Action now for mandatory climate reporting in Australia

Treasury's second climate consultation significantly expands the reporting scope

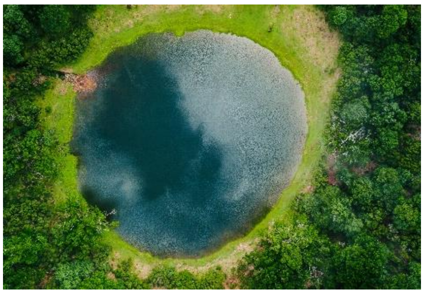
On 27 June 2023, the Federal Treasury released a consultation paper outlining its finalised proposals for the implementation of mandatory climate-related financial disclosure requirements in Australia. In summary:

- Mandatory climate-related financial disclosures will be required, starting in 2024-2025 and phased in to the 2027-2028 financial year for entities meeting the prescribed size thresholds
- **Majority of entities (including privately held entities) reporting under Chapter 2M of the Corporations Act 2001** and all entities reporting under the *National Greenhouse and Energy Reporting Act 2007* (NGER) would be required to report for 2027-2028 and later financial years
- Disclosures are expected to be closely aligned with the International Sustainability Standards Board (ISSB) Standards, with Australian equivalents to be set by the Australian Accounting Standards Board (AASB) considering Australian-specific requirements
- Disclosures are to be included in an entity's directors' report and financial report
- Assurance to be phased in over a four-year period for each reporting entity, with the scope and level of assurance increasing over that period.

"The consultation paper [...] is the next step in delivering the Government's commitment to ensuring Australia's large business and financial institutions provide more information and greater transparency on how they are responding to climate change and contributing to the net zero transformation."

The Hon Dr Jim Chalmers MP – Treasurer of Australia

Background



Climate change poses significant risks to Australian entities, encompassing both physical risks associated with the impact of climate change and transition risks arising from policy, regulatory, and technological changes aimed at mitigating climate change. Disclosure of these risks and opportunities arising from transitioning to low carbon economy is crucial for effective risk management at individual entity and systemic levels.

Recognising the importance of transparency and accountability of this matter, the Australian government committed to implementing standardised, internationally-aligned reporting requirements based on the final standards issued by the ISSB. These requirements would cover areas such as governance, strategy, risk management and metrics and target including greenhouse gas emissions.

Treasury initiated its second consultation seeking views on proposed positions for the detailed implementation and sequencing of standardised, internationally-aligned requirements for disclosure of climate-related financial risks and opportunities in Australia.

Phased timeline for climate disclosures

The mandatory climate-related financial disclosures would be implemented in a phased approach, commencing in 2024-2025 and reaching its 'end state' for 2027-2028 and later financial years.

Entities reporting under Chapter 2M

The phased approach to entities reporting under Chapter 2M[1] of the *Corporations Act 2001* applies to entities that meet at least **two of the following criteria** for the year shown:

Group	First year of reporting	Meets two or more of these thresholds		
		Employees	Consolidated assets	Consolidated revenue
1	2024-2025	More than 500	$1 billion or more	$500 million or more
2	2026-2027	More than 250	$500 million or more	$200 million or more
3	2027-2028	More than 100	$25 million or more	$50 million or more

'Controlling corporations' NGER entities reporting under Chapter 2M

Regardless of size thresholds, importantly, the requirements will apply from the 2024-2025 financial year to **all** entities reporting under Chapter 2M of the *Corporations Act 2001* that are also registered as a 'controlling corporation' reporting under the *National Greenhouse and Energy Reporting Act 2007 (NGER)*, where the entity exceeds the publication threshold[2] used by the Clean Energy Regulator (CER) to determine which emissions data to report publicly. From 2027-2028, all controlling corporations that also report under the *Corporations Act 2001* would be required to publicly report climate-related financial disclosures.

[1] Corporations Act 2001, Chapter 2M

[2] Publication thresholds is based on whether the CER publishes emissions data about reporters. For 'controlling corporations' data is published if corporate totals have combined scope 1 and 2 GHG emissions equal or greater than 50 kilotonnes $CO2^{-e}$ and for 'reporting transfer certificate holders' data is published if a facility has GHG emissions of 25 kilotonnes $CO2^{-e}$ or more; production of energy of 100 terajoules or more; or consumption of energy of 100 terajoules or more

Phase-in of assurance requirements

Assurance requirements for the climate-related financial disclosure information would also be subject to a phased approach, with each group subject to a multi-year increase in the scope and level of assurance provided from an entity's first year of reporting.

Treasury propose that financial auditors would lead climate disclosure assurance engagements, supported by technical climate and sustainability experts when required, whilst always respecting independence considerations.

Reporting content

On 26 June 2023, the ISSB issued its first two IFRS Sustainability Disclosure Standards, IFRS S1 *General Requirements for Disclosure of Sustainability-related Financial Information* (IFRS S1) and IFRS S2 *Climate-related Disclosures* (IFRS S2). The consultation paper proposes that the ISSB's IFRS Sustainability Disclosure Standards be used as the basis for the mandatory Australian requirements, initially focused on close alignment with IFRS S2.

Treasury have clearly indicated that an underlying principle behind the reforms is that of alignment with international reporting practice. The proposals contained in the Treasury consultation are broadly consistent with the requirements and transitional approaches of the ISSB's Standards. For example, in relation to governance, Treasury propose disclosure of an explanation of whether (and how) climate-related performance metrics are factored into executive remuneration, which largely aligns to the requirements outlined IFRS S2:6(a)(v).

Whilst consistent with the ISSB's standards, Treasury has outlined some proposals to specifically consider the Australian environment, as set out below.

Scenario analysis – quantitative disclosures

Qualitative moving to quantitative scenario analysis by end state

From commencement reporting entities would be required to disclose information to help users understand the basis of scenario analysis undertaken including methodology, limitations and critical assumptions and to undertake qualitative scenario analysis at a minimum. By end state, quantitative scenario analysis would be required.

Scenario analysis – future state

Climate resilience assessments against at least two possible future states

When selecting scenarios, one of these must be consistent with the global temperature goal set out in the Australian *Climate Change Act 2022*[3]. The paper illustrates the Government's commitment to reduce emissions by 43 per cent by 2030 and to net zero by 2050 as another possible future state.

Metrics and targets – industry metrics

Industry-based metrics for Australian industry specific sectors

While IFRS S2 provides the industry-based guidance derived from SASB Standards in its Accompanying Guidance, Treasury expects that there would be industry-based metrics available that are appropriate for Australian industry-specific sectors by the end state of phased reporting timeline, in consultation with members of industry sectors.

Assurance timeline

First year reporting

Limited assurance of scope 1 and 2 emissions

Reasonable assurance over governance disclosures

Second year reporting

Reasonable assurance scope 1 and 2 emissions

Limited assurance scope 3 (specific)

Third year reporting

Reasonable assurance scope 1, 2 emissions and other climate disclosures

Limited assurance scope 3 (full)

Beyond year three

Reasonable assurance on all climate disclosures

[3] Which is to contribute to 'holding the increase in the global average temperature to well below 2°C above pre-industrial levels and pursuing efforts to limit the temperature increase to 1.5°C above pre-industrial levels'.

Metrics and targets – reporting period
Use Scope 3 information of a different reporting period Extending the IFRS S2's relief to use information from a reporting period that is different from the entity's reporting period in specific circumstances, the paper proposes to allow that material scope 3 emissions disclosures made could be in relation to any one-year period that ended up to 12 months prior to the current reporting period.

Treasury considers that further guidance and progress on data challenges is necessary to support broad adoption of best-practice disclosure in the medium term. The Government is currently developing a Sustainable Finance Strategy which will look in more detail at options and priorities for addressing key data challenges and providing clearer guidance in these areas including scope 3 estimation methodologies, interpretation of materiality, boundaries for estimation, etc for Australian reporters.

Location, frequency and timing

The consultation paper proposes that entities would include climate-related financial disclosures in their annual report prepared under Chapter 2M of the *Corporations Act 2001*. Entities would be required to include the disclosures across their:

Directors' report	OFR	Financial report

For listed entities, the disclosures would form part of the operating and financial review (OFR) included in the directors' report, but there would be an option of producing and referencing a separate report for metrics and targets disclosures. There would be specific requirements mandated in how the climate-related financial disclosures would be presented, including an 'index table' to allow users to easily find relevant information.

Timing of reports will remain consistent with existing requirements under the Corporations Act

The reporting timetable would be consistent with the existing requirements under the *Corporations Act 2001*, with disclosing entities, registered managed investment schemes (and also registrable superannuation entities from 1 July 2023) to report within three months of the end of the financial year and other entities within four months of the end of the financial year. There is no discussion of a deferral of first year reporting to not align with the preparation of the annual report, as is permitted under the IFRS S1:E4.

Liability and enforcement – A "modified liability" framework

Given the fact that climate disclosures may require positions to be taken on inherently uncertain matters and thereby potentially leave company directors open to liability for misleading or deceptive conduct, concerns were raised about the applicability and operation of the current liability framework to forward-looking statements as well as the class action regime in place in Australia's legislative environment.

Specifically in the case of scope 3 emissions, there are concerns that significant data availability issues do not allow for confident and accurate reporting of these emissions. There is a risk that without appropriate protections for directors, entities would provide overly cautious disclosures that do not meet the needs and expectations of the market or investors.

The proposed modified liability framework offers protection to directors in relation to climate-related disclosure requirements, scope 3 emissions and forward-looking statements

In response, Treasury have proposed a transitional "modified liability" framework to balance the importance of disclosing decision-useful information with appropriate protections for reporting entities. The climate-related financial disclosure requirements are proposed to be drafted as civil penalty provisions in the *Corporations Act 2001*. The application of misleading and deceptive conduct provisions to scope 3 emissions and forward-looking statements would be limited to regulator-only actions for a fixed period of three years from the commencement of the regime.

Next steps

The consultation paper is open for comment until 21 July 2023, with enabling legislation exposed prior to being implemented in line with the initial commencement date of 1 July 2024. Following the consultation, detailed disclosure standards will be formally established by the AASB, with consultation expected in the second half of 2023, with a view to finalise standards in Q2 of 2024.

Key resources

Treasury consultations

- **Second consultation** (June 2023)
- **Initial consultation** (December 2022)

iGAAP in Focus

- **Sustainability reporting: ISSB publishes first IFRS Sustainability Disclosure Standards** (June 2023)

IFRS® Sustainability Disclosure Standards

- **IFRS S1** *General Requirements for Disclosure of Sustainability-related Financial Information*
- **IFRS S2** *Climate-related Disclosures*

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