17 February 2023

Climate Disclosure Unit
Market Conduct Division
The Treasury
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By email: climatereportingconsultation@treasury.gov.au

Climate-related financial disclosure Consultation paper

The Australian Financial Markets Association (AFMA) is providing comment on the *Climate-related financial disclosure Consultation paper* (Consultation).

AFMA represents the interests of over 125 participants in Australia's wholesale banking and financial markets. Our members include Australian and foreign-owned banks, securities companies, treasury corporations, and traders across a wide range of markets and industry service providers. Our members are the major providers of services to Australian businesses and retail investors who use the financial markets.

AFMA has also consulted with the Asia Securities Industry & Financial Markets Association (ASIFMA), with whom we share many members, in the preparation of this submission. They have indicated their support for these comments.

AFMA supports the Australian Government policy of providing the Australian community in general, and investors, with greater transparency to assist in climate-related planning, identifying financial risks, and opportunities. AFMA agrees with the objective of standardised, internationally-aligned reporting requirements for businesses to make disclosures regarding governance, strategy, risk management, targets and metrics – including greenhouse gases.

Overall, mandatory business disclosure standards should, as far as possible, be aligned with international reporting practices, to minimise compliance costs for Australian businesses that operate internationally, safeguard Australia's financial centre attractiveness, and to ensure Australia's regime is viewed with credibility by international markets.

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AFMA agrees with the principle that Australian standards should build on the existing financial reporting system and be both scalable and flexible to accommodate future developments in the global baseline for climate and sustainability reporting, to minimise the expected compliance costs and potential for unintended consequences.

AFMA's responses to the Consultation paper questions follow in the Attachment to this letter starting, with a Summary Table to provide a brief overview.

Please contact [redacted] either on [redacted] or by email at [redacted] in regard to this letter.

Yours sincerely

[redacted]

[redacted]
General Counsel & International Adviser

Climate-related financial disclosure Consultation paper

Responses to Consultation Questions

Summary Table

This table provides an executive summary of the detailed responses which follow. Numbers refer to the Consultation question numbering.

1	It will reduce confusion for entities and regulators; reduce overhead costs; ensure Australia's access to global markets; avoid costs associated with preparing, settling and publishing multiple sets of reports; reduce the risk of arbitrage and minimise complexity in any extra-territoriality application and conflict of laws.
1.1	They will impose a regulatory burden cost, system establishment and maintenance costs, as well as other related IT costs. For issuer respondents, the highest ranked benefit was better performance in meeting sustainability, climate, ESG, and SDG goals, followed by better access to data capable of enhancing corporate strategy. Some issuers also cited "lower cost of capital" as a benefit, and a correlation was found between spending more on overall climate-related disclosure and recognizing a lower cost of capital.
1.2	If Australia does not align with international practice, it stands the risk of becoming a global outlier. Based on current status of global ESG adoption / pending public policy proposals, there is broad consensus in favour of the ISSB (which leverages TCFD, SASB and others). Using existing global standards will help keep costs low. There is potential for significant cost for preparers if they are required to meet slightly different requirements in international markets.
2	A phased approach to adoption across entity types, sectors and/or sizes will be needed to comply with disclosure requirements, covered entities will need to develop complex infrastructure, including hiring new personnel with relevant skills, developing new systems, processes and policies and designing and implementing new disclosure control and internal control mechanism. Depending on the reporting entity's size, sophistication, and experience with voluntarily disclosing emissions data, the development and implementation of these new systems and processes will require significant time and impose significant up-front compliance costs.
2.1	The following factors should be taken into account: incorporate all entities that are currently subject to financial reporting under the Corporations Act as well as comparably sized financial companies, public authorities, and government enterprises into the reporting regime; larger entities will need to rely on averages and proxies – which will impact their reporting; the phasing-in of assurance requirements; offshore operations that are not as material as domestic operations should be able to submit branch/subsidiary reporting; clearly defined phase-ins periods may motivate large customers and suppliers to introduce the necessary internal processes for reporting these metrics where they have not done so already

	and further consideration of what an appropriate disclosure looks like for smaller entities.
3	Reference is made to the comments on phasing-in of entities without definite recommendations. It is important to view corporations at a 'Legal Entity' level based on appropriate thresholds to determine if they are in scope for Phase 1 of the disclosure requirements. Likewise, the reliance and dependency on third parties for data must be considered and that reporting for these entities are required prior to reporting by financial institutions to ensure data availability and quality data for climate related disclosures.
3.1	Regardless of exact thresholds, there should be exemptions for large foreign financial institutions that are already required to report climate-related financial information in their home jurisdictions, or at least a possibility to reference to parent-level reporting to fulfill the requirements.
3.2	Thresholds need to be sufficiently high in a phased approached to avoid unnecessarily burdening smaller entities without the systems, processes, and resources in place to implement.
3.3	No comment.
4	AFMA supports the establishment by ISSB of a global baseline for disclosure and agrees that consistent and comparable disclosures are necessary. However, there may be a future need for the Australian Government to explore interoperability between jurisdictions that select different disclosure baselines. Australia should only adopt ISSB standards when they are finalised. While AFMA firmly supports the ISSB developing a global baseline for climate and sustainability disclosure, there should not be mandatory reporting that references the ISSB until such a standard is final.
4.1	The basis of alignment is the TCFD reporting principles. As the TCFD has already gained significant acceptance in alignment of the disclosure objectives, on this basis is supported. Account needs to be taken of the fact that governance, strategy, and risk management are integrated into general frameworks for financial reporting and prudential regulation requirements and sustainability and climate are not, and should not, be treated as independent elements. They are part of a broader integrated framework and cannot be simply disaggregated.
4.2	AFMA supports the establishment by ISSB of a global baseline for disclosure and agrees that consistent and comparable disclosures are necessary. AFMA does not support providing any indications that the upcoming final standards will include mandatory Scope 3 GHG disclosure.
5	Refer to 4.1. Key considerations on framework development are: leveraging existing, industry developed guidance and standards rather than inventing a new standard; Include a materiality standard that is rooted in financial materiality; include safe harbors for disclosures that rely on third party or estimated data; disclosures on forward-looking information or assumptions related to how an organization intends

	to navigate climate-related risks/opportunities should be largely principles-based and specific considerations related to governance, strategy, and risk management should be high-level and principles-based.
6	There should not be a requirement to include the contemplated disclosure within an annual report as long as the reporting provided is available and accessible. Flexibility at this point makes it easier for large international firms to consolidate their climate disclosures to comply with various requirements in different jurisdictions.
7	The starting point with the materiality standard for a reporting entity would be that, for the entity's general-purpose financial statements, to avoid having multiple definitions relating to materiality applicable to a particular entity. The ISSB's definition appears to be rooted in disclosing information that investors would find useful in making an investment decision (financial materiality).
8	Settings around disclosure should be implemented first and then a staged approach to assurance be undertaken later. Criteria would be needed to provide enough clarity for an assurance process that would meet prospective rules-based compliance expectations in Australia. The climate-related disclosure statements assurance cannot be done at present, and considerable capacity building needs to occur before climate related financial disclosures can be adequately assured. We also do not accept the role of auditors in verifying the robustness, validity or appropriateness of bank models which are used for portfolio analysis and through which the result of the analysis would feed into the disclosures.
9	AFMA recommends that Australia adopt reciprocal recognition of a comparable internationality aligned disclosure regime, i.e. framework developed by the Task Force on Climate-Related Financial Disclosure (TCFD Framework) and the greenhouse gas (GHG) accounting standards under the GHG Protocol. This encompasses mandatory Scope 1 and 2, but Scope 3 should only be a progressively adopted when there are future globally agreed Scope 3 estimation methodologies.
10	AFMA supports disclosure of industry specific metrics and a common global baseline, but not all metrics will be relevant to all entities and entities should not be required to report on metrics that are irrelevant to them. However, firms should be able to select metrics most relevant to their business models. Australia should coordinate and work with the ISSB as they move forward with making SASB mandatory in the future.
11	There is support for covered entities providing transparent information about how they are managing climate related risks. Structured transition periods will be required for a range of specific clearly defined and bounded disclosures. Greater specificity of expectations, requirements, and definitions could help guide entities to prepare transparent disclosure of information. To ensure flexibility, this could be provided in the form of guidance documents, rather than regulation.

12	AFMA recommends a phased approach for disclosure reporting in Australia. Entities may need time to ensure sufficient completeness and reliability data needed to support the disclosures and build their capacity to disclose the required information - a phased approach recognises the need for initial flexibility and allows time for methodologies to mature, for greater standardisation to be developed and data to become more readily available. The assurance providers will also then have time to review reports across industries and ascertain best practice approaches.
13	From an Australian perspective, an efficient data collection infrastructure needs to be put in place which will require time and sequencing over a transition period. The current availability and reliability of data and methodologies will present a medium-term challenge. For Australia, a phased approach to adoption across entity types, sectors and/or sizes will be needed. Structured transition periods will be required for a range of specific clearly defined and bounded disclosures.
13.1	There are opportunities for public-private collaboration to address data gaps and ensure consistency across key datasets. For example: standardised Scope 3 methodologies or emissions factors could be included in NGER regulations; more information from government organisations could be made available to disclosing entities, potentially from a centrally coordinated entity and the frequency of government surveys (such as the Australian Energy Survey) could be increased to allow for more accurate disclosures.
13.2	Some examples include: elements of the New Zealand approach could be adopted; the GHG Protocol and PCAF contain guidance on calculating Scope 3 emissions; and the French Government's new advice-based Climate Data Steering Committee.
14	There is a strong case for public provision of common data and other information, including methodologies and scenarios. The need to improve the availability, quality and comparability of climate-related data is recognised globally. Recommendation 4 of the NGFS Final Report on Bridging Data Gaps, highlighted the role for regulators and central banks in developing tools.
15	Compared to traditional financial reporting, climate disclosures involve substantial use of forward-looking information and depend upon external parameters that are subject to uncertainty, such as climate scenarios. While the need and urgency for standards climate-related financial disclosures is accepted and recognised, we must start somewhere. However, AFMA is concerned with the potential for a sizable increase on civil litigation that such disclosures may encourage. To address these concerns, we would welcome a safe harbour provision.
16	Secondary impacts on legislation, will need to be considered. These impacts include: The Banking Executive Accountability Regime (BEAR) and potential successor Financial Accountability Regime (FAR); continuous disclosure obligations under the Corporations Act 2001 and ASX Listing Rules; the Australian Competition Law and Australian Securities and Investments Commission Act; Director's & officer's

	fiduciary & statutory duties and other prudential requirements and delegated legislation.
17	It is appropriate to build appropriate levels of flexibility into governance structures, while the immediate focus should remain on climate-related financial disclosure. Social issues are even more complex and difficult to measure/compare between jurisdictions. Standards need to be flexible and dynamic, however other topics such as biodiversity and sustainability will require referencing to standards and requirements specific to those topics. For example, TCFD is climate focused and generally should not be used as a baseline for sustainability or biodiversity - that should be TFND framework which is yet to be published.
18	Digital reporting should only be optional i.e. on voluntary basis. Digital reporting will require an additional step to convert the data for report lodgement. Mandating digital reporting for sustainability risk reporting would create a discrepancy with broader financial reporting. There would be additional costs and time to implement digital reporting, which may be an additional level of complexity for limited benefit.
19	Option (2) better reflects international developments. An effective reporting framework for climate-related financial risks will require close integration of expertise in both financial reporting and climate risk. As a less desirable option, we would look to Option (3), conditional on inclusion of appropriate expertise. This option may have the potential advantage of allowing flexibility and avoiding regulatory arbitrage and/or duplication.

Introductory comment

There is the need for principles based non-prescriptive, dynamic framework that is aligned with existing frameworks regionally and globally to help achieve convergence on disclosure requirements. This directs alignment of the Australian disclosure framework with global baselines standards such as TCFD and ISSB, once finalised.

Climate change is a global challenge, so a globally consistent approach to tackle the issue is required. IOSCO has articulated this principle well when it says - 'to cooperate in developing, implementing and promoting adherence to internationally recognized and consistent standards of regulation…'[1]

To this end, Australia should align its disclosure requirements with internationally recognised standards and frameworks. The objective is to increase decision-useful information for investors on how companies are addressing climate risk to their business. This means standards setters need to continue to engage and harmonise their requirements. The TCFD has served as an important framework for regulators to draw from, and we anticipate that when the ISSB is finalised, it could serve a similar role.

As a principle, overly extensive disclosure requirements make it challenging for users of disclosure to understand which elements are most important. Overwhelming investors with extensive non-material disclosure on climate and sustainability issues will undercut the policy objective of focusing investors on important information that they need to make investment decisions.

Globally consistent approaches to disclosures are pivotal to prevent the proliferation of competing regimes and regulatory fragmentation, increasing the cost and complexity of preparation — impairing reliability and making comparisons more time consuming and confusing for users.

Account should be taken of global institutions having frameworks, policies, standards, and procedures which should be recognised and permitted to be applied in country rather than a requirement for standalone frameworks in country.

New disclosure standards do not front-run the adoption by companies and their capacity to provide such disclosures.

[1] IOSCO Good Practices: https://www.iosco.org/news/pdf/IOSCONEWS633.pdf

Question responses

> ***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 benefits of Australia aligning with international practice on climate-related financial disclosure primarily include:

- reducing confusion for entities and regulators
- reducing overhead costs of international trade finance arrangements and ensure Australia's access to global markets
- avoiding costs associated with preparing, settling, and publishing multiple sets of reporting
- reducing the risk of arbitrage
- minimising complexity in any extra-territoriality application and conflict of laws.

Leveraging off a global baseline for corporate sustainability standards (TCFD/ISSB) will help companies navigate a myriad of inconsistent voluntary regimes. In addition, investors will benefit from clear, comparable, reliable, and decision-useful information.

From a regulatory burden and compliance cost perspective, the reporting should allow firms, where relevant, to defer to consolidated / group-level reporting. This would minimise some of the costs associated with reporting as it would avoid duplicative processes.

Costs could be limited if the requirements are based on financial materiality, in line with existing international best practice. As a caution, any suggestions about transaction reporting as part of the mandatory reporting should be rejected as this is wholly different. It is operationally complex and costly, as has been demonstrated in other financial regulatory reporting contexts.

> *1.1. What are the costs and benefits of meeting existing climate reporting expectations?*

Disclosure standards will impose a major regulatory burden on businesses. Beyond initial system establishment, costs for data collection these need to be maintained on an ongoing basis.

Implementation costs will be significant in absolute terms for large entities and significant in relative terms for smaller entities. A local example of costs is APRA's Climate Vulnerability Assessment (CVA) of five banks, over 2021-22, involved many hundreds of bank staff, some of whom were taken out of their daily duties to perform the test. Many banks also engaged consultants to support the work.

The most authoritative source for gauging the cost is a US survey data, based on SEC proposed reporting requirements analogous to those of the ISSB. The survey by the SustainAbility Institute at ERM[2], found that on average, corporate issuers are spending USD 533,000 (approx. AUD 765,074) annually on climate-related disclosure, while institutional investors are spending an average of USD 1,372,000 (approx. AUD 1,969,383) annually to collect, analyse, and report climate data to inform their investment decisions.

The ERM survey provides insight into what issuers currently spend on climate-related disclosure activities that would be required under the SEC's proposed rules. Its assessment of current average annual issuer costs is similar to the SEC's estimate of $530,000 (approx. 773, 046) in annual issuer costs after the first year of implementation.

Part of this includes significant costs associated with developing appropriate processes and controls as well as IT infrastructures. Another consideration is the increased legal liability costs associated with disclosures that need to be managed and catered for; as well as up-skilling staff.

Along with discussions of costs, the ERM survey asked respondents to rate the potential benefits of climate-related disclosures and impact assessments. For issuers, the highest-ranking benefits were as follows.

1. better performance in meeting sustainability, climate, and SDG goals
2. better access to data capable of enhancing corporate strategy
3. some issuers also cited "lower cost of capital" as a benefit, as a correlation was found between spending more on overall climate-related disclosure and recognizing a lower cost of capital.

Standardised climate-related disclosures may also reduce uncertainty for companies regarding the specific content to disclose. Before companies can take any tangible steps toward preparing climate-related disclosures, they must first determine which specific climate-related discussions, metrics, and analyses are most appropriate to disclose—a process that, under the current regime, can involve significant uncertainty.

In addition, the uncertain, complex, and multidimensional nature unique to climate-related risks, combined with the unpredictability of investor responses to such disclosures— can also make it costly for management to determine the risks which meet the materiality threshold.

By implementing a standardised climate disclosure framework, the proposed disclosure could potentially reduce the burden that companies may face in the environment of diverging voluntary frameworks and help clarify for reporting entities what they should disclose, where and when to make their disclosures, and what structure or methodology to use.

[2] ERM Study:
https://www.sustainability.com/globalassets/sustainability.com/thinking/pdfs/2022/costs-and-benefits-of-climate-related-disclosure-activities-by-corporate-issuers-and-institutional-investors-17-may-22.pdf

Similarly, implementing globalised standards alleviates exposure to claims of greenwashing arising from multiple reporting requirements over different areas of global portfolios.

Meeting existing climate reporting expectations requires dedicated teams to collect data, prepare reports, and prepare data inputs from across corporate groups. For reporting obligations where methodologies are not standardised, additional time and effort is required to re-work data, identify available data sources (or proxies), and refine methodologies. This work requires ongoing upskilling across a broad cross-section of staff.

It should also be borne in mind that additional professional services fees will be incurred for the preparation of assurance reports as well as internal costs for the preparation of statements. Assurance will also significantly increase costs with limited benefit to investors/users of sustainability information. This is because there are no global auditing/assurance standards for climate-related information / TCFD aligned disclosure. It will be some time before there are credible professional services in this regard. The result is that the information will be reviewed/audited against different standards (undermining the quality of reported information).

The human resource element also needs to be taken into consideration. Staff need to be trained to professional levels of competence in a world which is facing serious staffing shortages in relation to regulatory reporting, compliance, and assurance work.

1.2.	What are the costs and benefits of Australia not aligning with international practice and in particular global baseline standards for climate reporting?

If Australia does not align with international practice, it stands the risk of becoming a global outlier. Based on current status of global ESG adoption / pending public policy proposals, there is broad consensus in favour of the ISSB (which leverages TCFD, SASB and others).

UK, EU, Singapore, Japan are aligning climate risk management principle and disclosures with global standards (notably, TCFD) and the United States has adopted analogous reporting. It should be noted that global investors and financial institutions will require increased availability of internationally aligned climate disclosures for both investment strategies/decisions and also broader risk management purposes. Issuers that do not provide that information may, in the medium-term, encounter more difficulties attracting investors or funding from financial institutions.

The need for globally consistent standards was recognised by the Network for Greening the Financial System (NGFS) Progress Report on Bridging Data Gaps, which noted that fragmentation of disclosure frameworks complicates comparability, assurance and impacts availability of climate-related data. While we support alignment with ISSB in-principle, we note that there may be challenges in aligning to 'a global baseline' when there is currently more than one such 'baseline', but the benefits of alignment outweigh costs of not aligning.

2. Should Australia adopt a phased approach to climate disclosure, with the first report for initially covered entities being financial year 2024-25?

As highlighted above, in order to comply with disclosure requirements, covered entities will need to develop complex infrastructure, including hiring new personnel with relevant skills, developing new systems, processes and policies and designing and implementing new disclosure control and internal control mechanism. Depending on the reporting entity's size, sophistication, and experience with voluntarily disclosing emissions data, we believe the development and implementation of these new systems and processes will require significant time and impose significant up-front compliance costs — as evidenced above.

For Australia, a phased approach to adoption across entity types, sectors and/or sizes will be needed. Depending when the disclosure proposal is finalized, covered entities may need time to ensure sufficient completeness and reliability data needed to support the disclosures and build their capacity to disclose the required information - a phased in approach recognises the need for initial flexibility and allows time for methodologies to mature, for greater standardisation to be developed and data to become more readily available.

AFMA supports regulators engaging in an iterative process as they work through developing climate-related disclosure regulation to give industry the opportunity to offer feedback.

In regard to the timing of reporting for financial year 2024 -25, this will be dependent on a number of factors such as:

- Interoperability of the Australian disclosure framework with global standards
- Global institutions' ability to leverage home requirements
- Data availability for specific disclosure aspects such as Scope 3

AFMA considers it premature to mandate Scope 3 reporting at an early phase. Data issues are of concern, but more importantly, inconsistent estimation methodologies for all 15 categories of Scope 3 emissions (especially Category 15, 'Investments'). It should be noted that even the GHG Protocol does not have a comprehensive approach (e.g. for financed and facilitated emission), nor does it intend to.

Based on experience with the transition period allowed for the implementation of major accounting standards such as IFRS 9 Financial Instruments, IFRS 16 Leases and IFRS 15 Revenue from Contracts with Customers— this would mean at least three years as a minimum timeline.

Structured transition periods will be required for a range of specific clearly defined and bounded disclosures. The financial services sector is dependent on its customer base being able to report information for their dependent disclosures. This is particularly relevant to Scope 3 climate disclosures, which are dependent on established reporting of Scope 1 emissions by clients of financial institutions.

Elsewhere, a phased approach is being put in place and we suggest looking at the United Kingdom in particular. Lessons learnt from the UK regime could looked at along with consideration of safe harbours as discussed further below.

A phased approach will need to take into account the fact that large entities (including ADIs) require data from other smaller entities for Scope 3 emissions, and that the quality of this data may remain low while only large entities are required to meet disclosure obligations. The safe harbour may be the best way to address this technical issue.

We also note the TCFD already 'recommends' reporting within financial statements.

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

A phased approach to reporting with clearly defined thresholds for advancing to subsequent phases would be most beneficial. The following factors should be taken into account in considering how phasing would work -

- The goal would be to incorporate all entities that are currently subject to financial reporting under the Corporations Act 2001 as well as comparably sized financial companies, public authorities, and government enterprises into the reporting regime.
- Large entities (including banks) may require data from smaller entities for Scope 3 emissions. Without access to data from smaller entities, larger entities will need to rely on averages and proxies – which will impact their reporting. They will require time to scale up their expertise and capacity.
- Particular consideration needs to be given to the phasing-in of assurance requirements. Which is dealt with in more detail in response to Questions 7 and 8.
- At present, there are simply not the trained staff available, both because of the general shortage of workers and the need to develop training courses and then train a cadre of people to do the required work. Regardless of the desire to move expeditiously, the training process along with the development of data collection systems will take time.
- Adoption by regulators of a pragmatic approach in early phases. Consideration by regulators regarding comparative disclosures in the first year of reporting, and guidance on when comparatives should be re-stated.
- Offshore operations that are not as material as domestic operations should be able to submit branch/subsidiary reporting, similar to the rules in place for financial reporting.
- Clearly defined phase-ins periods may motivate large customers and suppliers to introduce the necessary internal processes for reporting these metrics where they have not done so already.
- There may be a need for further consideration of what an appropriate disclosure looks like for smaller entities. There may be an intermediary solution short of full ISSB disclosure – such as moving towards economy-wide reporting of GHG emissions or similar metrics. This could have the benefit of minimising reporting requirements on small entities while still supporting Scope 3 emissions disclosures by larger entities.

While size is suggested as an obvious threshold mark, other considerations should also be taken into account. For financial institutions, requirements should be applied based upon the nature of their business activities and exposure to material climate-related financial risks, not necessarily just size. Other relevant considerations include: the nature and purpose of a financial institution's balance sheet and the magnitude of climate risk-sensitive assets to which it is exposed(e.g. as a custody bank, balance sheet has limited direct exposure to climate-related financial risks given the nature of its composition, whereas these risks may pose a much greater threat to a smaller bank with significant exposure through its direct financing of carbon-emitting industries, or other similarly climate risk-sensitive assets).

3. To which entities should mandatory climate disclosures apply initially?

As a starting point, it is important to view corporations at a 'Legal Entity' level based on appropriate thresholds to determine if they are in scope for Phase 1 of the disclosure requirements.

Given that financial institutions are reliant on information from their counterparties/clients/third parties (particularly for Scope 3), as explained above, this is another consideration for the phasing in of reporting. It is important that reporting for these entities are required prior to reporting by financial institutions to ensure data availability and quality data for climate related disclosures.

Account needs to be made for branches of banks in particular, which while part of a large legal entities are often, in the Australian domestic context, actually quite small and limited businesses. Regardless of exact thresholds, there should be exemptions for large foreign financial institutions that are already required to report climate-related financial information in their home jurisdictions, or at least a possibility to reference to parent-level reporting to fulfill the requirements in a similar way that is allowed for prudential reporting.

3.1. Should Australia seek to align our climate reporting requirements with the global baseline envisaged by the International Sustainability Boards?

Alignment with the global baseline envisaged by the ISSB is supported subject to this being based on a phased approach that would initially apply to large listed entities.

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

Thresholds need to be sufficiently high in a phased approached to avoid unnecessarily burdening smaller entities without the systems, processes, and resources in place to implement. Again, reference is made to the detailed comments in respect of Question 2.

3.3. 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?

No comment.

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

AFMA supports ISSB establishing a global baseline for disclosure and agrees that consistent and comparable disclosures are necessary. However, regulators should avoid crafting regulations that reference ISSB until such a standard is final. In addition, regulators and the Australian Government will need to consider a future need to explore interoperability between jurisdictions that select different disclosure baselines.

Australia should only adopt ISSB standards when they are finalised. While AFMA firmly supports the ISSB developing a global baseline for climate and sustainability disclosure there should not be mandatory reporting that references the ISSB until such standard is final.

There were significant challenges with the original ISSB standards that led the ISSB to revisit the standards throughout 2022. Instead, we encourage the Australian Treasury to continue to use the TCFD framework as a reference until the ISSB standards are finalized. At which point, it would be appropriate to evaluate implementing the ISSB. Once the ISSB standards have been assessed as final, and it becomes clear how many of the challenges pointed out by members (e.g. on materiality, which is also mentioned in this consultation later on) have been resolved in the final version — this would determine, to a large degree, how quickly covered entities would be able to bring their reporting processes up to speed.

AFMA suggests that Australia adopt reciprocal recognition of comparable disclosure requirements across jurisdictions and allow for the availability of substituted compliance with respect to such comparable requirements.

Given the global nature of climate risk, we would ask that locally, incorporated foreign financial institutions and branches of foreign financial institutions operating in Australia be permitted to leverage the group or parent company climate-related policies and procedures to meet the climate-related disclosure requirements. We would also suggest that such entities' disclosure to be consolidated at group or head office level (i.e. "Group report"). Allowing parent level disclosures would be consistent with the treatment in some of the other countries in Asia, for example Singapore and Hong Kong, which have rolled out climate related disclosure requirements but have permitted parent level disclosures to be considered for compliance.

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?

There are three considerations that should be noted about the Australian context:

1. The need to source Australia-specific data to perform scenario analysis and quantify financial risk and opportunity, including how the Government would support that through the National Greenhouse and Energy Reporting (NGER) scheme or other regulation; and
2. There is a proposed metric in ISSB Scope 2 requiring disclosure of how an entity is applying an internal carbon price in decision-making. Any proposed Australian carbon pricing mechanisms would need to be aligned.
3. Attention needs to be paid to the overall framework in which such disclosure will occur in Australia. Governance, strategy, and risk management need to be integrated into general frameworks for financial reporting and prudential regulation requirements and sustainability and climate are part of a broader integrated framework.

Generally, disclosure of governance, strategy, risk management and metrics and targets is being done by entities reporting under the TCFD principles. Disclosure should be directed to measures to be undertaken by the entity and not demand release of commercially sensitive information to competitors. These measures fit within an integrated broader financial and prudential reporting framework. Specific content should not be required in regard to these matters.

In this regard the following points should be taken into account:

- *Governance:* Climate governance disclosure needs to take account that it will be fitting with an existing general governance disclosure framework. This is particularly the case for financial institutions which are heavily regulated and sit under prudential rules. Governance is an integrated process and climate governance should not be, and it is difficult, to disaggregated it from it's the general governance framework.

- *Risk management:* The primary purpose of disclosing risk management processes is to provide context for how the reporting entity thinks about and addresses the most significant risks to successfully executing its business objectives and accomplishing its strategy. Climate change considerations would be appropriately included in the elements of risk management processes consistently and proportionately, taking into account other risks to which the risk management analysis applies. This implies that interconnections between climate-related risks and other risks should be considered as part of an integral process where the existing elements are applied to a limited business or strategic planning horizon which has realistic validity in the near term but becomes more speculative into the medium term. This is the key point of challenge and distinction in doing so, as integration would have to take account of the longer time horizons over which climate-related risks might materialise.

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?

AFMA supports the establishment by ISSB of a global baseline for disclosure and agrees that consistent and comparable disclosures are necessary. However, as mentioned previously, rules that reference ISSB should be mandatory until such standard is final.

AFMA does not support providing any indications that the upcoming final standards will include mandatory Scope 3 GHG disclosure.

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?

Refer to 4.1

AFMA supports flexibility to provide legal certainty, the ability to amend and adapt regulatory requirements and rules (subject to parliamentary oversight) as well as clarity on the detail of disclosure, interoperability with other regimes and in scope entities are important considerations for the designing of an Australian disclosure framework. Where appropriate, the new regulatory framework should align with established standards (e.g. definition of a reporting entity). Reporting should be on a full-year basis, with interim reporting only required for material changes from full-year disclosures. There could also be standardisation of metrics /targets, similar to how financial statements are already relatively standardised across industries.

It is suggested the law should set out the core principles and regulations set out the requirements to meet the principles. This will allow for regulations to be amended and evolve without needing to pass a new law.

Key considerations on framework development are noted below -

- As regulators look to design a new climate disclosure standard, it is recommended that leveraging existing, industry developed guidance and standards rather than inventing a new standard. Harmonising disclosure requirements with internationally recognized standards and frameworks will assist in producing consistent and comparable climate information.
- Include a materiality standard that is rooted in financial materiality, i.e., disclosing information that an investor would find important in making an investment decision. While assessing materiality of climate reporting is an evolving area, we have found that aligning the traditional financial materiality standard may generate more consistent and comparable information across sectors. We also support regulators applying the currently accepted materiality standard for that

jurisdiction as a helpful starting point when designing a disclosure standard. We caution against departing from standards that generate the types and amount of information required by the regulator on other risk topics.

- Include safe harbors for disclosures that rely on third party or estimated data. Due to climate-related data gaps and nascent state of methodologies needed to conduct disclosure that relies on third party or estimated data, such as Scope 3 and scenario analysis, we support the inclusion of 'safe harbor' from liability — as expressed above. This will encourage companies to be transparent and provide important information to the best of their ability (based on currently available information). We suggest this should be applicable to forward looking statements (transition plans and scenario analysis) and also for statements where companies need to rely on third party information that is essentially outside of the financial institutions control.
- Disclosures on forward-looking information or assumptions related to how an organisation intends to navigate climate-related risks/opportunities should be largely principles-based. This is a relatively new and untested concept that we are seeing emerge in climate disclosure standards, going further than the requirements to test the resilience of the entity's strategy as required by the TCFD. Forward looking assumptions about climate-related risks or opportunities requires forward projections of factors that we do not currently take into account. It can also include disclosure of potentially proprietary or confidential information.
- Specific considerations related to governance, strategy, and risk management should be high-level and principles based. This will allow businesses to tailor their disclosures to fit the material considerations of their companies and industries.

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?

There should not be a requirement to include the contemplated disclosure within an annual report as long as the reporting provided is available and accessible. Flexibility in this point makes it easier for large international firms to consolidate their climate disclosures to comply with various requirements in different jurisdictions.

Over time, it is important to encourage and enhance corporate climate related information, and not to constrain it through unnecessarily prescriptive requirements.

Disclosures could be included as part of general-purpose financial reporting. ISSB is an investor-oriented standard and placing disclosures in this document will help with articulating potential financial impacts due to climate change. This is consistent with TCFD expectations and will assist with comparability.

Consideration will need to be given to the practical considerations. For example, if different materiality definitions emerge for financial statements and the climate reporting or if different levels of external assurance are applied it could add complexity for preparers and may require changes to the Corporations Act 2001. Should the new requirements be added to the financial statements, there will need to be a level of flexibility in how the information is presented to minimise the risk that either of the disclosures (existing financial and new climate reporting requirements) do not obfuscate the other.

The timing to obtain emissions information and related financial metrics for a given fiscal year is expected to be longer. Accurately disclosing Scope 3 emission (if required) will be challenging, given that the reliable emission data is from companies in the value chain (including financed emissions) and will not be available at the time we need to begin preparing our own disclosures.

In contemplation of these data limitations and realities, we recommend the Standards clarify that reporting entities should use the most readily available, highest quality information, including best estimates where applicable, similar to the concepts employed under U.S. GAAP and IFRS in regards to fair value measurement, which are based on known valuation concepts and the use of information quality hierarchies (e.g., Levels 1, 2 and 3 defined in U.S. GAAP and IFRS to describe the information quality of fair value measurements). This means that such disclosures may be based on emissions information that is one to two years old because such information is the most readily available and highest quality information.

Furthermore, given the timing concerns discussed above, deadlines for climate reporting, after those applicable for annual financial reports, by which companies must provide climate related disclosures (e.g., a jurisdiction might provide an additional 225 days beyond its standard deadline/s for annual general financial reporting). This would help alleviate the challenge of having all relevant data available and ready for disclosure by general financial reporting filing deadlines and would allow for inclusion of the highest quality information on emissions.

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)?

The starting point with the materiality standard for a reporting entity would be that for the entity's general purpose financial statements, to avoid having multiple definitions relating to materiality applicable to a particular entity. Recently, the ISSB agreed to fully align its description of materiality with IFRS Accounting Standards. In doing so, it has removed the existing definition of 'enterprise value' and the words 'to assess enterprise value' from the objective and description of materiality in the proposals. It also agreed to remove 'significant' from the description of which sustainability-related risks and opportunities to disclose. The ISSB's definition appears to be rooted in disclosing

information that investors would find useful in making an investment decision (financial materiality).

Applying financial materiality principles to assessing materiality of climate risks i.e. including materiality qualifiers throughout the framework to only report on what is deemed material, rather than requiring disclosure regardless of materiality.

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 issue of assurance processes is considered to be a critical area of challenge with practical implementation of the requirements. Criteria would be needed to provide enough clarity for an assurance process that would meet prospective rules-based compliance expectations in Australia.

Feedback to AFMA indicates the climate-related disclosure statements assurance cannot be done at present and considerable capacity building needs to occur before climate related financial disclosures can be adequately assured. We also do not accept the role of auditors in verifying the robustness, validity or appropriateness of bank models which are used for portfolio analysis and through which the result of the analysis would feed into the disclosures.

It is suggested that settings around disclosure be implemented first and then a staged approach to assurance be undertaken later. We suggest that the phased approach have the following characteristics:

- Climate-related financial disclosures would form an alternative category of assurance.
- There would be an initial requirement for agreement upon procedures, including on the precise matters of what auditors are auditing – assertions/statements, alignment with ISSB requirements, targets, scenarios, etc. This will also help to determine the level of assurance required.
- Assurance levels would initially be limited to greenhouse gas emissions, gradually expanding to other areas (e.g., the reasonableness of disclosures) as standards and industry capability matures.
- There will be a dependency on high quality data availability and consideration needs to be given to publication and reporting of any exceptions.
- Subsequent consultations would occur on the specifics of independent assurance.

Assurance providers should be subject to independence and quality management standards. There may also need to be greater alignment across the industry from assurance providers to ensure that assurances are appropriate and consistent. The existing Australian external auditor independence and quality management standards would be a logical starting point for such requirements. Professional standards will also be required to be developed for assurance providers.

9. What considerations should apply to requirements to report emissions (Scope 1, 2 and 3) including use of any relevant Australian emissions reporting frameworks?

AFMA recommends that Australia adopt reciprocal recognition of comparable internationality aligned disclosure regime, i.e. framework developed by the Task Force on Climate-Related Financial Disclosure (TCFD Framework) and the greenhouse gas (GHG) accounting standards under the GHG Protocol. This encompasses mandatory Scope 1 and 2, but Scope 3 should be progressively adopted when there is a future globally agreed Scope 3 estimation methodology.

The recent updates to the GHG emissions reporting requirements in the ISSB proposal: The ISSB recognizes that Scope 3 information involves sourcing emissions data from third parties in a firm's value chain and that it may not be possible to get value chain emissions data from that reporting year, among other challenges mentioned above. Therefore, we support the ISSB's decision to include a later effective date for all Scope 3 disclosures and permitting inclusion of value chain information with non-aligned reporting period.

The ISSB climate proposal does not specify how a financial institution should calculate its financed and facilitated emissions. The ISSB confirmed that financed emissions disclosure would be required for commercial banking, insurance, and asset management. Therefore, flexibility to disclose which categories are included or not in the targets, will be necessary.

There are timing challenges related to reporting emissions: Scope 1 and Scope 2 emissions, while easier to calculate than Scope 3 emissions, are not immediately available and require some data gathering and calculations of their own.

Scope 2 emissions, for instance, may be based on third-party data, which must be obtained after the fiscal year-end, verified, and incorporated into models to produce accurate figures.

Avoiding duplication of existing emissions and climate-related risk reporting requirements should be a key consideration.

While there may be opportunities to align reporting requirements with the NGER, this would need to be done in such a way as to not apply the NGER to smaller entities where that would not deliver any significant emissions reduction or community benefit.

Market-based emissions (in addition to location-based emissions required under NGER) should be considered. The GHG protocol states dual reporting of both is required – and PCAF states preference for financed emissions to utilise market-based numbers.

Finally, consideration should also be given to existing NGER reporting and timing. NGER reporting is 1 July to 30 June and companies may have different reporting dates. Exemptions around the use of differing timing for Scope 3 emissions should be considered.

The main advantage of using GHG accounting is that a single metric can be used to encompass an entire portfolio rather than just segments of the portfolio at the asset class level.

However, multi-asset portfolios are more difficult. Data for financial institutions' exposures to transition risks are also subject to numerous gaps. GHG emissions data are still generally not available at the level of individual firms, and those data sets that are available are, in some cases, limited to Scope 1 (direct) GHG emissions, rather than capturing emissions across their value chains.

There are still significant challenges facing application of the GHG Protocol: namely

- Emissions data availability.
- Inability to track "green" activities directly (except through avoided emissions accounting).
- Lack of accounting standard and agreement on some measurement issues.
- Data availability and confidentiality issues outside listed companies and projects.
- Difficult to apply to off–balance sheet services.

Scope 3

Scope 3 financed emissions will consist, at least in part, of the Scope 1 and 2 emissions of other companies, it is impracticable to expect disclosure of Scope 3 disclosures at the same time as other required climate-related disclosures; based on the aforementioned rationale. Furthermore, much of the client Scope 3 emissions data are modelled, which adds an additional delay for the financial institution. Generally, financial institutions receive the data needed to calculate financed emissions on a 15-month or more time lag. This makes reporting GHG emissions along other typical general purpose reporting timelines difficult.

There are data challenges with Scope 3 emissions. There are significant concerns with data quality/availability, error margins, double-counting, and methodology that are still developing. Scope 3 emissions are based on (i) third-party data that is not necessarily complete, reliable, timely and (ii) calculation methodologies that are still developing for certain types of financed emissions. As previously highlighted, much of the data that is necessary to produce these disclosures must be gathered directly from clients and can be incomplete or unreliable or include many estimates and assumptions.

Given this situation provisions should be made for 'safe harbours' for emissions reporting and reporting Scope 3 emissions only where its deemed material.

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

AFMA supports disclosure of industry specific metrics and a common global baseline. However, it is important to note that not all metrics will be relevant to all entities, and entities should not be required to report on metrics that are irrelevant to them.

The choice of metrics for industries reflects the US market and are less relevant in other jurisdictions such as Australia. Industry metrics are encouraged rather than specified, with Sustainability Accounting Standards Board (SASB) metrics suggested as a source of industry metrics. Disclosure of industry-based metrics in line with the SASB standards should be those that are deemed material to the entity providing the disclosure.

Australia should coordinate and work with the ISSB as they move forward with making SASB mandatory in the future. The ISSB provides a list of industry specific materials as illustrative examples based on the Sustainability Accounting Standards Board (SASB) and plans to make content based on SASB mandatory in the future. We encourage regulators to coordinate and work with the ISSB on this effort.

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?

There is support for reporting entities providing transparent information about how they are managing climate related risks. Structured transition periods will be required for a range of specific clearly defined and bounded disclosures.

We note that transition plan disclosure is about disclosing a company's business strategy on how it is planning to navigate the energy transition. Climate risk management disclosure is separate. We draw attention to the flexibility that the ISSB provides in their draft standards where information related to a transition plan disclosure is optional.

Greater specificity of expectations, requirements, and definitions could help guide entities to prepare transparent disclosure of information. To ensure flexibility, this could be provided in the form of guidance documents, rather than regulation. Guidance could include examples of expected narrative points, such as initiatives and process improvements. It might identify activities that would be considered leading practice climate-related risk management or identify the elements that make up a robust leading practice transition plan, like carbon offset use. This would help users / investors understand a reporting entities approach to reducing emissions.

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

AFMA recommends a phased approach for disclosure reporting in Australia. Entities may need time to ensure sufficient completeness and reliability data needed to support the disclosures and build their capacity to disclose the required information - a phased approach recognises the need for initial flexibility and allows time for methodologies to mature, for greater standardisation to be developed and data to become more readily available. The assurance providers will also then have time to review reports across industries and ascertain best practice approaches.

Once the policy settings are determined, the lead time should be sufficient to enable reporting. Initial disclosure should establish a baseline while providing enough lead time for data collection and agreement on procedures.

13. 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?

Data collection infrastructure is the fundamental building block on which reporting metrics and targets will rely. Consistent disclosure standards are essential for defining what data and systems need to be put in place. From an Australian perspective, an efficient data collection infrastructure needs to be put in place which will require time and sequencing over a transition period. The current availability and reliability of data and methodologies will present a medium-term challenge. For Australia, a phased approach to adoption across entity types, sectors and/or sizes will be needed.

Structured transition periods will be required for a range of specific clearly defined and bounded disclosures. The financial services sector is dependent on its customer base being able to report information for their dependent disclosures.

As noted already, data availability remains a key challenge for banks' Scope 3 emissions reporting, as it relies heavily on the accurate reporting of their customers. In the absence of such reporting, banks will need to rely on proxy data to estimate emissions. It can also be challenging to define boundaries for value chains.

Scope 3 Climate disclosures, which are dependent on established reporting of Scope 1 emissions by clients of financial institutions. Regardless of the desire to move expeditiously, the training process along with the development of data collection systems, will take time. The financial services sector is more aware than other sectors given the volume of regulatory change it has dealt with over the last fifteen years of the enormous scale and realities of the task facing industry in making the proposed disclosure regime work.

While the analysis undertaken by APRA and five major banks in its climate vulnerability assessment related to prudential risks, there are several pertinent learnings from that exercise:

- Climate scenario analysis is an emerging and maturing discipline, with capabilities, modelling and supporting data continuing to develop.
- Most banks adopted a hybrid approach where internal subject matter expert (typically on a project basis), and external partners were used to bridge resource and skills gaps.
- Climate-related data quality and accessibility remain a challenge.
- From a transition risk perspective, inputs and estimates are essential to modelling a transition to a lower emissions economy scenario remain a significant challenge.
- For data relating to physical risk, business lending asset location and future climatic data modelling remains an area for improvement.

13.1. How and by whom might any data gaps be addressed?

Given the current data collection, infrastructure gaps and issues that need to be addressed from an Australian perspective, the current availability and reliability of data and methodologies will present a medium-term challenge.

Appropriate central accountability should be defined and developed as reporting requirements expand and smaller companies come into scope. There are opportunities for public-private collaboration to address data gaps and ensure consistency across key datasets. For example:

- Standardised Scope 3 methodologies or emissions factors could be included in NGER regulations. For example, methods and factors to calculate Scope 3 emissions from mining.
- More information from government organisations could be made available to disclosing entities, potentially from a centrally coordinated entity (such as weather patterns, impact of storm events, sea level rise, flood maps and so on).
- The frequency of government surveys (such as the Australian Energy Survey) could be increased to allow for more accurate disclosures.

13.2. Are there any specific initiatives in comparable jurisdictions that may assist users and preparers of this information in addressing these challenges?

Some examples include:

- Elements of the New Zealand approach could be adopted, where the External Reporting Board worked with banks to increase the quality of climate scenarios and underpinning data.

- The GHG Protocol and PCAF contain guidance on calculating Scope 3 emissions.
- The French Government's announcement of a Climate Data Steering Committee to advise on how to capture and create open, centralised climate data.

As highlighted previously, alignment to comparable jurisdictions would be optimal.

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?

There is a strong case for public provision of common data and other information, including methodologies and scenarios. The need to improve the availability, quality and comparability of climate-related data is recognised globally. Recommendation 4 of the NGFS Final Report on Bridging Data Gaps, highlighted the role for regulators and central banks in developing tools such as:

- Publicly available dashboards offering currently available macro data;
- Publicly available repositories of micro data; and
- Other tools to automate collection and central storage of data, for example data hubs.

AFMA is working on and looking to assist the Government in considering how such an approach may apply within the Australian context – using Australia-specific data – and would welcome the opportunity to work with the Treasury to do so. The benefits of this approach include -

- *Transparency and comparability*. A single source of truth provided by a public facility would improve transparency and comparability as entities would be reporting from a single agreed dataset. Use of common information would likewise help to allay concerns of greenwashing.
- *Simplification and ease of access*. Scope 3 emissions calculations require an entity to source data from a range of suppliers and customers across the entity's value chain. Even for large firms, this is a costly and complex exercise, and small-to-medium firms may struggle to source this information on their own. Digital reporting may provide a partial solution (see response to Question 18) but only for in-scope entities to which the mandate applies. Consolidation and provision of supporting information via a public facility would greatly assist.
- *Labour supply*. A public facility would help alleviate capacity constraint of appropriate skillsets within the Australian labour market, as in-scope entities would not need to compete for scarce talent.

Subject to being based on Australian specific data, Australia should follow internationally recognised scenarios on a sector basis rather than create unique onshore scenarios.

Scenario analysis is suited to a high-level and principles based. For example, as part of our annual climate report, we use internationally recognized scenarios from the Network for Greening the Financial System (NGFS) and the Intergovernmental Panel on Climate

Change (IPCC) to inform our measurement of the potential financial and economic impacts to the Firm from the manifestation of climate risks.

Common information may be particularly useful in several areas:

- APRA's CVA process highlighted the importance of an aligned industry approach to some aspects of climate scenario development. A key challenge is data availability in critical areas, such as insufficient data on emissions, limited reconstruction of historical data to inform future physical risk assessments, lack of Australia-specific climate projections, among others;
- National expected transition pathways for key sectors; and
- In developing options for simple, scalable, and cost-effective solutions for emissions reporting from small enterprises and households.

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?

Compared to traditional financial reporting, climate disclosures involve substantial use of forward-looking information and depend upon external parameters that are subject to uncertainty, such as climate scenarios.

Where climate disclosures are in whole or part dependent on third parties (for example, for Scope 3 emissions), banks will have to rely on information provided by those parties if available and may need to make assumptions where there may be gaps in data. There are other areas in which assumptions may need to be applied, including uncertainty around technological advancement. Many key methodologies remain under development at the global level, including accounting and reporting standards issued by the Partnership for Carbon Accounting Financials (PCAF).

A staff paper issued by the IFRS in December 2022, recommended that the ISSB provide a temporary exemption from the proposed requirement to disclose Scope 3 emissions for a minimum of one year following the effective date of IFRS S2. This recommendation recognised the challenges that many entities may not be able to provide Scope 3 emissions disclosures of sufficient quality to be decision-useful for users of general-purpose financial reporting.

While the need and urgency for standards climate-related financial disclosures is accepted and recognise that we must start somewhere. However, AFMA is concerned with the potential for a sizable increase on civil litigation that such disclosures may encourage. There are over 2200 climate change litigation cases globally, representing an exponential shift on litigation compared to ten years ago. Forward statements that are based on measures with low probability of occurrence or for which there is low confidence will fuel civil litigation. Australia has been highlighted as a particular focal point for litigation.

Safe Harbour Provision

To address these concerns, we would welcome a safe harbour provision that strikes the balance between incentivising climate-related disclosures and ensuring that the disclosures are reliable and sufficient. We recommend legislated safe harbour arrangements that prevent litigation against well intentioned and considered disclosures by preparers, such provisions are a pre-requisite to allow robust disclosures and statements. Without safe harbour protections, there is a strong risk of overly cautious statements disclosures that do not meet the needs of the market or investors.

For this reason, we advocate a 'safe harbour' provision that -

- Covers climate related-disclosures dependent on forward looking statements, information provided by third parties (e.g. for Scope 3 emissions) and/or other uncertainties such as climate scenarios or technological advancements.
- Provides clarity on the level of diligence to be taken be a reporting entity to meet the safe harbour.
- Provides clarity on the disclosures required to be made by a reporting entity (e.g. assumptions and disclaimers) to meet the safe harbour, such that the information remains useful without the reader of such information having to go through extensive descriptions.
- Recognises the ongoing development of standards and methodologies at a global level, including when key data gaps and methodologies will be solved.

Alternatively, legal certainty may be enhanced by changing the legal test from whether the reporting entity had "reasonable grounds" for making the disclosure to another measure (such as that the reporting entity prepared the information in "good faith") or providing clarity on how the reasonable grounds for disclosure test (and the related ACL assumption) apply to climate-related disclosures, including on the level of diligence required from reporting entities and assumptions to be included as part of the disclosures.

It should be noted that US law already contains a general safe harbour for certain forward-looking statements that apply more broadly than climate disclosures. There is no such equivalent in Australian common law, where the terms remain somewhat ambiguous.

In this regard, clarification could be given as to what would forms of conduct would meet these standards. For example, elements could include whether the disclosure is accompanied by meaningful cautionary statements identifying factors that could cause the statement made to differ in a material sense, or whether the disclosure also contained the assumptions used to make the statement.

As mentioned in previous responses - we support the inclusion of safe harbor provisions for disclosures related to forward looking information, including information related to Scope 3 emissions, transition plans, and scenario analysis disclosure. There is a recognition of the difficulty of calculating Scope 3 emissions (including double counting, variability in methodologies, and incomplete guidance and reporting) and the need for reliance on forward-looking information for transition planning and scenario analyses.

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

Secondary impacts on legislation, will need to be considered. These impacts include -

- The Banking Executive Accountability Regime (BEAR) and its potential successor the Financial Accountability Regime (FAR). Where and how the reporting requirements are situated may influence who exactly is the accountable executive under BEAR/FAR. Any new legislated reporting obligations should be consistent with any equivalent accountability obligation under the BEAR/FAR in terms of scope, limitations, and consequences for breach.
- Continuous disclosure obligations under the Corporations Act and ASX Listing Rules. Companies will provide updates if there is a material change to their business, and we would expect that the ASX and ASIC would provide guidance on when this relates to sustainability information.
- The Australian Competition Law and Australian Securities and Investments Commission Act each provide that a representation with respect to any future matter that is made without "reasonable grounds" is taken to be misleading. As discussed above in our answer to Question 15, these matters may require further consideration or clarification under any safe harbour provision.
- Director's & officer's fiduciary & statutory duties (such as trust & loyalty and competence duties).
- Other prudential requirements (such as CPS 229 Climate Change Financial Risks) and delegated legislation under the Banking Act & APRA regulatory guidance, ASX Corporate Governance Practice.

National and international alignment on the relevant climate-related disclosure rules and liabilities regimes to the extent appropriate, to ensure that companies (including banks operating and raising funds in multiple jurisdictions) have clarity on the rules required to meet by reporting entities and in relation to continuous disclosure and fundraising requirements in all relevant jurisdictions.

17. While the focus of this reform is on climate reporting, how much should flexibility to incorporate the growth of other sustainability reporting be considered in the practical design of these reforms?

Flexibility is an important principle, even climate sustainability reporting standards remain under development and nature-related standards are in an even more nascent state. Social issues are even more complex and difficult to measure/compare between jurisdictions. Standards need to be flexible and dynamic, however, other topics such as biodiversity and sustainability will require referencing to standards and requirements specific to those topics. For example TCFD is climate focused and generally should not be

used as a baseline for sustainability or biodiversity - that should be TFND framework which is yet to be published.

Therefore, it is appropriate to build the necessary levels of flexibility into governance structures, while the immediate focus should remain on climate-related financial disclosure.

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

Digital reporting should only be optional i.e. on voluntary basis. Digital reporting will require an additional step to convert the data for report lodgement. Depending on the complexity of reports, additional work on data transmission increases opportunity for errors.

The option to make financial reports via digital channels has been available since 2010 but has not been mandated. Mandating digital reporting for sustainability risk reporting would create a discrepancy with broader financial reporting. While digital reporting could theoretically improve comparability, this would only be for comparisons between Australian entities subject to the regime.

In the absence of a global agreement on digital reporting, Australian entities operating globally would have to prepare multiple sets of reports. This would add duplication and cost and could partially unwind the benefits of alignment to a global baseline.

There would be additional costs and time to implement digital reporting, which may be an additional level of complexity for limited benefit.

19. Which of the potential structures presented (or any other) would best improve the effectiveness and efficiency of the financial reporting system, including to support introduction of climate related risk reporting? Why?

Option (2) better reflects international developments. An effective reporting framework for climate-related financial risks will require close integration of expertise in both financial reporting and climate risk. If, as envisaged by Question 17, sustainability reporting will gradually expand beyond climate-risk reporting, then this will require further extensions of expertise to cover new areas such as biodiversity.

There are several unique features of climate-related financial risk reporting that distinguishes them from traditional financial risk reporting. These include, but are not limited to:

- New conceptual considerations, such as transition and physical risk (each of which is linked to different risk typologies and possesses unique characteristics), estimating the impacts of mitigation and adaptation, and forecasting uncertainty.

- Unique data needs, such as functions to translate climate-adjusted risk into financial risk that consider the inherent uncertainties and the limited ability of the past to act as a guide for future developments.

Given these and other unique and specialised characteristics, we support the establishment of a standalone sustainability standards body. Establishing such a body on a standalone basis would allow it to develop and deepen this specific expertise over time and extend into new areas as necessary.

As a less desirable option we would look to Option (3), conditional on inclusion of appropriate expertise. This option may have the potential advantage of allowing flexibility and avoiding regulatory arbitrage and/or duplication.