

16 February 2023

Corporations Branch
Market Conduct Division
Treasury
Langton Cres
Parkes ACT 2600

By email: climatereportingconsultation@treasury.gov.au

Dear Sir/Madam,

Consultation Paper – Climate-related financial disclosure

Thank you for the opportunity to comment on the Consultation Paper.

IPA commends Treasury in its issue of the Consultation Paper, which addresses the pertinent areas that would provide much-needed certainty to enable entities in their plans for implementing the impending climate-related financial disclosures (CFD).

The Consultation Paper is a considered document that contains proposals that are practical and consistent with the reform principles. IPA, therefore, supports many of the proposals and offers the following comments:

- IPA supports the phased approach of the initial mandatory application of CFD to large entities and financial institutions for the 2024-25 financial year. In terms of determining which entities should initially apply mandatory CFD, the criteria need to align with existing financial reporting frameworks of the Australian Accounting Standards Board and regulators (refer to our response to Questions 2 and 3 in Attachment 1 for our suggested phases for implementing CFD).
- Significant simplification and relief from specific aspects of CFD (eg Scope 3 emissions and scientific and scenario analyses) should be permitted for some entities (eg small-to-medium enterprises) where the proposals are deemed onerous.
- For the disclosed information to be relevant, reliable, timely, comparable and verifiable, the information must be independently assured by assurers who have the knowledge and expertise in CFD.
- To facilitate the application of CFD requirements and minimise additional compliance and regulatory burden and costs:
 - Climate-related requirements should be aligned to those of the ISSB standards so as to achieve credible and verifiable disclosures that are comparable to other jurisdictions
 - Where possible, terminologies (such as materiality) that are used for both financial reporting and climate reporting should be the same and

- Periodic reporting of CFD should be in the existing location for disclosing such similar information in the directors' report as part of an operating and financial review required under the Corporations Act, or in another section of the annual financial report that is reserved for climate reporting and sustainability reporting.
- IPA does not have a preference for any of the proposed structures for developing, making and monitoring climate and sustainability-related standards. IPA supports a structure where the staff and the boards have the necessary CFD/sustainability reporting technical expertise to draft, deliberate and approve the standards for issuance.

Further details on our comments above and response to the specific questions in the Consultation Paper are in Attachment 1

If you have any queries with respect to our comments or require further information, please contact me at vicki.stylianou@publicaccountants.org.au.

Yours faithfully



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About the IPA

The IPA is one of the three professional accounting bodies in Australia with over 50,000 members and students across 100 countries. Approximately three-quarters of our members either work in or are advisers to the small business and SME sectors.

ATTACHMENT 1 – IPA’s response to specific to Consultation Paper questions

Question 1: What are the costs and benefits of Australia aligning with international practice on climate-related financial risk disclosure (including mandatory reporting for certain entities)? In particular:

- 1.1 What are the costs and benefits of meeting existing climate reporting expectations?**
- 1.2 What are the costs and benefits of Australia not aligning with international practice and in particular global baseline standards for climate reporting?**

Sustainability reporting, for which climate-related financial disclosures (CFD) is a component, is an area of increasing demand in Australia and internationally. The demand stems from users of an entity (which includes an entity’s investors, customers and regulators) seeking credible and comparable information on sustainability reporting. The benefits of CFD are to provide decision-useful information to users about the financial risks that an entity face from climate change and provide regulators with information on how an entity manages such risks. Accordingly, aligning Australian practices with international practices on climate-related financial risk disclosures is a must in order to achieve credible and verifiable disclosures that are comparable to other jurisdictions. The costs of not doing so would diminish Australia’s standing of being at the forefront of standard-setting and reporting. This may in turn result in Australian entities being less competitive in their commerce and trade, as markets are likely to place a price on entities that do not report climate-related financial risk information on a timely and/or adequate basis compared to similar entities in other countries that do.

The costs of initially meeting the climate reporting expectations for all entities would be significant, particularly for small-to-medium enterprises (SMEs), as SMEs would not currently be reporting or assuring climate-related information. SMEs would need to allocate substantial resources to acquire the necessary skills and systems for their reporting. However, once CFD is embedded in an entity, the benefits would likely outweigh the costs of their disclosures over time.

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

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

and

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

- 3.1 What size thresholds would be appropriate to determine a large, listed entity and a large financial institution, respectively?**
- 3.2 Are there any other types of entities (that is, apart from large, listed entities and financial institutions) that should be included in the initial phase?**

IPA’s position is that a phased approach is the only practicable approach to enable SMEs to comply with the mandatory disclosure requirements. We are of the view that determining which entities should initially apply mandatory climate disclosures needs to align with existing financial reporting frameworks of the Australian Accounting Standards Board and regulators. Our preferred phases are:

- Phase 1 – Initial mandatory application to large entities and financial institutions for the 2024-25 financial year, with the option for other entities to elect to apply the disclosure requirements if they are ready.
- Phase 2 – Mandatory application to Tier 1 (other than those in phase 1) and Tier 2 entities as determined under AASB 1053 *Application of Tiers of Australian Accounting Standards* for the 2025-26 financial year. Additional guidance and simplification to reduce the scope and breadth of reporting where possible should be developed.
- Phase 3 – Mandatory application for small entities (such as AASB’s proposed Tier 3 entities) with significant simplification in disclosure requirements. The effective date should align with that of the AASB’s Tier 3 reporting requirements.

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

- 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?**
- 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?**

IPA supports aligning Australia’s climate reporting requirements with those of the ISSB as a prudent approach to achieving comparable disclosures with other jurisdictions, as the ISSB’s remit is to set the global baseline for sustainability reporting. Additionally, in February 2022, the AASB committed to using the ISSB standards as a foundation for setting the equivalent Australian requirements.

Nevertheless, whilst international alignment of climate reporting is important, the disclosure requirements need to incorporate other Australian requirements (such as the National Greenhouse Energy Reporting legislation for greenhouse gas emissions) to reduce the burden of reporting. The requirements also need to be scalable to different entity types and sizes.

Question 5: What are the key considerations that should inform the design of a new regulatory framework, in particular when setting overarching climate disclosure obligations (strategy, governance, risk management and targets)?

In November 2022, the Australian Government proposed Treasury Laws Amendment (Measures for Consultation) Bill 2022¹ that provides the AASB and AUASB with the functions to develop and formulate sustainability reporting and assurance standards, and the Financial Reporting Council to have strategic oversight and governance functions over the two Boards’ sustainability standards functions. Consistent with IPA’s support for the proposed Bill, IPA also supports a similar framework for climate reporting obligations with legislation setting out (at a minimum) the details of the applicable entities, the location of any reporting requirements (eg in the annual report), and requirements to follow prescribed standards for CFD. Our support is on the basis that the existing framework is robust, workable and enforceable.

Question 6: Where should new climate reporting requirements be situated in relation to other periodic reporting requirements? For instance, should they continue to be included in an operating and financial review, or in an alternative separate report included as part of the annual report?

IPA supports the periodic reporting requirements that minimise any additional regulatory burden and costs. IPA, therefore, supports the existing location for disclosing such similar information in the directors’ report as part of an operating and financial review required under the Corporations Act, or in another section of the annual financial report that is reserved for CFD and other sustainability reporting.

¹ Treasury Laws Amendment (Measures for Consultation) Bill 2022: sustainability standards – Exposure Draft and Explanatory Material (issued Nov 2022)

Question 7: What considerations should apply to materiality judgements when undertaking climate reporting, and what should be the reference point for materiality (for instance, should it align with ISSB guidance on materiality and is enterprise value a useful consideration)?

To facilitate the application of the disclosure requirements in the annual report, IPA is of the view that where possible, terminologies that are used for both financial reporting and climate reporting should be the same. This is consistent with the ISSB's recent decision to remove material judgements with reference to 'enterprise value' and instead to use the same definition of materiality as in IFRS accounting standards.

Question 8: What level of assurance should be required for climate disclosures, who should provide assurance (for instance, auditor of the financial report or other expert), and should assurance providers be subject to independence and quality management standards?
and

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

For information to be useful for users to assess the entity's climate-related risks and opportunities for making decisions about the entity, the disclosed information must be relevant, reliable, timely, comparable and verifiable. To achieve this:

- The information must be capable of being independently assured by assurers who have the knowledge and expertise in CFD. IPA is of the view that CFD are similar to other specialised areas for which traditional accountants and auditors may not have expertise. However, their disclosures and assurance rely on the use of experts in the relevant areas. Consequently, CFD should be subject to independent assurance, conducted by assurers (such as financial report auditors and/or other experts), and are subject to independence and quality standards.
- The disclosure requirements and/or their assurances should ideally commence at the same date/phase. However, given the pace of ISSB's development and issuance of sustainability standards, a transition period of one year may be appropriate for certain areas of disclosure and/or assurance. Where an entity applies the one-year transition, the entity must disclose that fact and the reasons why there is a delay in complying with the disclosure requirements.

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

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

IPA supports the requirement to report Scope 1, 2 and 3 emissions including the use of any relevant Australian emissions reporting framework for large entities and financial institutions in phase 1 of implementing sustainability standards. However, relief from specific aspects of the Scope 3 emissions and scientific and scenario analyses should be permitted for some entities where the proposals are deemed onerous. The relief can be for SMEs in Phases 2 and 3 of implementation (refer to Questions 2 and 3 above for IPA's suggested phases).

Question 11: What considerations should apply to ensure covered entities provide transparent information about how they are managing climate related risks, including what transition plans they have in place and any use of greenhouse gas emissions offsets to meet their published targets?

The disclosure of an entity's transition plans is useful for users of the report and ensures that an entity is in the process of meeting the necessary disclosure requirements by the applicable date. Consequently, an entity should be required to disclose its transition plans in the intervening reporting periods leading up to the operative date of the disclosure standards. Where the entity is unable to disclose its transition plans, the entity must disclose this fact along with explanations as to reasons for not being able to do so.

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

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

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

and

Question 14: Regarding any supporting information necessary to meet required disclosures (for instance, climate scenarios), is there a case for a particular entity or entities to provide that information and the governance of such information?

For CFD to be consistent, comparable and verifiable across entities and over time, an entity must have the capability and/or resources to invest in staff to acquire the necessary skills and systems to capture, measure and prepare disclosure reports that comply with the requirements, and auditors having the necessary skills and assurance frameworks. The pace of sustainability standards development and the limited pool of practitioners with CFD expertise will exacerbate the capability and data challenges even for large entities that may currently be disclosing some form of CFD.

These challenges are more pronounced for entities and practitioners in the SME sectors, for the following reasons:

- This sector would not currently be disclosing or assuring CFD. This contrasts with large entities that are already reporting some form of CFD and would have staff, systems and resources that can be adapted to implement the requirements of the draft standards. Similarly, large audit firms that are already providing some form of assurance on the disclosed information can adapt to future assurance frameworks.
- Whilst there may be a delay in CFD for SMEs in phases 2 and 3 (as per IPA's suggestion in Question 2), all entities will be indirectly affected by the implementation timeline of entities in phase 1 – as the phase 1 entities will require climate-related information from entities (including SMEs) in its supply chain.

The capability and data challenges can be lessened by the establishment of an authority (as proposed in Question 14) to provide not only the supporting information necessary to meet the required disclosures but also provide the data itself, where possible. IPA does not have a preference as to whether the authority responsible for providing the information is a standard-setter or a scientific body, so long as the authority has the expertise to do so.

Question 15: How suitable are the ‘reasonable grounds’ requirements and disclosures of uncertainties or assumptions in the context of climate reporting? Are there other tests or measures that could be considered to ensure liability is proportionate to inherent uncertainty within some required climate disclosures?

IPA supports the use of ASIC’s existing approach that forward-looking statements must be made on ‘reasonable grounds’ to requirements and disclosures of uncertainties or assumptions in the context of climate reporting. Other suitable provisions that could be considered to ensure liability is proportionate to the inherent uncertainty of the CFD is the ‘safe harbour’ provision that protects company directors from personal liability for insolvent trading.

Question 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?

IPA has no comments in addition to those stated in the Consultation Paper.

Question 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?

Whilst IPA agrees with this reform on CFD, the reform should be as flexible as possible to incorporate the ever-expanding sustainability reporting topics, as CFD is a limited perspective of the broader sustainability reporting. The reform, as a minimum should include the future topics that the ISSB is considering in the short and medium term, such as biodiversity, human capital, and human rights.

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

IPA is of the view that, given the advances in technology, there is a role for digital financial reporting in its lodgement and to aid better analyses for decision-making. However, digital financial reporting is an area that has been in development for a number of decades, and yet there are no definitive Australian guidance/standards in this area. Consequently, whilst we support the use of digital reporting in principle, analyses of the reasons for the lack of impetus and what has changed would enable the medium to achieve its intended purposes.

Question 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?

IPA offers the following views on the potential structures for developing, making and monitoring climate and sustainability-related standards:

- Each of the proposed structures² has its advantages and disadvantages, as outlined in the Consultation Paper.
- IPA supports a structure where the staff and the boards have the necessary CFD/sustainability reporting technical expertise to draft, deliberate and approve the standards for issuance.

² The Consultation Paper proposes the following three potential structures:

Structure 1 – Confirm AASB as the entity responsible for developing, making and monitoring climate and sustainability-related standards

Structure 2 – Establish a separate sustainability standards board and

Structure 3 – Reform existing financial reporting bodies into a single flexible entity.