CEF Position Statement on Treasury's Climate-related Financial Disclosure Exposure Draft Legislation

Nishtha Aggarwal, Financed Emissions Analyst
9 February 2024

Climate Energy Finance applauds the Government’s move to establish common disclosure requirements for climate-related financial risks and opportunities for Australian companies. Delay is the enemy of climate science and, given we lost a decade under the previous Federal Government, we are more than a decade behind leaders in Europe. We applaud the draft legislation’s focus on materiality, substance and speed, rather than delay and perfection. The new disclosure requirements will drive a common baseline of transparency and comparability in emissions reporting and transition planning, starting with the largest, best resourced corporates who have the most material impact.

We would welcome additional measures to ensure disclosures are underpinned by the principles of information completeness, cross-sector comparability and integrity. The added dimension of ‘directionality’ in terms of driving Paris-aligned transitions is critically important, and we look forward to the release of science-aligned sector decarbonisation pathways and a credible sustainable finance taxonomy also aligned with the climate science, both due for release in CY2024.

We show broad support for legislating the following:

- **Climate statements** that include **scope 3 emissions** will drive transparency in value chain emissions and highlight where the risks are most material. This will, for example, expose the greenwash used in propping up methane gas as a ‘transition fuel’ whereby >90% of the sector’s emissions are exported scope 3. The **focus on materiality** in risks and opportunities, especially for group 3 entities, is also welcome and we expect that scope to widen over time to account for unforeseen and emerging risks.

- **Consolidated reporting** into a single ‘sustainability report’ will make information more accessible compared with the current disparate and disaggregated approach to corporate sustainability disclosures. We look forward to standards being developed around transition plan disclosures which should include setting the science-aligned direction of travel, e.g. disclosing current scope 3 emissions as well as the standard that dictates how much and how fast emissions need to be reduced by. This will drive Australian corporate climate disclosures to meet international financial institutions requirements.
- **Director’s declaration** of their opinion on whether the statements are in accordance with the Corporations Act, including whether climate statements are in compliance with the relevant sustainability standards. This should be caveated by a ‘best endeavours’ clause using all currently known information, leaving room for improvement as rules and practices are enhanced with better understanding. As Treasury notes, the Director’s declaration will complement “the existing liability framework under the Corporations Act and Australian Securities and Investments Commission Act 2001 (Cth) which includes director’s duties, misleading and deceptive conduct provisions, and general disclosure obligations. This is appropriate to ensure directors engage fully with climate disclosure obligations and to support investor confidence in the information disclosed.”

- **Modified liability** that provides temporary relief from litigative threats outside of those raised by the corporate regulator (ASIC). This will reduce the fear that drives greenhushing, allowing corporates a three-year period of adjustment to the new disclosure requirements and investing in improving the quality of those disclosures over time, especially as it relates to the most uncertain parts of a climate statement, i.e. scope 3 emissions and scenario analysis. It allows corporates to learn by doing over time. “Roughly right” will keep activists and lawyers at bay whilst still allowing global investors the information and comparability they need.

- **Phasing** - we endorse the three-tiered phase in approach which requires larger Australian companies to have to report first, leveraging their comparatively larger balance sheets to invest in improving data availability across the market, before group 3 has to begin reporting three years later.

We offer the following insights and/or suggestions to improve the effectiveness of this legislation in driving its stated outcomes:

- As noted by Treasury, the **International Sustainability Standards Board** (ISSB), in June 2023, released standards that are considered to be the global baseline for climate-risk reporting. Making significant departures from ISSB when developing and adopting the Australian standard reduces interoperability, and therefore also reduces the attractiveness of inbound global capital as investors overseas grapple with a different, and potentially weaker, Australian standard. It also imposes additional effort on Australian transnational investments in having to comply with both the domestic and offshore standard. It would be prudent from a climate finance perspective to have the Australian standard follow and support the ISSB as closely as possible.

- **Climate resilience assessment requirements** should be extended from two to four scenarios, with the additional scenarios being required to reflect higher warming scenarios. This would motivate businesses to better understand the risks at higher warming intervals and, therefore, act to limit their exposure and the likeliness of this outcome occurring. But, we do advocate for guidance centred on the IEA Net Zero Emissions by 2050 1.5°C alignment scenario, to prevent gaming of the system by cherry-picking alternative less credible scenario providers, reducing comparability and transition credibility.
● Additional sector-related disclosure guidance, especially rules for industry on scope 3 emissions, would improve comparability of the information that global investors require for capital allocation decisions both within Australia and globally. Investors need things to be roughly right and sectorally comparable, as opposed to precisely wrong.

● The introduction of the language around “asset owners” is potentially confusing and we would encourage the Government to clarify reporting thresholds for fund managers based on assets under management (AuM), which is more appropriate than a revenue figure for example. We also urge clarification on whether reporting is required at the fund manager level or at the fund level, the latter being much more beneficial in terms of reducing information asymmetry and allowing markets to function optimally.

● Limited assurance of sustainability reports on scope 1 and 2 emissions disclosures from 1 July 2024, with assurance being phased in for all climate disclosures made from 1 July 2030 onwards. We suggest that assurance of scope 3 disclosures and scenario analysis could be brought forward to align with the time when the modified liability clause expires (i.e. 2027 as currently proposed), and that all assurance must be done in the public interest rather than against weak standards.

*Contributing editors: Tim Buckley, CEF*