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

Dear Treasury

Consultation: Climate-related financial disclosure, June 2023 consultation

Thank you for the opportunity to provide a submission on Treasury's consultation paper on mandatory climate reporting, which sets out a proposed Government position (**Consultation**).

The Australian Institute of Company Directors (**AICD**) welcomes the opportunity to comment on the development of this important policy. The AICD's mission is to be the independent and trusted voice of governance, building the capability of a community of leaders for the benefit of society. The AICD's membership of over 50,000 reflects the diversity of Australia's director community, comprised of directors and leaders of not-for-profits, large and small businesses and the government sector.

The AICD sees Treasury's proposals as a key step towards an effective climate disclosure framework which incentivises organisations to make high quality, comparable and useful climate disclosures. We support strong alignment of the Australian climate reporting standards with those recently issued by the International Sustainability Standards Board (IFRS S2).

Critically, the complexity and potential impact of this "once in a generation change in corporate reporting"[1] should not be underestimated. Treasury's proposals will require material changes to the Corporations Act and financial reporting framework, which will have consequences which need to be carefully managed.

We note the current Consultation has been subject to an abridged comment period, and with limited detail provided to stakeholders on the specific mechanics to give effect to the stated policy intent. Whilst we appreciate that the current focus is on communicating the Government's overarching position, it is critical that the relevant legislative amendments and new climate standards are drafted with a clear view of their impact on the overall corporate reporting and liability framework.

Without an adequate consultation period, including with technical experts, being factored into the legislative drafting timetable, there is a risk of unintended consequences arising, and the policy objectives of the proposals being undermined.

[1] ASIC Chair's CEDA State of the Nation Conference speech dated 13 June 2023.

With the above in mind, we provide our perspective on Treasury's proposals. These comments have been drafted with a view to giving effect to the stated policy intent, and have been informed by engagement with AICD members, legal experts and other peak bodies.

1. Executive Summary

1. The AICD supports the Government's proposal to limit certain forms of enforcement action to regulators in the first three years of the regime (Transitional Liability Relief). However, the **relief should apply for three years for each reporting cohorts** (rather than being a fixed 3-year period), to support the policy objective of allowing entities time to develop internal capabilities and capacity to meet disclosure requirements. In addition to scope 3 disclosures, we consider that **the Transitional Liability Relief should cover *all* forward-looking disclosures required under IFRS S2**, not just transition plans and scenario analysis, particularly if entities are to be supported to make as fulsome disclosures as possible. Finally, the regulatory framework should make clear that private claims cannot be commenced post the Transitional Liability Relief period for disclosures made during that time.

2. To give organisations an understanding of what is expected of them, **it is critical that the Australian Securities and Exchange Commission (ASIC) makes clear its regulatory approach to enforcement and adopts a pragmatic stance**.

3. Given the proposal to locate climate disclosures within both the Directors' Report *and* Financial Report, we consider **there is a need for modified Director Declarations and CEO and CFO Declarations (Management Declarations) for Financial Reports, and amendments to the Directors Resolution authorising the Directors' Report** - specifically:

    a. **the Directors' Report**: the Directors' Resolution authorising the issue of the Directors' Report should include a statement that the directors have complied with the climate standards on a good faith and best endeavours basis, subject to the uncertainties, judgments and assumptions set out in the report, and listing the disclosures over which assurance has been provided; and

    b. **the Financial Report**: the respective Directors' and Management Declarations should be similarly modified, reflecting the emerging nature of the disclosures, the lack of certainty regarding full compliance with the climate standards, and absence of reasonable assurance. This means that the usual, unreserved "true and fair view" declaration cannot be given.

4. Any amending legislation must **clearly state that climate disclosures need to be made on an annual basis only**. As such, half-yearly reports will not need to include climate disclosures. Treasury also needs to make clear that there is **no expectation that climate disclosures will be updated throughout the year** unless (in a listed entity's case) a Continuous Disclosure obligation is triggered. In such an instance, the Continuous Disclosure regime's financial materiality test applies. To that end, we strongly support Treasury's proposal that the ASX issue guidance to provide clarity to the market.

5. **The Government should clarify which disclosures are mandatory, and which disclosures are subject to an organisation's materiality assessment**. For the latter category, entities that consider, but ultimately conclude that disclosures are not necessary because they are not material, may wish to explain their process and basis for that conclusion.

6. We are concerned that Cohort 3 would capture too many entities, relative to jurisdictions such as the EU, and that the compliance burden would be excessive for organisations which are likely to have a limited climate impact. As such, **we recommend a significant lifting of relevant thresholds or, alternatively, less onerous disclosure requirements be applied to Cohort 3 reporting entities**. **We also seek confirmation that reporting will be required on a consolidated group level**, rather than on an individual entity basis to reduce the compliance burden.

7. The AICD recommends **dedicated consultation be undertaken with the charities and NFP sector** given there appears to be limited awareness of the potential application of the reporting regime.

We set out our detailed views on the Government's proposed policy position below**.**

2. Transitional Liability Relief

The AICD supports Transitional Liability Relief as an important mechanism to provide organisations with the time to develop sufficient internal capability to navigate the significant uplift in climate reporting required by IFRS S2. However, in our view:

1. the Transitional Liability Relief should be applied to each reporting cohort, rather than being a "fixed" period of three years from 1 July 2024;
2. the Transitional Liability Relief should cover all forward-looking disclosures, and not just scenario analysis and transition plans, to facilitate comprehensive disclosure (including of quantitative information). We also consider that the Transitional Liability Relief should apply to disclosures made in key fundraising documents such as prospectuses;
3. it should be clarified that upon expiry of the Transitional Liability Relief period, private claims cannot later be brought for disclosures made within the Transitional Liability Relief period; and
4. ASIC should clarify its expectations of companies during the Transitional Relief Period and ensure they take a proportionate and risk-based approach to enforcement as organisations upskill and adjust to a complex, new reporting regime.

2.1 – Transitional Liability Relief should apply to each Cohort

The AICD strongly recommends that **a three-year Transitional Liability Relief period should apply for each of the three reporting Cohorts** – as currently drafted there may be only one year of relief for Cohort 2 and none for Cohort 3. We also seek confirmation that the relevant relief applies to the first three financial years of mandatory reporting, rather than being limited by publication date. For example, as a practical matter, Cohort 1 entities would be publishing their third year of climate reporting *after* 1 July 2027 given standard reporting cycles.

Further, IFRS S2 allows organisations to not make scope 3 disclosures in their first year of reporting. If organisations make use of this relief, they will effectively be losing an additional one year of the Transitional Liability Relief. For Cohort 2 organisations, this would mean no Transitional Liability Relief. This would create an uneven policy outcome where Cohort 1 entities, which comprise the largest and most well-resourced companies, would be the only cohort subject to the full period of liability relief, whereas the smallest and most resource constrained Cohort 3 entities, would be provided with no relief.

2.2 - Transitional Liability Relief should apply to all forward-looking disclosures and to climate disclosures in fundraising documents

We submit that **the Transitional Liability Relief should apply to all forward-looking disclosures required under IFRS S2 and not just scenario analysis and transition plans**. This is because all forward-looking disclosures suffer from a high degree of measurement and outcome uncertainty and are highly novel in the Australian market.

It would be inconsistent to apply Transitional Liability Relief to some of IFRS S2's forward-looking disclosures, and not others. Further, expanding the Transitional Liability Relief to these additional disclosures will create stronger and clearer regulatory incentives to companies to make more detailed and/or quantitative disclosure, which will help improve reporting practices and provide more useful information to the market.

For clarity, the forward-looking disclosures in IFRS S2 which are currently not explicitly included in the Transitional Liability Relief, include disclosures which often form part of the transition planning process such as:

a. anticipated effects of climate- related risks and opportunities on the entity's business model and value chain;[2]

b. anticipated changes to the entity's business model, including its resource allocation;[3]

c. how the entity expects its financial position to change over the short, medium and long term given its strategy to manage climate-related risks and opportunities, taking into consideration its investment and disposal plans, and its planned sources of funding to implement its strategy;[4] and

d. how the entity expects its financial performance and cash flows to change over the short, medium and long term, given its strategy to manage climate-related risks and opportunities.[5]

The AICD's assessment is that the types of disclosures outlined above are likely to be highly generalised, and of limited value to investors, without liability relief.

Further, to ensure a consistent policy approach and to avoid the intent of Transitional Liability Relief from being potentially circumvented, we recommend that the relief also apply to disclosures made in key fundraising documents such as prospectuses.

2.3 – Disclosures made during the Transitional Liability Relief period should be precluded from private claims made after the expiry of the Transitional Relief Period

The rationale behind providing a Transitional Liability Relief period is to give entities time to develop their climate reporting capability without heightened private litigation risk arising from the novel nature of these disclosures. This policy objective would be jeopardised if private claims *after* the expiry of the Transitional Liability Relief period could be brought in respect of disclosures made *during* the Transitional Liability Relief period.

As such, we submit that **any amending legislation should confirm that private claims brought after the expiry of the Transitional Liability Relief period cannot be made in respect of disclosures made during the Transitional Liability Relief period**.

[2] Paragraph 13 IFRS S2.
[3] Paragraph 14(a)(i) IFRS S2.
[4] Paragraph 16(c) IFRS S2.
[5] Paragraph 169(d) IFRS S2.

2.4 - Clarification of regulator expectations during Transitional Relief Period

To explain to organisations what is expected of them, **it is critical that ASIC clearly sets out its approach to enforcement during the Transitional Liability Relief period**.

Firstly, ASIC needs to be clear that enforcement will focus on disclosures made under the mandatory regime, rather than backward-looking (other than clear cases of greenwashing). The reality is that mandating ISSB disclosures will inevitably mean that organisations are disclosing much more, and differently, to how they had previously disclosed on climate. ASIC should make clear that organisations should not fear this, and that ASIC will not generally be undertaking comparative assessments of an entity's disclosures. A failure to take such a pragmatic, targeted approach risks companies prioritising consistency with previous years, rather than a fresh approach to reporting that seeks to meet shifting regulatory and investor expectations.

Secondly, ASIC needs to take a proportionate and facilitative enforcement approach to incentivise fulsome disclosure, particularly during the initial years of the regime. This means that expectations of disclosure and penalties for non-compliance are commensurate to the reporting maturity and resources of the disclosing entity. As such, civil penalty proceedings should be reserved only for egregious cases of non-disclosure or inadequate disclosure. Further, ASIC needs to reinforce that it will not be targeting organisations that make best endeavours, good faith disclosures in areas subject to high levels of uncertainty.

Thirdly, ASIC needs to provide guidance as to how organisations can disclose where there is measurement or outcome uncertainty. The ISSB recognises that many disclosures will require the use of estimates involving assumptions about possible future events with uncertain outcomes. However, the ISSB's approach that *"even a high level of measurement uncertainty would not necessarily prevent such an estimate from providing useful information,"*[6] does not recognise the significant legal risks that Australian corporations would be subject to if they "simply disclosed" as the ISSB suggests. This is because, unlike other jurisdictions such as the US, Australian courts are sceptical of disclaimers and cautionary language as a way of minimising liability.[7]

There are a number of options open to Government to manage these risks, including:

a. **Clarification of "reasonable grounds" in the context of climate disclosures.** Any such clarification would be focused on the due diligence organisations would need to undertake to establish "reasonable grounds" when making a forward-looking climate disclosure. As set out in our submission to the First Treasury Climate Consultation, we consider that legislative clarification, rather than regulator guidance, is preferable because regulator guidance is not required to be considered by a court when interpreting legislation.[8] However, in the event that the Government is not minded to provide legislative clarification, we would expect that ASIC provides clear regulator guidance (even if a court would not be obligated to consider this when interpreting the provision). We note that the current ASIC discussion on the "Reasonable Grounds test" in INFO270 is relatively high level and specifically directed at those offering or promoting sustainability-related financial products. It is critical that at the very least, ASIC clarify its expectations on how all regulated entities will be expected to show "reasonable grounds" in the context of mandatory climate disclosure.

[6] Paragraph 79 of IFRS S1.

[7] Advice by HSF, as provided to Treasury on 4 April 2023.

[8] *Acts Interpretation Act 1901*, section 15AB

b. **Providing guidance on regulator expectations as to how to disclose where there is significant measurement or outcome uncertainty**. There is significant confusion and concern as to how to make meaningful disclosures on inherently uncertain matters, without being exposed to greenwashing risk. For instance, companies wish to know how to appropriately disclose a transition plan where climate targets are partly premised on the development of technologies that are currently in a protype or testing phase, or which are not currently commercially scalable. Such guidance could explicitly reference the ISSB's implementation guidance on judgments, uncertainties and errors[9] and provide some standardised wording that corporations could apply.

3. Modified Director and Management authorisations

We note that the current proposal is for climate disclosures to be made in *both* the Directors' Report and Financial Report. It is currently unclear which specific disclosures will be located in the Directors' Report and which will be located in the Financial Report, and what level of cross-referencing will be required and/or allowed.

Existing financial reporting requirements under Part 2M of the Corporations Act are complex and interconnected. As such, modification of any part of the regime needs to be carefully managed and will require precise drafting to avoid unintended consequences. It is critical that the Government provides sufficient time for consultation on any future draft legislation, including with relevant experts with deep knowledge of the complexities of the Corporations Act, ASIC Act and related legislation/regulations.

Mandating the inclusion of climate reporting requirements within the Financial Reporting framework also has implications for the director authorisations required. The Corporations Act currently requires the following director and management authorisations for both the annual and half-year reports:

a. for the **Financial Report**, a declaration by directors that the *Financial Statements and notes,* which are subject to mandatory audit requirements, provide a true and fair view of the financial position and performance of the company, and that they comply with the Australian Accounting Standards (**Directors' Declaration**). A declaration to the same effect must also be provided by the CEO and CFO of listed entities (**Management Declaration**); and

b. for the **Directors' Report**, directors must resolve to issue the Directors' Report through the passing of a Directors' Resolution. There is no declaration that accompanies the resolution – the resolution simply resolves to issue the Directors' Report.

A failure of directors to take all reasonable steps to ensure that the entity complies with its reporting obligations and that authorised company documents are not materially false or misleading amounts to a civil penalty under sections 344 and 1308 of the Corporations Act.

Financial Reports are subject to a "true and fair view" sign-off and relate to disclosures that are primarily backwards-looking in nature. Such disclosures are also subject to well-established accounting standards which set out the procedures for the collection, measurement, verification and recording of financial information. These disclosures are also subject to external audit based on the application of an established audit methodology. The Directors' Report, which provides qualitative information about strategy and prospects which may

[9] IFRS S1, paragraphs 77 to 82.

include forward-looking statements, does not require a "true and fair view" sign off, in recognition that there is no "true" view, rather just opinion.

Treasury has indicated that some forward-looking disclosures, including scenario analysis and transition plans, will apply from commencement. These disclosures require the exercise of judgment and the interpretation of possible future states based on fast-changing external factors and inherently uncertain assumptions and information. Clear market feedback is that a "true and fair" sign off cannot be provided over such disclosures. For instance, there is no "true" view of how to interpret a scenario analysis and make conclusions of the organisation's climate resilience - there are simply various interpretations underpinned by imprecise and uncertain assumptions.

In light of this, **it is clear that a modified authorisation approach will be required.** The AICD recommends that for:

a. **the Directors' Report**, the Directors' Resolution authorising the issue of the Directors' Report should include a statement noting that the directors have complied with the climate standards on a good faith and best endeavours basis, subject to the uncertainties, judgments and assumptions set out in the report, and listing the disclosures over which assurance has been provided; and

b. **the Financial Report**, the respective Directors' and Management Declarations should be similarly modified, reflecting the emerging nature of the disclosures, the lack of certainty regarding full compliance with the climate standards, and absence of reasonable assurance. This means that the usual, unreserved "true and fair view" declaration cannot be given.

4. Liability framework

Treasury has proposed that the new climate reporting requirements would be "drafted as civil penalty provisions." It is unclear whether this means that new civil penalties will be added, or where and how these penalties will fit within the existing civil penalty regime.

In the AICD's view, the Government should clearly highlight any identified gaps in liability which would need to be addressed to maintain the integrity of the proposed reporting regime. At this stage, we are unable to see where such gaps lie. For instance, failure to disclose or inadequate climate disclosure could potentially trigger the following civil penalty provisions:

a. failure to take reasonable steps to comply with financial reporting obligations;[10]

b. failure of a financial services licensee to comply with financial services laws;[11]

c. failure to take all reasonable steps, or knowingly or recklessly authorising a materially false or misleading document to be lodged with ASIC;[12]

d. failure to take reasonable steps to ensure that information provided to a director, auditor or the ASX is not false or material;[13]

e. negligently, recklessly or knowingly failing to comply with continuous disclosure obligations (for listed entities);[14] and

[10] S 344(1) CA.
[11] S 912A(1)(c) and (ca) CA.
[12] S 1308 CA.
[13] S 1309 CA.
[14] Ss 674, s 674A, s 675 and 675A CA.

f. engaging in misleading or deceptive conduct in relation to a financial product or service.[15]

Directors are additionally subject to directors' duties, including the duty to act with due care and diligence.[16] In some cases, directors are alleged to have breached their director's duties where the company itself has breached a regulatory obligation, such as that relating to market disclosure (so-called "stepping stone" liability).

4.1 - Climate reporting is "point in time"– no liability if disclosure not amended between reporting cycles

Given climate disclosures are meant to be disclosed annually only and sit within the financial report which is a 'point-in-time' document, we recommend the Government makes clear, in both the amending legislation and the climate standards, that **the obligation is to disclose once per year, and that the document will not be updated throughout the year** (continuous disclosure obligations aside, see section 8 below). For the avoidance of doubt, the relevant law should exclude liability (including for potential misleading and deceptive conduct) for failing to update such a periodic climate disclosure. This would help alleviate liability concerns of companies and directors arising from having a document circulating in the public domain which may be out-of-date or no longer fully accurate.

4.2 - Sections 1317S and 1318 "protections" from liability

Our consultation with legal practitioners has confirmed that sections 1317S and 1318 of the Corporations Act are relatively obscure in nature and provide little protection for directors and entities in practice. Fundamentally, the relief is only available from the court after a contravention has been proven, rather than acting as a defence.

Accordingly, these provisions will offer negligible protection to directors and officers and would create no comfort to make fulsome disclosures given the inherent uncertainty of much of the proposed disclosures.

5. Timing of Disclosures

Firstly, the legislation and the Australian climate standards themselves should make clear that **climate disclosures only need to be made once a year within the Financial Report and Directors' Report,** and that there is no requirement to provide a half-year report or any update until the next year's climate disclosure *unless* a continuous disclosure requirement is triggered (see our discussion of Continuous Disclosure in section 8 below).

Clarifying this requirement is critical, as directors are concerned that they will be required to update climate disclosures every time there is a change, which could happen multiple times in a year as a result of changes to climate science, economic scenarios/projections, or regulatory developments. This concern is amplified by differing investor views on materiality which may not accord with those held by entities and their officers.

Secondly, we note that there are some disclosures that are not required to be undertaken on an annual basis. For instance, IFRS S2 allows for scenario analysis to be carried out in line with an entity's strategic planning cycle, including multi-year strategic planning cycles, rather than annually, even though disclosure of how scenario analysis informs the entity's resilience assessment, needs to be made annually. These nuances need to be reflected in implementing legislation and/or standards.

[15] S 1041H CA and ss 12DA, 12DB and 12DF of the ASIC Act.
[16] S 180 CA.

Thirdly, we have received feedback that directors (including Chairs of Audit Committees) are concerned about the compliance burden of undertaking climate disclosures at the same time as financial reporting disclosures. There is concern that the additional resources needed for climate reporting will delay the financial reports.

This is particularly likely in the first year of reporting, when entities are adjusting to the new climate disclosure regime and have not yet developed the required skills and capabilities. IFRS S1 acknowledged this issue, and allows entities, in their first reporting year, to issue their climate disclosures within a maximum of nine months following the issue of their financial statements.[17] We propose a similar approach, albeit providing a shorter period between the issue of the financial statements and the issue of the climate disclosures.

In the Australian context, we consider there are two potential options to deal with this issue (for the first year of reporting only):

a. require climate disclosures to be lodged as part of the Financial Report and Directors' Report but allow additional time i.e. from 3 months following year end to 4 or 5 months. However, this would disrupt the regular reporting cycle and market information flows; or

b. our preferred approach - allow organisations to submit their Financial Report and Directors' Report without relevant mandatory climate disclosures, and instead **allow a stand-alone climate report to be submitted within 2 months after the issue of the annual report**. Given the disaggregation from the financial reports, this stand-alone report would be limited to qualitative disclosures only (which accords with Treasury's proposed phase-in of the content of disclosures, starting from qualitative and moving towards quantitative).

We consider that Option 2 is preferable as it reduces the impact on the financial reporting regime and on market information flows, whilst allowing entities additional time to prepare for this generational change in corporate reporting.

6. Location of disclosures

The Government will need to make clear which disclosures it requires in the Financial Report, and which it requires in the Directors' Report. Given the majority of ISSB disclosures pertain to strategy and risk management issues, we consider that the Directors' Report is the appropriate place for the majority of proposed climate disclosures.

Further, given Treasury's policy objective appears to be integration of financial and climate reporting, **we recommend that Treasury consider how to reduce duplication of information and the Government provide guidance on how to integrate climate change into financial reports.**

One approach which is already built-into the ISSB Standards (paragraph 63 of IFRS S1) is to allow for disclosures to be made by way of cross-reference to another report published by the entity, provided: the cross-referenced information is available on the same terms and at the same time as the mandatory disclosures; and that the mandatory disclosures are not made less understandable by including information by cross-reference.[18] Such an approach could significantly reduce the compliance burden for organisations and duplication for users.

[17] Paragraph E4 of Appendix E of IFRS1.
[18] Paragraphs B45 and B47 of IFRS S1.

7. Different definitions of materiality and their application

We understand there are at least two relevant types of materiality that exist under Australian regulation, namely:

a. **"decision useful" materiality**, which is applied for periodic reporting under the Australian Accounting Standards and under the ISSB standards. This requires disclosures of any information if *"omitting, misstating or obscuring that information could reasonably be expected to influence decisions of primary users of general purpose financial reports."* "Primary users" are defined in the Australian Accounting Standards and under the ISSB Standards as existing and potential investors, lenders and other creditors;[19] and

b. **continuous disclosure materiality,** which is applied by the ASX when evaluating continuous disclosure reporting requirements and considering whether information had a "material effect on the price or value of the entity's securities." ASX Guidance Note 8 states that the ASX looks to the material impact on share price when considering whether the continuous disclosure obligation has been triggered, with an expected price movement of 10% or more generally being presumed to be material, and anything 5% or below being presumed to be immaterial.[20] We discuss the implications of continuous disclosure materiality in section 8 below.

The climate disclosures under the ISSB standards are subject to the "decision useful" materiality threshold. That is, organisations only need to disclose material information about the climate risks and opportunities that could reasonably be expected to affect the entity' prospects.[21] Application Guidance in IFRS S1 states that "*assessing whether information could reasonably be expected to influence the decisions made by primary users requires consideration of the characteristics of those users and of the entity's own circumstances*."[22] It is unclear how materiality through an investor or financier lens will apply to private corporations whose investors are often family members.

Against this context, we note that Treasury's position is that *"relying on judgements about materiality would not provide the level of certainty and clarity to all businesses about their obligations that comes with clear quantitative thresholds"*[23] and that *"climate-related risks, either physical or transition, will be material for the vast majority of large companies in the near term, if they are not already."*[24]

This suggests that Treasury has concluded that climate is material to *all* entities captured by the mandatory disclosure regime, and as such, organisations have no discretion to consider, and conclude, that climate is not material. Conversely, we understand that Treasury intends that only disclosure of "material" scope 3 emissions will be required.[25] This suggests that this specific metric is subject to a materiality assessment.

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[19] See footnote 4 of the AASB "Conceptual Framework for Financial Reporting."
[20] Guidance Note 8 suggests that ASX300 entities or those with a very stable or predictable earnings should consider applying a materiality threshold of 5% rather than 10%, whereas those with relatively variable earnings should stick to 10%.
[21] Paragraph 17 IFRS S1.
[22] B16 IFRS S1.
[23] Treasury's Consultation Paper at page 7.
[24] Ibid.
[25] Ibid, at page 16.

Whilst we agree that climate will have an impact on virtually all organisations, on some level, it may not be material to the investors or financiers of each company, particularly if the company is a smaller privately held company (many of which may be captured in proposed Cohort 3). In those circumstances, it is unclear what is expected of companies.

We seek **clarification on how materiality is expected to apply.** In particular, the Government should clarify which disclosures are:

a. **compulsory, notwithstanding an entity's materiality assessment**. This may include core elements of IFRS S2 such as scope 1 and 2 emissions and the identification of climate risks and opportunities; and

b. **subject to a materiality assessment**, such as current and future anticipated financial effects of climate change and opportunities, quantitative scenario analysis and transition plans and climate targets. If a company forms the view that these disclosures are unnecessary because they are not material, it may be appropriate for the entity to disclose its reasoning.

8. Continuous disclosure

Member feedback is that there is uncertainty regarding when and how revisions to climate disclosures need to be made. This is compounded by the fact that materiality definitions differ as applied by the ASX under the Continuous Disclosure regime, and as applied by the AASB and ISSB under the periodic disclosure regime (as set out in section 7 above).

The different materiality thresholds create significant confusion as to whether, when and how organisations need to act when there is a change that renders aspects of their climate disclosures obsolete or inaccurate. In particular, there is concern among some listed company directors that any change to the assumptions, inputs or methodologies underpinning climate disclosures could activate a continuous disclosure obligation, irrespective of the impact on share price (particularly given the relatively broad view on materiality taken by some investors). This issue is not dealt with by the ISSB standards, which only requires periodic disclosure.

To reduce confusion, and support consistent market practice, **we strongly support Treasury's proposal that the ASX issue guidance on the intersection between climate disclosures and continuous disclosure obligations**. More specifically, we recommend that:

a. both the Australian version of the climate standard and the implementing legislation make clear that organisations need to make climate disclosures on an *annual basis only*, and that there is no requirement to update the climate disclosures until the next reporting cycle, unless the Continuous Disclosure threshold is triggered;

b. the ASX confirms that continuous disclosure obligations continue to be subject to the existing materiality thresholds and provides guidance on how to manage those obligations in the climate context; and

c. ASIC confirms the above when setting out its enforcement approach to climate reporting (see section 2.4 which discusses regulatory enforcement approach).

9. Addressing data gaps

It is critical that Government uses the Transitional Liability Relief period to work with industry to resolve key data and methodology gaps and uncertainties. Specific areas include: the calculation of emissions for scope 3 disclosures (including financed emissions); definition of time horizons when making forward-looking disclosures; where to source and how to apply scenarios for scenario analysis; and requirements for, and how to ensure, connectivity between

climate disclosures and financial statements.

Regarding scope 3 emissions disclosures, there is considerable concern about the regulatory compliance burden on smaller entities which fall within the value chain of Cohort 1, 2 and 3 entities, as well as larger entities' ability to rely on the data of small, resource-constrained entities within their supply chain. Government should consider avenues to streamline the process of how disclosing organisations make information requests to those within their value chains. Smaller entities will also need to be provided with support and guidance as to how to respond to such information requests, and how to go about collecting the necessary data.

Regarding scenario analysis, we note that the First Treasury Climate Consultation raised the possibility of creating an authority responsible for providing information for use in climate-related financial disclosures in Australia, which could include the provision of agreed scenarios for scenario analysis. The AICD strongly supports the creation of such an authority.

Regarding connectivity between climate disclosures and financial statements, given Treasury requires that certain climate disclosures will be set out in the financial statements, guidance needs to be issued which provides practical examples of how organisations can connect their climate disclosures and financial disclosures, and expectations for disclosures in the financial statements. Current market practice is that such disclosure in the financial statements is rare.[26]

To this end, we note that the International Accounting Standards Board (IASB) is undertaking a project to explore whether and how companies' financial statements can provide better information about climate-related risks. In July 2023, the IASB reissued education material originally published in November 2020 which provides some examples illustrating when IFRS Accounting Standards may require companies to consider the effects of climate-related matters.

In Australia, the AASB and AUSB published a Joint Bulletin in April 2019 which also provided examples of how climate change may carry through to the financial statements. Given the significant developments that have taken place since April 2019 including the introduction of the ISSB standards, we strongly recommend that the AASB update this Guidance. The Government also needs to ensure adequate resources are allocated to the AASB to provide the education and support needed to uplift organisations' skills and capabilities in this regard.

10. Assurance

Treasury is proposing that reporting entities will be required to undertake scenario analysis and make transition plan disclosures from commencement, without mandating assurance over these disclosures until the second disclosing year.

In the absence of mandatory assurance, brief cautionary language should be incorporated into disclosures to ensure that investors and other market users are clear as to the limitations of that information, and that legal liability is correspondingly limited. The proposed amended Director and Management authorisations may be one way of giving effect to this suggestion (see section 3 above).

Scaling up assurance from limited to reasonable will require significant upskilling within the assurance profession. In addition, audits can only proceed when the preconditions for assurance engagements are satisfied. Under current assurance standards,[27] this requires that

[26] Research by the AASB and AUASB released in December 2022 found that in 2021 only 10.5% of all ASX-listed companies made climate-related disclosures in the notes to their financial reports. See Roger Simnett and Jean You (2022) AASB- AUASB Research Report: Climate-related disclosures and assurance in the annual Reports of ASX-listed entities, at page 10.

[27] ISAE 3000 (Revised) and Non-Authoritative Guidance on applying ISAE3000 (Revised) to Sustainability and Other Extended External Reporting (EER) Assurance engagements.

the underlying subject matter is relevant, complete, reliable, neutral, and understandable. This may be difficult to establish where there are significant measurement and outcome uncertainty underpinning many of the required climate disclosures. We recommend that further support and guidance is provided to companies to ensure they satisfy the preconditions for audit. The forthcoming issue of the International Audit Standards Board (IAASB)'s Sustainability Assurance standard is also likely to assist to clarify expectations and establish a common baseline (subject to jurisdictional adoption).

11. Scope

11.1- Breadth of reporting entities

The AICD supports a phase-in approach which requires large emitters (under NGERS) and corporations to disclose first. The AICD also **seeks confirmation that reporting will be required on a consolidated group level**, rather than on an individual entity level, in order to reduce the compliance burden.

Whilst we support the definition of Cohorts 1 and 2, we have concerns about the breadth of Cohort 3, which we understand will capture approximately 20,000 entities and is significantly broader than reporting thresholds proposed by the EU.[28] Mandatory climate reporting will require a significant uplift in current reporting practices that will be a significant challenge for Cohort 1 entities - many of which have been at least partially reporting under the TCFD framework for several years – let alone Cohort 3 entities, many of which have never undertaken climate reporting.

For Cohort 3 entities, the compliance burden is unlikely to be commensurate with the expected benefit of climate reporting, particularly considering the substantial resources needed to undertake complex disclosures such as scope 3, scenario analysis and to prepare an evidence-based transition plan. If too many relatively unsophisticated entities are caught, there is likely to be poor disclosure practices at best, widespread non-compliance at worst. Consequently, we consider that **the revenue threshold for Cohort 3 should be increased to $100 million**, consistent with the approach taken to modern slavery reporting, with other relevant thresholds being correspondingly increased. To avoid scope creep, we also suggest that the thresholds be indexed to inflation. Alternatively, following the first three years of reporting of the Cohort 1, there may be value in a statutory review to consider the desirability of extending the scope of reporting beyond Cohort 2.

11.2- Application to charities and not-for-profit organisations

The AICD is concerned about the implications for non-Australian Charities and Not-for-Profits Commission (ACNC) registered Not-for-Profit (NFP) organisations which would be captured by the regime as a consequence of the reporting thresholds being based on Part 2M Reporting Entities definitions.

This is because, whilst NFPs which are registered with the ACNC are carved out of climate reporting as they do not report under Part 2M of the Corporations Act, NFPs which are not registered with the ACNC, are required to disclose under Part 2M of the Corporations Act, and are therefore captured.

[28] Being organisations with over EUR 20 million in total assets, a net turnover of EUR 40 million and/or 250+ employees.

To put this in context, whilst a December 2017 ACNC review found that there are 60,000 charities registered with the ACNC, it was estimated that there are at least 257,000 NFP organisations in Australia.[29] While many of these NFPs would be established under state laws, there are still a significant number of larger NFPs that are companies limited by guarantee under the Corporations Act, and are meeting 2M reporting obligations.

The AICD understands that there is limited awareness in the NFP and charities sector of if, and how, the proposed climate reporting regime may apply. Further, the ISSB standards have been developed with commercial entities and the needs of their investors in mind. Accordingly, we **strongly recommend that the Government undertake a separate consultation with the NFP and charities sector** to consider: whether it is appropriate that the regime applies to them; and if so, on what basis; and whether sector-specific support is needed.

12. Australian alignment with IFRS S2

We look forward to future AASB consultation on the content of the Australian climate standards. As stated in our submission to Treasury's first climate consultation, the AICD supports alignment of the content of disclosures to IFRS S2 for greater comparability to the global baseline. As such, we consider that **Australia should, to the extent possible, have minimum deviations from IFRS S2**.

Treasury's Consultation Paper appears to have proposed several deviations from IFRS S2, including prescribing that scenario analysis be undertaken in respect of at least two scenarios including one aligned to the *Climate Change Act,* and advising that quantitative scenario analysis would be mandated by "reporting end state." It is also worthwhile considering whether the commercially sensitive information exclusion set out in IFRS S1 which currently only applies to the disclosure of sustainability-related opportunities, would extend to other metrics, such as the disclosure of Internal Carbon Prices.

Notwithstanding the general policy objective of minimum deviation from the ISSB standards, given the breadth of the proposed Cohort 3 relative to other jurisdictions, there may need to be an adjustment of the content of obligations to ensure they are not subject to overburdensome disclosure requirements. To be clear though, per our comments above, we would recommend a significant narrowing in the scope of proposed Cohort 3.

If and when Cohort 3 entities are required to report, the AICD recommends they be subject to a more limited range of disclosure requirements, such that the more complex and resource intensive obligations (such as quantitative disclosures of financial effects, quantitative scenario analysis and advanced metrics such as Internal Carbon Price and remuneration) are excluded. In effect, this would be taking a similar approach to that taken by the AASB when applying Simplified Accounting Standards to Tier 2 and Tier 3 reporting entities.

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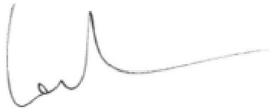
[29] See Review of Australian Charities and Not-for-profits Commission (ACNC) legislation (2017) and the Australian Charities Report, 9th Edition.

13. Next steps

We hope our submission will be of assistance to Treasury in this important and timely work. If you would like to discuss any aspects further, please contact Christian Gergis, Head of Policy at cgergis@aicd.com.au or Anna Gudkov, Senior Policy Adviser at agudkov@aicd.com.au.

Yours sincerely,



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