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Climate-related financial disclosure

ACCR response to Treasury consultation

ABOUT ACCR

The Australasian Centre for Corporate Responsibility (ACCR) is a not-for-profit, philanthropically-funded research organisation, based in Australia. ACCR monitors the environmental, social and governance (ESG) practices and performance of Australian-listed companies, including climate change, human rights, and labour rights. We undertake research and highlight emerging areas of business risk through private and public engagement. For more information, follow ACCR on [Facebook](#), [Twitter](#) and [LinkedIn](#).

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Introduction

ACCR is grateful for the opportunity to input into the Treasury's Climate-related financial disclosure consultation, and is supportive of the principles underpinning this planned reform.

Climate-related disclosures should be rigorous, comparable and consistent, allowing investors and other important actors to make meaningful assessments of a company's position.

Australia has just over 80 months to meet its legislated 2030 emissions reduction target. It is important to get these reforms right. It is also important that we start allocating capital in a way that drives a rapid transition away from fossil fuels as soon as possible. Implementing a robust climate disclosure regime from 2024 should complement existing guidance and standards which have already been issued by AUASB/AASB¹ and IFRS.²

A core part of ACCR's work is how climate-related risks are being assessed and disclosed, particularly by ASX-listed companies. Recently, we have focused on the way in which ASX-listed companies are treating climate change matters in the audited financial statements. Disclosure of which climate scenarios were used to prepare the statements, and the quantitative assumptions that they include, would assist investors to make informed investment and engagement decisions.

Investor expectations around climate risk disclosure are increasing, and several investor groups and other organisations have raised concerns that existing reporting practices are creating significant, material information gaps.

For instance, Climate Action 100+ (CA100+) has developed a new Climate Accounting and Audit Indicator for the Net Zero Company Benchmark, which requires companies and auditors to ensure visibility of how accelerating decarbonisation in alignment with the Paris goal of limiting warming to 1.5C will impact companies' financial positions and profitability.

CA100+ expects companies and their auditors to publish evidence that they have comprehensively considered climate in audited financial statements and notes, and to incorporate the impacts of 'net-zero by 2050' (or sooner). However, CA100+'s application of this benchmark in 2022 found that companies are failing to integrate climate risk into accounting and audit practices. Not a single company had incorporated the impacts of net-zero by 2050.³ This assessment included 14 ASX-listed companies, with only BHP and Rio Tinto meeting the requirements for one of seven sub indicators.

Relatedly, Carbon Tracker has recently warned that, despite recent urgencies of global accounting and auditing standard-setters, material climate-related risks are not being adequately considered in financial reporting, and that the exclusion of climate impacts from financial accounts can lead to 'overstated profits and asset values, and understated liabilities'.⁴ Carbon Tracker's 2021 report 'Flying Blind: The glaring absence of climate risks in financial reporting' found that over 70% of companies reviewed did not indicate that they had considered climate matters in preparing their financial statements, and that 80% of auditors did not indicate if or how they had considered material climate-related matters in their audits.

¹ AASB & AUASB, 2019, [Climate-related and other emerging risks disclosures: assessing financial statement materiality using AASB/IASB Practice Statement 2](#).

² IFRS, 2020, [Effects of climate-related matters on financial statements](#).

³ Climate Action 100+, 2021, [Global Investors Driving Business Transition](#), pp. 56-7.

⁴ Carbon Tracker, 2021, [Flying Blind: The Glaring Absence of Climate Risks in Financial Reporting](#), p. 53.

Subsequent to the publication of that report, non-profit environmental law organisation ClientEarth wrote to KPMG, outlining their concerns that they and other auditors are 'habitually failing to demonstrate compliance with their legal and professional duties and public commitments on climate change', and that this failure was 'systemic within corporate reporting and parts of the audit profession'. In the same letter, ClientEarth signaled their intention to work with regulators to increase scrutiny of auditors' performance.⁵

Since 2019, a group of investors, led by Sarasin & Partners, have engaged with the 'big four' auditors - Deloitte, EY, PwC and KPMG - about how they are integrating material climate risks into auditing practices. By 2021 this investor group represented \$4.5 trillion, and wrote to the 'big four' requesting that they improve their management of risks associated with 'accounting misrepresentation', and that they pursue accounting disclosures that align with a 1.5C pathway.⁶ Since materiality is a function of what investors deem is relevant and important for their own decision-making, such considerations are now material for those auditors.

A 2022 report by the Climateworks Centre assessing ASX200 alignment to the 1.5 degree climate goal found that only 23% of the 187 companies assessed actually have a net zero emissions target for applicable emissions, and only 9% of 177 companies assessed have set Scope 3 emissions reduction targets in line with a 1.5 degree pathway.⁷ Notably, based on current targets and commitments, the ASX200 will overspend its 1.5°C carbon budget by 741 MtCO₂e or 36% for the period 2021 to 2050.

As these concerning findings suggest, there is an urgent need in Australia for watertight climate financial disclosure laws, and for those laws to comprehensively cover company transition plans.

⁵ ClientEarth, December 2021, ['Accounting for climate change - the role of audit'](#).

⁶ Sarasin and Partners, November 2021, ['Investor expectations: net zero audits'](#).

⁷ Climateworks Centre, December 2022, ['Methodology report: Assessing ASX200 alignment to the 1.5°C climate goal'](#).

ACCR response to consultation questions

Question	ACCR Response
<p>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:</p> <p>1.1 What are the costs and benefits of meeting existing climate reporting expectations?</p> <p>1.2 What are the costs and benefits of Australia not aligning with international practice and in particular global baseline standards for climate reporting?</p>	<p>It is important for Australia to implement international best practice standards regarding climate-related financial risk disclosure, in order to remain a competitive jurisdiction for investment. If Australia lags behind in this area, this will further create an added degree of risk when investing in ASX-listed companies as it will be more difficult for investors to analyse, compare performance, and engage with ASX-listed companies exposed to transition and physical risks.</p> <p>This is particularly so in light of incoming EU and other international standards, which will require companies to disclose Paris-aligned transition plans.</p> <p>This would have subsequent, negative effects on Australia's own decarbonisation progress, and impede the country's climate resilience. Clear, accurate, comparable and consistent disclosures will help.</p> <p>As the consultation paper notes, climate change is internationally recognised as a material risk to the global financial system. A comprehensive climate risk disclosure framework will cover the impacts that issuers have on the climate, as well as the risks they face.</p>
<p>Question 2: Should Australia adopt a phased approach to climate disclosure, with the first report for initially covered entities being financial year 2024-25?</p> <p>2.1 What considerations should apply to determining the cohorts covered in subsequent phases of mandatory disclosure, and the timing of future phases?</p>	<p>We anticipate that some degree of phasing will be inevitable, but want to emphasise the urgency of implementing and enforcing robust reporting standards. The development of a scheme to commence no later than 2024 is reasonable.</p> <p>Many large entities already collect a lot of the information which will be covered by this proposed reporting scheme, and will be in a position to adapt quickly to new reporting requirements.</p>
<p>Question 3: To which entities should mandatory climate disclosures apply initially?</p> <p>3.1 What size thresholds would be appropriate to determine a large, listed entity and a large financial institution, respectively?</p> <p>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?</p>	<p>ACCR is keen to ensure that any mandatory climate disclosure scheme will cover the most systemically significant listed and non-listed entities, from an emissions and physical risk perspective, to enhance the resilience of the Australian economy.</p> <p>A number of financial institutions could be categorised as 'universal owners', as they manage large, highly-diversified portfolios, capturing a 'slice' of the whole market.⁸ Since their returns depend on the health and performance of that market, in general, the proper exercise of their fiduciary duty involves protecting the whole economy, and the environment which it depends upon.</p> <p>Implementation of a rigorous, comparable, and consistent climate disclosure scheme, applicable to listed and non-listed entities, will support Australia to achieve its climate goals, and in turn will support these 'universal owners' to safeguard their portfolios.</p> <p>It is vital that the mandatory climate disclosure scheme initially covers entities that are current or potential heavy emitters. This could be</p>

⁸ PRI, 2011, ['Universal Ownership: Why environmental externalities matter to institutional investors'](#), p. 3.

	<p>achieved by drawing on the National Greenhouse and Energy Reporting Act thresholds, along with prioritising companies working in specific industry sectors (such as Petroleum Exploration) using Australian and New Zealand Standard Industrial Classification (ANZSIC) codes.</p>
<p>Question 4: Should Australia seek to align our climate reporting requirements with the global baseline envisaged by the International Sustainability Boards?</p> <p>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?</p> <p>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?</p>	<p>The draft ISSB climate disclosure standard could form the basis of Australian reporting requirements. There are some important improvements that should be made to that draft standard, including requirements to ensure that:</p> <ul style="list-style-type: none"> ● Transition risk assessments include information to allow users to assess a company's alignment with a 1.5C scenario; ● Transition plans consider lifecycle emissions and are benchmarked against 1.5C scenarios; ● The contribution that different strategies make to a company's transition plan, such as reliance on offsets, divestment or CCS, are clearly quantified; ● There is a high degree of consistency between financial statements and climate disclosures - for example, if companies make public commitments in their transition plans then these should be reflected in their financial accounts; ● Companies are required to nominate a director who is responsible for climate matters and transition planning, as a matter of good governance. <p>Such improvements would assist investors and other users of company financial statements to make meaningful and informed assessments as to whether a company's transition plan is aligned with the Paris Agreement.</p>
<p>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?</p>	<p>Material financial issues belong in the financial statements.</p> <p>Where climate-related disclosures are made outside of the audited financial statements, they should be subject to the same governance and assurance as the financial report including board certification, auditing, etc. There should be consistency across all reporting.</p> <p>For example, while the equivalent rules in New Zealand allow disclosures to be made in existing financial statements or a standalone document, from late October 2024 all statements relating to greenhouse gas emissions must be subject to, at minimum, a limited assurance engagement.⁹</p> <p>Where companies make disclosures or commitments around, for example, net-zero or transition planning, we expect that these disclosures will be reflected in their financial accounts.</p>

⁹ [Aotearoa New Zealand Climate Standard 3](#), p. 9; *Financial Sector (Climate-related Disclosures and Other Matters) Amendment Act 2021* (New Zealand), s 461ZH; [Aotearoa New Zealand Climate Standard 1](#), p. 11.

<p>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)?</p>	<p>ACCR supports the existing guidance from the AASB on materiality assessments, “sustainability-related financial information is material if omitting, misstating or obscuring that information could reasonably be expected to influence decisions that the primary users of general purpose financial reporting make on the basis of that reporting”, since this highlights that materiality a decisions cannot be made by an issuer in isolation.</p> <p>Double materiality - ACCR encourages the implementation of a double materiality assessment in line with the standards being introduced in the EU. This would ensure that disclosures would capture both: (a) the financial impact of climate risks and opportunities; and (b) the impact of companies on climate and environment. In turn, this would give investors a better view of how (a) is affected by (b).¹⁰</p> <p>This double materiality assessment is likely to be adopted elsewhere, including in the European Union, and so its inclusion under Australian rules would significantly enhance comparability.</p> <p>Under the standards proposed by EFRAG, which underpin the EU’s Corporate Sustainability Reporting Directive, “a sustainability matter meets the criteria of double materiality if it is material from an impact perspective or from a financial perspective or from both” and if that test is met then in-scope companies would need to report on the matter. This could be applied to climate matters in Australia to match international standards.</p>
<p>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?</p>	<p>As outlined above, ACCR is concerned that current financial audit independence arrangements are not working well, despite calls from global accounting and auditing standard-setters. Carbon Tracker Initiative’s 2021 study of 107 companies’ reporting practices revealed that 80% of auditors did not appear to have conducted an assessment of climate risk, and that 63% failed to identify inconsistencies regarding climate risks/targets across company reporting.¹¹ In practice, standards and guidance around climate risk disclosure are not being met.</p> <p>Audits should provide reasonable assurance of all mandatory metrics, limited assurance of the remainder of the report and explicitly consider information which may be omitted from reports.</p> <p>Assurance providers must be subject to high independence and quality management standards. The current model where an entity appoints and pays its own auditor creates a tension with genuine independence.</p>
<p>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?</p>	<p>All companies should be required to disclose all of the emissions associated with their operations and value chains i.e. scopes 1, 2 and 3, along with their emission targets and transition plans.</p> <p>Scope 3 emissions, in particular, will be critical to determining a complete picture of an undertaking’s emissions and prospects for achieving Paris alignment. Further, the disclosure of scope 3 emissions will better enable the Australian (and international) sustainable finance markets to be</p>

¹⁰ As explained by EFRAG in the Draft European Sustainability Reporting Standards, “Impact materiality and financial materiality assessments are inter-related and the interdependencies between these two dimensions shall be considered.” 2022, [ESRS 1 General Requirements](#), p. 11.

¹¹ PRI & Carbon Tracker, 2021, [Flying Blind: The glaring absence of climate risks in financial reporting](#).

	<p>equally robust on climate, by enabling the associated reductions in GHG emissions financing.</p> <p>Scope 3 emissions, by their nature, include a diversity of emission sources, some of which are genuinely uncertain. Most global emissions are due to ‘use of sold product’ emissions from fossil fuel production. These emissions are easy to calculate and are already reported by many fossil fuel producers.</p> <p>For transition plans, companies should be required to: set absolute, rather than intensity targets; set interim targets; and not rely on the use of GHG removals or carbon credits, or unproven technologies, to abate, except in the case of residual emissions.</p> <p>We support the use of existing Australian emissions reporting frameworks, where available.</p>
<p>Question 10: Should a common baseline of metrics be defined so that there is a degree of consistency between disclosures, including industry-specific metrics?</p>	<p>Yes. One of the fundamental problems with current disclosures is that issuers select metrics that present their entity in a favourable light. This reduces the comparability and decision-usefulness of these disclosures. As a case study, ACCR reviewed the draft IFRS S2 oil and gas metrics¹² and considers that these are insufficient. They do not, for example, include:</p> <ul style="list-style-type: none"> • scope 3 metrics • the use of offsets, divestment and CCS contributing towards the company’s long term strategy and expenses • key assumptions used for impairment testing
<p>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?</p>	<p>ACCR is concerned that companies are not providing transparent public information about how they are facing and managing climate related risks, including those relating to transition planning, Carbon Capture and Storage (CCS), divestment of high emission assets, and the use of offsets.</p> <p>We are encouraged by ASIC's increasing focus on 'greenwashing', which partly responds to this issue. Per ASIC, 'Greenwashing distorts relevant information that a current or prospective investor might require in order to make informed investment decisions. It can erode investor confidence in the market for sustainability-related products and poses a threat to a fair and efficient financial system.'¹³ In January 2023, listed energy company Black Mountain Energy Limited (BME) was issued with three infringement notices and a fine, relating to its claims that two of its gas projects were 'net zero emissions'.¹⁴</p> <p>Climate disclosures are intended to increase market transparency, and improve capital allocation. In this light, requiring listed entities to seek support for their climate disclosures at annual general meetings would allow investors to voice their opinion on the sufficiency of these reports. Elements of the ‘two strike’ approach applied to remuneration reports could be applied to climate disclosures, and would be a powerful mechanism to ensure that climate reports meet investors’ expectations.</p>
<p>Question 12: Should particular disclosure requirements and/or assurance of those requirements commence in different phases, and why?</p>	<p>At most, there could be a single year lag between reporting unaudited and then audited disclosures.</p>

¹² IFRS, 2022, [\[Draft\] IFRS S2 Climate-related Disclosures Appendix B Industry-based disclosure requirements Volume B11–Oil & Gas-Exploration & Production](#).

¹³ ASIC, 2022, [How to avoid greenwashing when offering or promoting sustainability-related products](#).

¹⁴ ASIC, 2023, [23-001MR ASIC issues infringement notices to energy company for greenwashing](#).

<p>Question 13: Are there any specific capability or data challenges in the Australian context that should be considered when implementing new requirements?</p> <p>13.1 How and by whom might any data gaps be addressed?</p> <p>13.2 Are there any specific initiatives in comparable jurisdictions that may assist users and preparers of this information in addressing these challenges?</p>	<p>We note that there are specialist physical climate risk valuation and data provider services now available, and while this data availability has been a limiting factor in the past, there is now no excuse to not include an assessment of risks to assets from the impacts of changes to climate, including the primary and secondary impacts of: riverine and surface flooding; coastal inundation (including sea level rise); forest fire; subsidence; wind, cyclones; heatwaves; coastal erosion.</p>
<p>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?</p>	<p>A common set of commodity prices for various scenarios and scope 3 emissions factors could be useful to give companies a way to disclose impacts without disclosing commercially sensitive information. This doesn't necessarily preclude issuers using additional scenarios. A key focus of ACCR is on industry lobbying, and we would note that any agency that publishes scenario analysis assumptions would need governance that ensures it remains impartial. Where companies use non-publicly available scenarios, they should provide sufficient information on the inputs, so that users can understand the assumptions.</p>
<p>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?</p>	<p>ACCR recognises that climate disclosures necessarily involve the use of forward-looking information, such as climate scenarios. However, directors will not face increased legal risks for disclosing climate-related financial risks, and in our view they do not require further legal protections. The recent legal opinion of barrister Sebastian Hartford Davis is relevant here: 'Directors must make a genuine assessment as to the appropriateness of the forward-looking disclosure at the time it is made, but they will not face liability merely because their assessment later turns out to be incorrect'.¹⁵ If directors are diligent, supported by capable management teams, and can demonstrate that their assessment of climate matters have a 'reasonable basis', then they will be sufficiently protected.</p>

¹⁵ AC SI, ['Advice regarding potential liability of directors under the ISSB draft standards for forward looking statements'](#), 6c. See also: AFR, February 2023, [Battle lines drawn over director protections in new climate regime](#).