Submission to Treasury on climate-related financial disclosure

17 February 2023

About EDO

EDO is a community legal centre specialising in public interest environmental law. We help people who want to protect the environment through law. Our reputation is built on:

Successful environmental outcomes using the law. With over 30 years' experience in environmental law, EDO has a proven track record in achieving positive environmental outcomes for the community.

Broad environmental expertise. EDO is the acknowledged expert when it comes to the law and how it applies to the environment. We help the community to solve environmental issues by providing legal and scientific advice, community legal education and proposals for better laws.

Independent and accessible services. As a non-government and not-for-profit legal centre, our services are provided without fear or favour. Anyone can contact us to get free initial legal advice about an environmental problem, with many of our services targeted at rural and regional communities.

Environmental Defenders Office is a legal centre dedicated to protecting the environment.

Submitted to: climatereportingconsultation@treasury.gov.au

For further information on this submission, please contact:

Kirsty Ruddock
Managing Lawyer
Safe Climate (Corporate and Commercial)
T: 02 9262 6989
E: kirsty.ruddock@edo.org.au;

Zoe Bush
Senior Solicitor
Safe Climate (Corporate and Commercial)
T: 02 9262 6989
E: zoe.bush@edo.org.au

EXECUTIVE SUMMARY

The Environmental Defenders Office (**EDO**) welcomes the opportunity to comment on Treasury's Consultation Paper on climate-related financial disclosure.

It is critical that alignment with the 1.5°C temperature goal of the Paris Agreement and Australia's legislated net zero emissions by 2050 target[1] is central to the design of a mandatory climate-related disclosure framework. Australia needs to be at the forefront of addressing climate change. The State of Environment Report 2021 found that climate change is profoundly affecting our environment and society with land and ocean temperatures increasing and rainfall patterns changing.[2] According to the State of Environment report, Australia has already warmed by 1.4C and is suffering significant losses from accelerating climate change.[3] Extreme weather events such as bushfires, floods, heatwaves and droughts are occurring more often and becoming more severe.[4]

As part of a national community legal centre specialising in public interest environmental law, the work of the EDO Safe Climate (Corporate and Commercial) lawyers includes highlighting cases where an organisation's net zero or emissions reduction plans contradict the organisation's actual business practices. We are concerned by the prevalence of transition plans that are not aligned with the scientific consensus of what is required to achieve the Paris Agreement's 1.5°C temperature goal, and consider this is a key deficiency that the mandatory climate-related disclosure framework should seek to rectify.

We set out **below** a summary of our key recommendations and detailed responses to the questions identified in the Consultation Paper.

KEY RECOMMENDATIONS

Recommendation 1 – The EDO recommends the adoption of the ISSB's draft standards for climate-related disclosures as a baseline that should be supplemented by:

- (a) the inclusion of "double materiality" as adopted by the EU in December 2022 (see Question 7 below);
- (b) a requirement that entities disclose their emissions on an equity basis, to improve the consistency and comparability of emissions disclosures (see Question 10 below); and
- (c) a requirement that entities use climate-related scenario analysis and pathways consistent with limiting warming to 1.5°C and disclose transition plans aligned with the Science Based Target Initiative's Corporate Net Zero Standard and findings of the UN's High-Level Expert Working Group on Net Zero Emissions Commitments of Non-State Entities (see Question 11 below).

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[1] *Climate Change Act 2022* (Cth) s 10(1)(b).
[2] Australian Government, *State of the Environment Report 2021* available at: https://soe.dcceew.gov.au/climate/introduction
[3] Australian Government, *State of the Environment Report 2021* available at: https://soe.dcceew.gov.au/climate/key-findings
[4] Climate Council of Australia Limited, *Power Up: Ten Climate Gamechangers (*2022) p 4 available at: https://www.climatecouncil.org.au/wp-content/uploads/2022/09/CC_MVSA0319-CC-Report-Power-Up-Ten-Energy-Game-Changers_V9-FA-Low_Res_Single-Screen.pdf

Recommendation 2 – The EDO strongly opposes the adoption of the US 'safe harbour' provisions in relation to entities' climate-related disclosures. The 'reasonable grounds' requirements are sufficiently flexible to accommodate any uncertainties or assumptions that may be inherent to certain aspects of climate-related disclosures, such as transition plans. The adoption of other tests or standards would introduce inconsistencies with well-established statutory norms. The EDO considers there is no principled reason for forward-looking statements to be subject to different statutory norms merely by virtue of being climate-related (see Question 15 below).

Recommendation 3 – The EDO recommends that *all* listed entities, large financial institutions, large entities that are neither publicly listed nor considered financial institutions, and government-owned corporations be included in the first phase of mandatory climate-related disclosures. The determination of these thresholds and subsequent phases should prioritise the inclusion of entities that are particularly exposed to climate-related risks and/or have a significant impact on the climate. We *oppose* the phasing of particular disclosure and/or assurance requirements (see Questions 2, 3 and 12 below).

Recommendation 4 – The EDO recommends the adoption of the first regulatory framework proposal in the Consultation Paper. That is, incorporating overarching obligations into legislation and detailing these obligations in regulatory guidance and standards (see Question 5 below).

Recommendation 5 – The EDO recommends that the 'two strikes' rule for listed entities' executive remuneration reports be extended to climate-related disclosures as an important accountability mechanism for shareholders concerned about directors' continued mismanagement of climate-related risks (see Question 5 below).

Recommendation 6 – The EDO recommends that, where climate-related risks and opportunities are *material*, entities be required to disclose them in accordance with their periodic reporting and continuous disclosure obligations, as they would any other material information. To the extent disclosures above and beyond these obligations are required, such as in relation to greenhouse gas emissions and transition plans, these should be contained in a separate report released on an annual basis (see Questions 6 and 16 below).

Recommendation 7 – The EDO recommends that assurance requirements be extended to greenhouse gas emission disclosures, as will be the case in New Zealand, in order to address concerns of significant underreporting in some sectors (see Question 8 below).

Recommendation 8 – The EDO recommends the adoption of the first potential structure in the Consultation Paper. That is, confirming the AASB as the entity responsible for developing, making, and monitoring climate- and sustainability-related disclosures (see Question 19 below).

DETAILED RESPONSES TO DISCUSSION PAPER QUESTIONS

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)?

The ISSB's Exposure Drafts of IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information (**Draft IFRS S1**) and IFRS S2 Climate-related Disclosures (**Draft IFRS S2**) (collectively, the **ISSB Draft Standards**) provide a comprehensive global baseline of sustainability-related disclosures, building on earlier work of the Task Force on Climate-related Financial Disclosures (**TCFD**) and other industry-based disclosure requirements. The issuance of the ISSB Draft Standards was prompted by users of general financial reporting expressing an 'urgent need for disclosure standards on climate change'[5] and a request from G20 leaders and the International Organisation of Securities Commissions, who are the peak body of corporate regulators worldwide.

Currently, Australia's regulatory response to these international disclosure standards has been the issuance by financial regulators of guidance that climate-related financial risks must be disclosed as part of existing obligations to disclose material risks, and a recommendation that this be done in accordance with the TCFD.[6]

In contrast, the United Kingdom (**UK**),[7] European Union (**EU**),[8] United States (**US**),[9] New Zealand,[10] Switzerland,[11] Hong Kong,[12] and Japan[13] have introduced, or are contemplating, mandatory climate-disclosure requirements that broadly align with the TCFD.

As at 2022, only 103 companies on the ASX200 were fully or partially aligned with the TCFD framework.[14] The introduction of mandatory climate-related disclosure requirements that align with the TCFD or ISSB Draft Standards would therefore inevitably require some resources

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[5] IFRS, *[Draft] IFRS S2 Climate-related Disclosures* (March 2022) pp 5-7.

[6] ASIC, *Regulatory Guide 247: Effective disclosure in an operating and financial review* (August 2019) pp 19-20; ASIC, *Report 593: Climate risk disclosure by Australia's listed companies* (September 2018); ASX Corporate Governance Council, *Corporate Governance Principles and Recommendations* (Fourth Edition, February 2019) Recommendation 7.4; AASB 101; AASB, *Climate-related and other emerging risk disclosures: assessing financial statement materiality using AASB Practice Statement 2* (December 2018).

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

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

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

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

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

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

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

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

expenditure by Australian entities, given their disparity with existing Australian climate-related reporting practices.

Further, Australian entities and officers may also be concerned that more onerous climate-related disclosure requirements will heighten their exposure to liability risks. The EDO agrees with the views recently expressed by Sebastian Hartford Davis in advice to the Australian Council of Superannuation Investors that while the ISSB Draft Standards would increase the *amount* of required climate-related disclosures, this should not create "heightened risk" for entities, as the ISSB Draft Standards are "*broadly* consistent with existing requirements that apply to listed companies in Australia, and requires disclosure of things which in our opinion company directors should *already* be considering in the proper discharge of their duties as directors".[15]

The EDO considers any potential costs of aligning with international climate reporting practice are significantly outweighed by the benefits, which include the following:

(a) Accelerating a timely and effective response to climate change by facilitating the reallocation of capital away from carbon-intensive businesses, and ensuring accountability for inadequate management of climate-related risks, impacts and opportunities. This will in turn help Australia fulfil its obligations under the Paris Agreement and achieve its net zero emissions by 2050 target.[16]

(b) Ensuring Australian companies fully understand, and are adequately prepared to navigate, the risks and opportunities presented by the energy transition. Many Australian companies are acutely exposed to climate-related risks, with the ASX50 being the most exposed major stock exchange in the world to stranded asset risks.[17] Already, 46% of companies are experiencing resource scarcity or increased cost of resources due to climate change, and 45% are experiencing changed demand for their products.[18]

(c) Minimising the risk of investors being exposed to major losses by providing them with more consistent, complete, comparable and verifiable information, to help them assess how climate-related matters and the associated risks and opportunities affect:
    i. a company's financial position and financial performance;
    ii. an amount, timing and certainty of a company's future cash flows over the short, medium and long term and, therefore, the assessment of enterprise value by users of general purpose financial reporting; and
    iii. a company's strategy and business model.[19]

(d) Providing investors with comparable information for international markets. This enables investors to assess entities' exposure to, and management of, climate-related risks and opportunities, across markets, to facilitate capital allocation and stewardship decisions.[20]

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[15] S.H. Hartford Davis and K. Dyon, *Advice regarding potential liability of directors under the ISSB draft standards for forward looking statements*(16 December 2022) (**Directors' liability advice**) available at: [Microsoft Word - Advice on ISSB Draft Standards (Final).docx (igcc.org.au)]

[16] *Climate Change Act 2022* (Cth) s 10(1)(b).

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

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

[19] IFRS, *[Draft] IFRS S2 Climate-related Disclosures* (March 2022) p 5.

[20] IFRS, *[Draft] IFRS S2 Climate-related Disclosures* (March 2022) p 5.

(e) Minimising the risk of markets being unfairly skewed in favour of companies failing to adequately disclose their climate-related risks, and unfairly away from companies that are acting responsibly.
(f) Ensuring Australian companies have sufficient certainty regarding their climate-related disclosure obligations.
(g) Facilitating Australia's integration into international markets.

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 converse of the costs and benefits identified in response to Question 1 above.

Failing to align with global baseline standards risks making Australia a 'laggard' and impairing Australian entities' ability to participate in global markets and attract international investment.

These costs are compounded by the costs of a delayed and inadequate response to climate change. Under a high emissions scenario, the costs of more frequent and severe events such as bushfires, storms and floods, as well as rising sea levels, could rise to $94 billion per year by 2060 and $129 billion by 2100.[21] The administrative costs of disclosure requirements are minimal in comparison. It is also likely that jurisdictions with more stringent requirements, such as the EU, may impose climate tariffs on Australia's economy if it does not adhere to international practice.[22]

<u>Question 2</u>: Should Australia adopt a phased approach to climate disclosure, with the first report for initially covered entities being financial year 2024-25?

The EDO does not oppose a phased approach in relation to the entities covered by mandatory climate-related disclosures. As detailed in response to Question 12 below, the EDO *does* oppose a phased approach in relation to particular disclosure and/or assurance requirements.

2.1 What considerations should apply to determining the cohorts covered in subsequent phases of mandatory disclosure, and the timing of future phases?

The 2021 Sixth Assessment Report of the Intergovernmental Panel on Climate Change (**IPCC**) underlines the urgency with which action to reduce emissions is required in order to limit warming to the Paris Agreement's temperature goal of 1.5°C.[23] As discussed in response to Question 1 above, mandatory climate-related disclosures will help facilitate these emissions reductions by: (1) facilitating the timely reallocation of capital away from carbon-intensive businesses; and (2) ensuring accountability for inadequate management of climate-related risks, impacts and opportunities.

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[21] Climate Council of Australia Ltd. *Markets are Moving: The Economic Costs of Australia's Climate Inactio*n (2021) available at: https://www.climatecouncil.org.au/wp-content/uploads/2021/10/Markets-Are-Moving_V5-FA_High_Res_Single_Pages.pdf
[22] Climate Council of Australia Ltd. *Markets are Moving: The Economic Costs of Australia's Climate Inactio*n (2021) available at: https://www.climatecouncil.org.au/resources/markets-moving-economic-costs-australias-climate-inaction/
[23] IPCC, 'Summary for Policymakers' in *Climate Change 2021: The Physical Science Basis. Contribution of Working Group I to the Sixth Assessment Report of the IPCC* (2021) Figure SPM.4, SSP1-1.9.

The determination of cohorts and timing should achieve the appropriate balance between this urgency and the "urgent need" for climate-related disclosure standards expressed by investors and other stakeholders and acknowledged by the ISSB,[24] on the one hand, and ensuring that entities with less resources are afforded sufficient time to develop robust systems and processes to comply with climate-related disclosure requirements, on the other.

The EDO considers this is best achieved by prioritising the inclusion of entities that are particularly exposed to climate-related risks and/or have a significant impact on the climate in the initial phases of mandatory disclosure, with some consideration of their market capitalisation, which will indicate an entity's ability to absorb additional compliance costs.

Question 3: To which entities should mandatory climate disclosures apply initially?

EDO **recommends** that mandatory climate-related disclosure requirements should initially apply to all listed entities, as in the US. These entities have been on notice of the need to consider, disclose and respond to climate-related risks since at least the seminal opinion of Noel Hutley SC and Sebastian Hartford Davis on directors' climate-related obligations in 2016.[25] This was followed by Australian regulators issuing guidance requiring the disclosure of material climate-related risks in 2018, and recommending the use of the TCFD.[26] Indeed, Australian listed entities have demonstrated their ability to quickly adapt to new climate-related disclosure regimes. Only 11 listed entities used the TCFD framework when it was first introduced in 2017.[27] As at 2022, 103 listed entities were partially or fully aligned with the TCFD.[28]

Large financial institutions and large entities that are neither publicly listed nor considered financial institutions should also be included in the first phase. It is important that the latter category of entities is included so that investors, consumers and other stakeholders are provided with decision-useful information regarding their climate-related risks, impacts and opportunities.

Large entities' preparedness for climate-related disclosure requirements is furthered by the mandatory climate-related disclosure regimes already in place in other jurisdictions, such as the UK and EU. Large entities with a presence in these jurisdictions would already be familiar with climate-related disclosure requirements and have systems and processes in place to comply with them.

EDO **recommends** that disclosure requirements should also initially apply to all government-owned corporations. For example, Snowy Hydro Limited is a Commonwealth-owned corporation involved in energy production. It is therefore exposed to material climate-related risks, such as

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[24] Draft IFRS S2, p 7.
[25] N. Hutley and S.H. Hartford Davis, *Climate Change and Directors' Duties: Further Supplementary Memorandum of Opinion* (23 April 2021) available at: https://cpd.org.au/2021/04/directors-duties-2021/
[26] ASIC, *Regulatory Guide 247: Effective disclosure in an operating and financial review* (August 2019); ASIC, *Report 593: Climate risk disclosure by Australia's listed companies* (September 2018); ASX Corporate Governance Council, *Corporate Governance Principles and Recommendations* (Fourth Edition, February 2019).
[27] Australian Council of Superannuation Investors, *Promises, pathways & performance: Climate change disclosure in the ASX200* (July 2022) p 6.
[28] Australian Council of Superannuation Investors, *Promises, pathways & performance: Climate change disclosure in the ASX200* (July 2022) p 6.

changed demand for its products, and has a material impact on the climate. Similarly, most State-owned forestry corporations contribute to the clearing of vegetation and should likewise have to disclose climate-related risks and impacts.

3.1 What size thresholds would be appropriate to determine a large, listed entity and a large financial institution, respectively?

The EDO does not support the staged introduction of climate-related disclosures in relation to listed entities for the reasons given in response to Question 3 above.

The EDO does not have a view on the particular size thresholds that should apply to financial institutions or other entities, but considers the determination of these thresholds should prioritise the inclusion of entities that are particularly exposed to climate-related risks and/or have a significant impact on the climate.

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?

See our response to Question 3 above. The EDO does not support the staged introduction of climate disclosures in relation to listed entities.

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

Yes. The ISSB Draft Standards are designed to be a global baseline that builds on the earlier work and learnings of the TCFD, which will improve the consistency, transparency, and comparability of climate-related disclosures. Derogation from this baseline would risk making Australia a 'laggard' and impede our integration into international markets.

We note that many Australian regulatory authorities such as the Australian Securities and Investments Commission (**ASIC**), Reserve Bank of Australia, Australian Prudential Regulatory Authority (**APRA**), the Australian Accounting Standards Board (**AASB**) and Auditing and Assurance Standards Board (**AUASB**) support the development of international standards through the ISSB and have been active in their development.[29]

The baseline requirements of the ISSB Draft Standards should be supplemented by the additional requirements outlined in response to Questions 9, 10 and 11 below to ensure Australia's climate-related disclosure regime adequately supports Australia's transition to net zero emissions by 2050, provides investors with useful and comparable disclosures, and aligns with international standards regarding net zero emission targets.

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[29] See https://asic.gov.au/about-asic/news-centre/find-a-media-release/2022-releases/22-161mr-asic-encourages-submissions-to-the-international-sustainability-standards-board-consultation-on-global-baseline-climate-and-sustainability-disclosures/ and Submission by AASB and AUSASB dated 28 July 2022 available at: https://aasb.gov.au/media/gjpbg5xr/issb_submission_ifrs_s1_and_s2a.

In addition to the benefits mentioned in response to Question 1 above, the following specific requirements of the ISSB Draft Standards would help remedy existing deficiencies in Australian entities' climate-related disclosures:

(a) Paragraphs 5(f) and 21(g) of the ISSB Draft Standards require entities to disclose, amongst other things, whether and how **climate-related performance metrics are included in remuneration policies.** The EDO considers this requirement would be helpful given that, as at 2022, 72% of ASX200 companies did not disclose how executive remuneration was linked with climate-related metrics.[30]

(b) Paragraph 13 of the ISSB Draft Standards requires entities to disclose how they **plan to achieve any climate-related targets**. As at 2022, 49% of ASX200 companies had net zero emissions targets,[31] which accounts for approximately 70% of the ASX200's collective market capitalisation.[32] However, only 55% of these companies disclose a reasonable level of detail on a plan to achieve these targets.[33] A lack of transparency about how entities intend to achieve climate-related targets limits investors' and other stakeholders' ability to assess the credibility of these targets and make informed financial decisions.

(c) In particular, paragraph 13(b)(iii) requires entities to disclose **the extent to which targets rely on the use of offsets**, whether those offsets will be verified by a third -party, the type(s) of offsets being used, and any other significant factors necessary for users to understand the credibility and integrity of offsets. The EDO considers this requirement helpful given Australian entities' heavy reliance on offsets to achieve climate-related targets, and investors' increasing concerns regarding their credibility. For example, in ongoing proceedings in the Federal Court, the Australasian Centre for Corporate Responsibility alleges that Santos misled investors when it said it had a 'clear' and 'credible' plan to achieve net zero emissions, in part because it failed to disclose the extent to which portions of the plan relied on offsets. However, as discussed in response to Question 11 below, the EDO considers it necessary that this requirement go further and prohibit the use of offsets to achieve entities' climate-related targets in order to be consistent with the Science Based Target Initiative's (**SBTi**) Corporate Net Zero Standard and the recent report of the UN's High-Level Expert Working Group on Net Zero Emissions Commitments of Non-State Entities (**UN Expert Group**).

(d) Paragraph 14 of the ISSB Draft Standards requires entities to disclose the **anticipated effects of climate-related risks on their financial position, financial performance and cash flows over the short, medium and long term**, and that they disclose quantitative information unless they are unable to do so. Existing regulatory guidance requires listed companies to disclose material climate-related risks in their financial statements[34] and corporate governance statements,[35] and discuss in their operating and financial reviews

[30] PWC, *ESG Reporting in Australia* (2022) p 10.
[31] PWC, *ESG Reporting in Australia* (2022) pp 5, 7.
[32] Australian Council of Superannuation Investors, *Promises, pathways & performance: Climate change disclosure in the ASX200* (July 2022) p 5.
[33] PWC, *ESG Reporting in Australia* (2022) pp 5, 7.
[34] AASB, *Climate-related and other emerging risks disclosures: assessing financial statement materiality using AASB Practice Statement 2* (December 2018).
[35] ASX Corporate Governance Council, *Corporate Governance Principles and Recommendations* (Fourth Edition, February 2019) Recommendation 7.4.

how material climate-related risks may impact financial performance and outcomes.[36] However, as at 2022, only 18% of ASX200 companies disclose how their financial position may change over time because of climate--related risks and opportunities.[37] According to the Australian Council of Superannuation Investors, the lack of quantification as to how the energy transition will impact a company's financial position and performance is a regular complaint of investors.[38]

(e) Paragraph 15 of the ISSB Draft Standards requires entities to use **climate-related scenario analysis to assess their climate resilience**, and to state whether, among those scenarios, they have used a scenario aligned with the latest international agreement on climate change. As at 2022, 88% of ASX200 companies use climate scenario analysis.[39] However, according to a report by the Australian Council of Superannuation Investors, the quality of these disclosures is highly variable.[40] The EDO is aware of multiple examples of Australian entities cherry-picking and/or using outdated climate scenarios that are inconsistent with the Paris Agreement's temperature goals in order to over-state their climate resilience. For example, the CEO of New Hope Coal Ltd (**NHC**) stated at its 2020 AGM that 'coal will remain a significant part of the energy mix' under the IEA's current policies scenario (projected to generate warming of 6°C by 2100)[41] and stated policies scenario (projected to generate warming of 2.6°C by 2100)[42]. He omitted that coal demand would dramatically decrease under the IEA's two Paris-aligned scenarios that existed at the time. Under the then net zero by 2050 scenario, coal demand would decrease 60% from 2019 to 2030.[43] It would have assisted investors if NHC had been required to disclose that the two scenarios it relied on were not aligned with the Paris Agreement. However, this requirement alone would not have provided investors with the information necessary to understand how an energy transition aligned with the Paris Agreement would affect demand for NHC's primary product. As such, in addition to the reasons discussed in response to Question 11 below, the EDO considers it necessary that this requirement go further and require that entities use a climate scenario aligned with limiting warming to 1.5°C.

(f) In particular, paragraph 15(a)(iii)(2) of the ISSB Draft Standards requires entities to disclose their **ability to redeploy, repurpose, upgrade or decommission existing assets**. This requirement is particularly important in Australia, given the ASXS50 is the most exposed major stock exchange in the world to stranded asset risks.[44] As at 2022, 83% of ASX200 companies did not disclose the amount and percentage of their assets or business activities vulnerable to physical climate-related risks, and 88% did not disclose the same

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[36] ASIC, *Regulatory Guide 247: Effective disclosure in an operating and financial review* (August 2019) RG247.61-RG247.66.
[37] PWC, *ESG Reporting in Australia* (2022) p 5.
[38] Australian Council of Superannuation Investors, *Promises, pathways & performance: Climate change disclosure in the ASX200* (July 2022) p 28.
[39] Australian Council of Superannuation Investors, *Promises, pathways & performance: Climate change disclosure in the ASX200* (July 2022) p 6.
[40] Australian Council of Superannuation Investors, *Promises, pathways & performance: Climate change disclosure in the ASX200* (July 2022) p 6.
[41] TCFD, *Technical Supplement: The Use of Scenario Analysis in Disclosure of Climate-Related Risks and Opportunities* (June 2017) p 17.
[42] IEA, *Scenario trajectories and temperature outcomes* (2021) available at: https://www.iea.org/reports/world-energy-outlook-2021/scenario-trajectories-and-temperature-outcomes>.
[43] IEA, *2020 World Energy Outlook* (13 October 2020) 123.
[44] S & P Dow Jones Indices, *The Carbon Scorecard* (May 2017).

regarding transition climate-related risks.[45] For example, in its 2021 Annual Report,[46] Origin Energy Ltd disclosed that lower demand for fossil fuels could result in the "potential for stranded assets" but without disclosing how that risk will be managed in specific terms. To the extent that Origin did disclose how it intends to manage the risk of stranded assets, it was expressed in general terms as "focussing on offering low-carbon solutions" and "accelerating growth in renewables and cleaner energy." Requiring entities to disclose in terms similar to the requirements set out in paragraph 15(a)(iii)(2) would ensure that investors are provided with sufficient information to determine the risk associated with stranded assets.

(g) Paragraph 21(a)(i) and (ii) of the ISSB Draft Standards requires entities to **disclose their emissions in CO2 equivalent (CO2e)**. That means entities' emissions disclosure must take into account all greenhouse gas emissions, rather than just CO2. This is important given the substantial contribution of other greenhouse gas emissions to global warming. For example, methane emissions are the second-largest contributor to anthropogenic climate change, having contributed to warming of 0.6°C between 1750 and 2019.[47] For example, Vintage Energy Ltd, an ASX-listed company with gas exploration assets in Australia, purports to report in accordance with the TCFD, but does not disclose its greenhouse gas emissions at all, let alone in CO2e. 48

(h) Paragraph 21(a)(i)(3) and (iv) of the ISSB Draft Standards requires entities to **disclose their upstream and downstream Scope 3 emissions**. As at 2022, only 49% of ASX200 companies disclosed some Scope 3 emissions, and only 14% disclosed all Scope 3 emissions.[48] Scope 3 emissions disclosures are critical for investors and other stakeholders to be able to assess the risks in a covered entity's value chain, for example, the covered entity's financed emissions.

(i) Paragraph 21(f) of the ISSB Draft Standards requires entities to **disclose the internal carbon price they use to assess the costs of their emissions**, and explain how they apply the carbon price in decision making. As at 2022, 72% of ASX200 companies did not disclose their use of an internal carbon price.[49] Further, entities that do disclose an internal carbon price may not be sufficiently transparent abouts its application. For example, in July 2020, Woodside Ltd announced that it was doubling its internal carbon price from US$40 a tonne to US$80 a tonne,[50] and has regularly trumpeted this claim since. However, small footnotes clarify that Woodside only applies this carbon price to 'Australian emissions that exceed facility-specific baselines in accordance with Australian regulations'.[51] Facility-specific baselines are very rarely exceeded given facility baselines under the safeguard mechanism are almost always above the level of emissions expected from a facility. The effect is that Woodside is applying its carbon price to a near zero volume of emissions. Unless investors read these small footnotes and understood the operation of the safeguard mechanism, they may have been misled into believing that returns from Woodside projects included a carbon price.

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[45] PWC, *ESG Reporting in Australia* (2022) p 10.

[46] Origin Energy, *2022 Annual Report* (June 2022) (**2022 Annual Report**) p 45-46.

[47] Intergovernmental Panel on Climate Change, *Climate Change 2021: The Physical Science Basis. Contribution of Working Group I to the Sixth Assessment Report of the Intergovernmental Panel on Climate Change* (2021) Chapter 6.

[48] PWC, *ESG Reporting in Australia* (2022) p 14.

[49] PWC, *ESG Reporting in Australia* (2022) p 10.

[50] ASX Announcement, *Asset Value Review and Other Items* (14 July 2020) p 3.

[51] See, for example, ASX Announcement, *Asset Value Review and Other Items* (14 July 2020) fn 4.

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

As detailed in response to Question 11 below, EDO **recommends** that the implementation of the ISSB Draft Standards be consistent with Australia's international and statutory climate-related commitments.

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)?

Australia's climate reporting framework should achieve the appropriate balance between covered entities' need for certainty regarding their disclosure obligations, and flexibility to accommodate the rapidly evolving regulatory and market landscape prompted by the energy transition. It is important that the framework includes sufficient enforcement mechanisms for interested persons, and that it is consistent with Australia's international and statutory climate-related commitments (see our response to Question 11 below) and international practice on climate-related disclosures.

The EDO considers this balance is best achieved by the first regulatory framework proposal in the Consultation Paper. Incorporating overarching obligations into legislation would help rectify the current fragmentation of climate reporting expectations in Australia, and improve their accessibility. The details of those obligations being contained in regulatory standards and guidance allows them to readily adapt to subsequent developments, such as the recommendations of the Taskforce on Nature-related Financial Disclosures, which are currently under development. Of the frameworks currently available, the EDO considers that the adoption of the ISSB Draft Standards would best provide covered entities with sufficient certainty regarding their minimum disclosure obligations (see our response to Question 10 below).

The new regulatory framework should also contain adequate enforcement mechanisms in relation to climate-related disclosure requirements. Given the significance of these disclosures to investors and a broad range of other stakeholders, these enforcement mechanisms should be available to any interested person, and not just regulators. Regulators should also be adequately resourced, including through adequate training for enforcement teams on climate-related matters.

In particular, the EDO supports the extension of the 'two strikes' rule in relation to listed entities' remuneration reports, as contained in Div 9 of Pt 2G.2 of the *Corporations Act 2001* (Cth), to listed entities' separate reports on climate-related matters (see our response to Question 6 below). This would mean that, if at least 25% of shareholders vote against the adoption of a listed entities' climate-related report for two consecutive annual general meetings (**AGM**), shareholders must vote at the latter AGM on whether the directors (except the managing director) need to stand for re-election.[52] If the 'spill resolution' passes with a majority of eligible votes cast, then a 'spill' meeting

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[52] As provided for in relation to remuneration reports in ss 250U and 250V of the *Corporations Act 2001* (Cth).

must take place within 90 days at which shareholders will elect new directors.[53] Already, shareholders are using AGMs to vote on listed entities' transition plan. For example, 48.97% of shareholders voted against Woodside Energy Ltd's transition plan at its 2022 AGM, partly because of its heavy reliance on offsets. 36.93% of shareholders voted against Santos' transition plan at its 2022 AGM. We **recommend** the introduction of the 'two strikes' rule in relation to these disclosures as an important accountability mechanism for shareholders frustrated with directors' continued mismanagement of climate-related risks.

Consideration should also be given to appropriate protections for whistle-blowers in relation to disclosure and risk issues. In this regard, the EDO commends the recommendations of a recent report, 'Protecting Australia's Whistleblowers: The Federal Roadmap'.[54]

<u>Question 6</u>: 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?

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

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

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

Listed disclosing entities' continuous disclosure obligations require them to notify the ASX of information that is not generally available if a "reasonable person would expect the information, if it were generally available, to have a material effect on the price or value" of the entity's securities, and provisions of the ASX Listing Rules require disclosure of that information (s 674).[55] ASX Listing Rule 3.1 requires listed entities to immediately disclose information to the ASX if they are or

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[53] As provided for in relation to remuneration reports in ss 250W and 250X of the *Corporations Act 2001* (Cth).
[54] Brown, A.J. and Pender K, *Protecting Australia's Whistleblowers: The Federal Roadmap* (2022, Griffith University, Human Rights Law Centre and Transparency International Australia: Brisbane and Melbourne) available at: https://static1.squarespace.com/static/580025f66b8f5b2dabbe4291/t/637733c7f74b51682fadbbfd/1668756427004/Protecting+Australia%27s+Whistleblowers+-+The+Federal+Roadmap+%282022%29+web.pdf
[55] Section 674A of the *Corporations Act 2001* (Cth) creates a civil penalty provision that requires listed disclosing entities to disclose information that is not generally availably if the entity "knows, or is reckless or negligent with respect to whether, the information would, if it were generally available, have a material effect on the price or value" of the entity's securities.

become aware of any information that a "reasonable person would expect to have a material effect on the price or value of the entity's securities", subject to the exceptions in Rule 3.1A, and lists examples of such information. A reasonable person would be taken to expect information to have a material effect on an entity's securities if the information "would, or would be likely to, influence persons who commonly invest in securities in deciding whether to acquire or dispose" of the entity's securities (s 677(1)).

Australian regulatory guidance has confirmed that climate-related risks and opportunities may be "material" for the purposes of these disclosure requirements.[56]

To the extent Australia's new climate reporting framework requires disclosures above and beyond these existing requirements, such as the disclosure of entities' greenhouse gas emissions and transition plans, the EDO **recommends** they should be contained in an annual separate report to ensure they are readily accessible for users of those reports.

<u>Question 7</u>: 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)?

Materiality judgments when undertaking climate reporting should be consistent with existing Australian materiality standards. Further guidance on materiality should be provided to assist users who are not as familiar with financial and accounting concepts, as has occurred in the UK, where the Financial Conduct Authority issued a Technical Note to clarify when climate change and environmental, social and governance matters will be material[57] (although we note that the draft UK Technical Note has been criticised for failing to adequately clarify the relevant legal tests of materiality.)[58]

The definitions of materiality detailed in response to Question 6 above are broadly consistent with the definition in Draft IFRS S1, except for their omission of any concept of "enterprise value". The EDO considers it would be unhelpful to incorporate enterprise value into materiality judgments for climate reporting. This would create unnecessary inconsistencies with the well understood definitions of materiality in the *Corporations Act 2001* (Cth), ASX Listing Rules, and AASB 101. The only potential benefit of using enterprise value would be alignment with the definition of materiality in Draft IFRS S1. However, similar concerns regarding potential inconsistencies prompted the ISSB to "tentatively decide" in its most recent meeting in December 2022 to remove enterprise value from the objective and description of materiality in Draft IFRS S1.[59] It was also concerned that the concept of enterprise value unduly narrows the scope of disclosures and would

[56] See, for example, ASIC, *Regulatory Guide 247: Effective disclosure in an operating and financial review* (August 2019); ASIC, *Report 593: Climate risk disclosure by Australia's listed companies* (September 2018); ASX Corporate Governance Council, *Corporate Governance Principles and Recommendations* (Fourth Edition, February 2019).
[57] Financial Conduct Authority, Technical Note 801.2, *Primary Market Technical Note: Disclosures in relation to ESG matters, including climate change*, (December 2021).
[58] ClientEarth, FCA Consultation CP20/3: Proposals to enhance climate-related disclosures, (August 2020).
[59] IFRS Sustainability, 'Staff paper: General Sustainability-related Disclosures' (December 2022) paragraph 8; IFRS Sustainability, 'Staff paper: General Sustainability-related Disclosures' (October 2022) paragraph 54.

exclude decision-useful information.[60] There is therefore minimal, if any, benefit to using enterprise value to inform materiality judgments for climate reporting.

The EDO **recommends** the inclusion of "double materiality" as adopted by the EU in December 2022.[61] In addition to disclosing material climate-related impacts on an entity, this would require an entity to disclose its material impacts on the climate. In our view, this appropriately acknowledges the inextricable link between entities' climate-related impacts and risks, and, given the increasing importance of entities' climate related impacts to financial decision making, ensures that investors and other stakeholders are provided with decision-useful information. Requiring covered entities to comply with international best practice also minimises the risk of future regulatory 'lag' and fragmentation, and resulting administrative costs and burdens which would require covered entities to also disclose their material impacts on the climate. Covered entities' greenhouse gas emissions should be disclosed regardless of their materiality, as encouraged by the TCFD[62] and required by Draft IFRS S2 (see our response to Questions 9 and 10).[63]

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?

The EDO **recommends** existing auditing requirements for financial reports being extended to covered entities' other climate-related disclosures, particularly their disclosure of greenhouse gas emissions, as will be required in New Zealand.[64] Using satellite data, the International Energy Agency (**IEA**) estimates that Australian coal mines emit double the amount of methane – a particularly potent greenhouse gas – than has been officially reported.[65] Recent analysis suggests that emissions from oil and gas facilities around the world are about three times higher than has been reported.[66] Ensuring that covered entities' emissions data is accurate and reliable is critical to ensuring Australia fulfils its international and statutory climate-related commitments.

It is important that auditors genuinely test the assumptions and estimates made in entities' climate-related disclosures. It is also important that ASIC regularly tests disclosures against Paris-aligned assumptions and estimates and, where these assumptions fall short, provide advice to shareholders of that information.

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[60] IFRS Sustainability, 'Staff paper: General Sustainability-related Disclosures' (October 2022) paragraph 54.
[61] EU Directive, arts 19a(1) and 29a(1).
[62] The TCFD encourages all organisations to disclose Scope 1 and 2 emissions independent of an assessment of materiality. The disclosure of Scope 3 emissions is subject to materiality, but the TCFD encourages organisations to disclose these emissions: TCFD, *Implementing the Recommendations of the Task Force on Climate-related Financial Disclosures* (October 2021), p 6.
[63] TCFD, *Implementing the Recommendations of the Task Force on Climate-related Financial Disclosures* (June 2017), Draft IFRS S2, paragraph 21(a).
[64] *Financial Sector (Climate-related Disclosures and Other Matters) Amendment Act 2021* (NZ) s 461ZH. This provision comes into effect on the third anniversary of the Act obtaining Royal Ascent, i.e. October 2024 (s 2(3)(b)).
[65] Sabina Assan et al, *Tackling Australia's Coal Mine Methane Problem* (June 2022) p 17.
[66] Climate Trace, *More than 70,000 of the highest emitting greenhouse has sources identified in largest available global emissions inventory* (Website, 26 January 2023) <available at: https://climatetrace.org/news/more-than-70000-of-the-highest-emitting-greenhouse-gas>.

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?

EDO **recommends** that covered entities should be required to report all emissions (Scope 1, 2 and 3), consistent with the ISSB Draft Standards. Paragraph 21 of the Draft IFRS S2 requires entities to report their Scope 1, 2 and 3 absolute greenhouse gas emissions in accordance with the widely-used *Greenhouse Gas Protocol Corporate Standard* (**GHG Protocol**). The main principles and calculation methodologies of the *National Greenhouse and Energy Reporting Act 2007* (Cth) (**NGER Act**) and related regulations are already aligned with the GHG Protocol.

The key difference between the emissions disclosures required by Draft IFRS S2 and the NGER Act is that, under Draft IFRS S2, entities are required to disclose Scope 3 (upstream and downstream) emissions. This is a positive improvement on the NGER Act. Scope 3 emissions disclosures are critical for investors and other stakeholders to be able to assess the risks in a covered entity's value chain, for example, the covered entity's financed emissions. However, as at 2022, only 49% of ASX200 companies disclosed some Scope 3 emissions, and only 14% disclosed all Scope 3 emissions.[67] For entities already disclosing Scope 3 emissions, the Draft IFRS S2's requirements will better equalise markets by bringing competitors up to leading practices. For entities not already disclosing Scope 3 emissions, it will prompt better understanding of climate-related risks and opportunities, and their ability to manage a range of physical, transitional, regulatory, reputational and other risks.

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

Yes. The EDO considers that the ISSB Draft Standards, and the industry-specific requirements in Appendix B to Draft IFRS S2 that are based on SASB Standards, provide appropriate common baseline metrics to ensure consistency and comparability of emissions disclosures. In particular, Draft IFRS S2 and the industry-specific SASB Standards appropriately require entities to:

(a) disclose absolute Scope 1, 2 and 3 greenhouse gas emissions;
(b) measure emissions in accordance with the GHG Protocol, which provides clear guidance on boundary-setting for corporate emissions accounting, amongst other things;
(c) express emissions as metric tonnes of CO_2 equivalent (**CO_2e**), meaning that entities' emissions disclosures must account for all seven greenhouse gas emissions covered by the Kyoto Protocol, and not just CO_2; and
(d) calculate the CO_2e of different greenhouse gases in accordance with the global warming potential values in the 2014 Fifth Assessment Report of the IPCC.

However, EDO **recommends** that the consistency and comparability of emissions disclosures could be improved by covered entities being required to use the *same* emissions accounting method in the GHG Protocol. In particular, covered entities should be required to report emissions

[67] PWC, *ESG Reporting in Australia* (2022) p 14.

on an operational *and* equity basis, or on an equity basis (which is the most decision-useful information for investors and other stakeholders). Covered entities being able to choose whether they report operational or equity emissions impedes an easy comparison of those emissions. For example, it was difficult to understand the impact of the oil and gas operations of BHP Ltd merging with Woodside Energy Ltd because BHP had been reporting emissions on an operational basis, while Woodside has been reporting them on an equity basis.

<u>Question 11</u>: 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?

Alignment with the 1.5°C temperature goal of the Paris Agreement and Australia's legislated net zero emissions by 2050 target[68] should be a central consideration for climate-related risk management disclosures. This would help ensure that Australia fulfils its international and statutory climate-related commitments, and that Australia's climate-related disclosure regime is scientifically-sound and aligned with international best practice.

A significant amount of the EDO's work relates to analysis of company transition plans. The EDO is concerned by the prevalence of transition plans that are not aligned with the scientific consensus of what is required to achieve the Paris Agreement's 1.5°C temperature goal, and considers this is a key deficiency that the mandatory climate-related disclosure framework should seek to rectify. Indeed, the Australian Council of Superannuation Investors has noted that investors now expect that all companies should be stress-testing their business against a 1.5°C scenario. However, as at 2022, only 39 companies on the ASX200 did so.[69]

The EDO considers that Draft IFRS S2's requirements regarding transition plan disclosures are not sufficient to rectify these problems. The Draft IFRS S2 requires covered entities to disclose whether their climate-related scenario analysis[70] and climate-related targets[71] are aligned with the Paris Agreement. However, it does not require covered entities to conduct climate--related scenario analysis aligned with the 1.5°C temperature goal of the Paris Agreement or to disclose transition plans compatible with limiting warming to 1.5°C. This is at odds with international standards regarding net zero emissions targets and international best practice:

(a) The EU requires "large undertakings" and "small and medium-sized undertakings, except micro undertakings, which are public-interest entities" to describe their plans, including implementing actions and related financial and investment plans, to ensure that their business model and strategy are compatible with limiting warming to 1.5°C and achieving the EU's target of carbon neutrality by 2050, and, where relevant, their exposure to coal-, oil- and gas-related activities.[72]

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[68] *Climate Change Act 2022* (Cth) s 10(1)(b).
[69] Australian Council of Superannuation Investors, *Promises, pathways & performance: Climate change disclosure in the ASX200* (July 2022) p 6.
[70] Draft IFRS S2 paragraph 15(b)(i)(4).
[71] Draft IFRS S2 paragraph 23(e).
[72] EU Directive, arts 19a(2)(iii), 29a(2)(iii).

(b) The SBTi's Corporate Net Zero Standard, which was the first international standard for corporate net-zero target setting aligned with the Paris Agreement, requires that, at a minimum, corporate Scope 1 and 2 emissions targets must be consistent with the level of decarbonisation required to keep warming to 1.5°C, and Scope 3 emissions targets must be consistent with well-below 2°C of warming.[73]

(c) The UN Expert Group concluded that non-state entities can only claim to be "net zero-aligned" if their transition plan is in line with the IPCC or IEA net zero emissions modelled pathways that limit warming to 1.5°C.[74]

Similarly, Draft IFRS S2 requires covered entities to disclose the extent to which their climate related targets rely on the use of offsets,[75] and does not require disclosure of which scope emissions are covered by their climate-related targets, let alone that climate-related targets cover all scope emissions.[76] This is inconsistent with international target setting standards aligned with the Paris Agreement, which prohibit the use of offsets to achieve emissions reduction targets, and require targets to cover all scope emissions (Scope 1, 2 and 3).[77]

The EDO **recommends** that, as in the EU, covered entities should be required to disclose scenario analysis and transition plans consistent with the IPCC and IEA modelled pathways that limit warming to 1.5°C. As noted above, this reflects investor expectations, and is necessary to help Australia fulfil its international and statutory climate-related commitments. We consider ASIC guidance on transition plan requirements that are consistent with the SBTi's Corporate Net Zero Standard and the findings of the UN Expert Group would assist covered entities by providing certainty regarding their obligations.

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

No. Once mandatory reporting requirements apply to an entity, all disclosure and/or assurance requirements should apply. The EDO considers the phased introduction of particular requirements would produce unnecessary fragmentation and confusion. Further, investors and other stakeholders have expressed, and the ISSB acknowledged, an "urgent need for disclosure standards on climate change".[78] As explained in response to Question 2 above, entities, particularly listed entities, should have already developed processes for complying with international climate-related disclosures given they have been on notice of those requirements for at least 5 years.

It is important that assurance requirements commence at the same time as disclosure requirements to ensure there is accurate reporting. Given there are well-established auditing

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[73] SBTi, *SBTi Criteria and Recommendations* (Version 5.0, October 2021) criterion 18.
[74] United Nations, *Integrity Matters: Net Zero Commitments by Businesses, Financial Institutions, Cities and Regions* (November 2022) (**UN Report**), Recommendation 1.
[75] Draft IFRS S2, paragraph 13(b)(iii).
[76] Draft IFRS S2, paragraph 23.
[77] SBTi, *SBTi Criteria and Recommendations* (Version 5.0, October 2021), criterion 4 (the SBTi requires companies to have a Scope 3 emissions target if their Scope 3 emissions are 40% or more of their total Scope 1, 2 and 3 emissions, or if companies are involved in the sale or distribution of natural gas and/or other fossil fuels, irrespective of the share of these emissions compared to their total Scope 1, 2 and 3 emissions); UN Report, Recommendation 1.
[78] Draft IFRS S2, p 7.

requirements under the *Corporations Act 2001* (Cth), the EDO considers there is no justification for the delayed implementation of those requirements in relation to climate-related disclosures.

Question 13: Are there any specific capability or data challenges in the Australian context that should be considered when implementing new requirements?

Data gaps or challenges should not delay mandatory reporting requirements. Covered entities should be able to provide best estimates where necessary and genuine gaps exist, and disclose any uncertainties regarding these estimates. The EDO has no further comments in relation to this question.

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?

The EDO supports efforts to improve the consistency of covered entities' climate-related disclosures, and to ensure these disclosures are premised on the best available science. According to analysis by the Australian Council of Superannuation Investors, inconsistent, incomplete, incomparable and unverifiable information within scenario analysis is a frequent complaint of investors. While the Council found some level of standardisation through the use of IEA scenarios, it also found 105 different scenarios used across varying levels of warming.[79]

The EDO **recommends** that the provision of consistent, scientifically-sound supporting information would be sufficiently achieved by requiring entities to disclose transition plans and scenario analysis aligned with the IPCC and IEA modelled pathways and scenarios that limit warming to 1.5°C (see response to Question 11 above). These pathways and scenarios reflect the best available science, and underpin international standards regarding emissions reduction targets aligned with the Paris Agreement, such as the SBTi's Corporate Net Zero Standard and the UN Expert Group. The provision of separate supporting information would create unnecessary fragmentation and impose additional regulatory burdens and costs.

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 EDO considers the "reasonable grounds" requirements are appropriate and sufficiently flexible to accommodate any uncertainties or assumptions that may be inherent to certain aspects of climate-related disclosures, such as transition plans. We **strongly oppose the adoption of other tests or measures**, such as the US "safe harbour" provisions, including in relation to Scope 3 emissions disclosures. This would introduce inconsistencies with well established statutory norms.

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

The EDO can see no principled reason why forward-looking statements should be subject to different statutory norms merely by virtue of being climate-related.

We note that this position is consistent with advice provided by Sebastian Hartford-Davis and Kellie Dyon to the Australian Council of Superannuation Investors, which concluded that the safe harbour provisions are not necessary or desirable.[80] Indeed, the authors concluded that such provisions may undermine the benefits of standardised climate reporting "by removing the effective incentive (liability risk) which will actuate them".[81]

Misleading or deceptive conduct is prohibited by the *Corporations Act 2001* (Cth), *Australian Consumer Law* (**ACL**) and *Australian Securities and Investments Commission Act 2001* (Cth) (**ASIC Act**).[82] Where a representation is made about a future matter, it will be "taken to be misleading" if the person making the representation "does not have reasonable grounds for making the representation".[83] Although this requirement does not shift the ultimate burden of proof, a finding that an entity has made a representation concerning a future matter places an evidential burden on the entity to adduce evidence that there were reasonable grounds for making that representation.[84]

For there to have been "reasonable grounds", there must have existed "facts sufficient to induce that state of mind in a reasonable person" at the time the representation was made.[85] So, where disclosures are made with appropriate disclosure of assumptions, methodologies and uncertainties, the assessment of reasonableness will take into account those assumptions and disclosed uncertainties.[86] Under existing law, a forward-looking statement is not misleading merely because it later turns out to be wrong.[87] A forward-looking statement that later turns out to be wrong might be found to have been made on a reasonable basis at the time, if, for example, it was consistent with the best available science at the time. Courts do not expect entities to predict the unpredictable, but instead to make sensible disclosures on a reasonable basis, and to update earlier disclosures if they become misleading by reason of later events.[88]

The EDO therefore considers that the "reasonableness" standard is sufficiently sensitive to accommodate the uncertainties that may be inherent in some climate-related disclosures, such as transition plans and Scope 3 emissions. The EDO appreciates that it may be difficult for covered entities to accurately quantify their Scope 3 emissions, given this will often rely on upstream suppliers and downstream consumers accurately reporting their own emissions. As long as entities are adequately disclosing the material assumptions, methodologies and uncertainties that

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[80] Directors' liability advice, p 2.
[81] Directors' liability advice, p 18.
[82] *Corporations Act 2001* (Cth) s 1041H; ACL s 18; ASIC Act s 12DA.
[83] *Corporations Act 2001* (Cth) s 796C; ACL s 4(1); ASIC Act s 12BB(1).
[84] *Australian Competition and Consumer Commission v Woolworths Limited* [2019] FCA 1039 at [113] (this finding was not disturbed on appeal).
[85] *Sykes v Reserve Bank of Australia* (1998) 158 ALR 710, 712 (Heerey J).
[86] See, eg, *ASIC v Macdonald (No 11)* (2009) 256 ALR 199 at [373]-[374] (the actuarial reports relied upon were "inherently uncertain"). See also [79]-[83] of the General Requirements Exposure Draft, including the statement at [79]: "The use of reasonable estimates is an essential part of preparing sustainability-related metrics and does not undermine the usefulness of the information if the estimates are accurately described and explained".
[87] *Bonham atf Aucham Super Fund v Iluka Resources Ltd* (2022) 404 ALR 15 at [698].
[88] See *Ambergate Ltd v CMA Corporation Ltd* (2016) 110 ACSR 642 at [36]-[37].

underpin these disclosures, and had a reasonable basis for using those assumptions and methodologies, the risk of being found liable for a forward-looking statement should be minimal.

<u>Question 16</u>: 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?

As indicated in response to Question 6 above, it is important that climate-related information that is *material* is disclosed in accordance with covered entities' continuous disclosure obligations, as would any other material information. Any disclosures that go above and beyond those already required under Australian disclosure law should be contained in an annual separate report that is easily accessible for investors and other stakeholders.

<u>Question 17</u>: 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?

It is important that the framework is sufficiently flexible to accommodate evolving regulatory and market expectations. As detailed in response to Question 5 above, the EDO considers the first regulatory framework proposal in the Consultation Paper would be sufficiently adaptable to accommodate developments such as the forthcoming recommendations of the Task Force on Nature-related Financial Disclosures.

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

The EDO supports any reporting system that will make it easier for investors and other stakeholders to easily access to covered entities' climate-related disclosures, including digital report. We otherwise have no comments in relation to this question.

<u>Question 19</u>: 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?

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

The EDO is concerned that the second potential structure could lead to further fragmentation of the regulatory landscape, and resulting confusion for users. The third potential structure risks

further delaying the implementation of a mandatory climate-disclosure framework at a time when Australia is already experiencing regulatory lag, and investors and other stakeholders have expressed an "urgent need for disclosure standards on climate change".[89]

[89] Draft IFRS S2, p 7.