards.

- Is required, and has the capability and capacity, to incorporate industry views – including the views of investors as the users of these statements - in the development of those standards.
- Has sufficient expertise in sustainability issues. ACSI notes that sustainability covers a number of areas of expertise ranging from climate change to human rights. As additional sustainability standards are developed, it will be important to ensure that the responsible body contains, or is able to access, a range of expertise across sustainability topics.
- Is an independent body.

Attachment Two: Legal Opinion

Refer separate PDF file sent with this submission.