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**Climate-Related Financial Disclosure Consultation Paper**

The Australian Energy Council ('AEC') welcomes the opportunity to make a submission to Treasury's consultation on *Climate-Related Financial Disclosure* ('Consultation Paper').

The Australian Energy Council is the peak industry body for electricity and downstream natural gas businesses operating in the competitive wholesale and retail energy markets. AEC members generate and sell energy to over 10 million homes and businesses and are major investors in renewable energy generation. The AEC supports reaching net-zero by 2050 as well as a 55 per cent emissions reduction target by 2035 and is committed to delivering the energy transition for the benefit of consumers.

The AEC continues to support the development of an Australian climate-related financial disclosure framework that is aligned with international best practice via the International Sustainability Standards Board ('ISSB') standards. A robust disclosure framework will help ensure Australia's transition to net-zero is as transparent and efficient as possible.

The publication of this Consultation Paper and the final ISSB Standards represent a significant evolution in the final design of Australia's climate disclosure rules. Treasury has opted for an ambitious phased implementation approach that will see significantly more entities captured from 2024-25 (Group 1) than what was originally flagged.[1] This was not anticipated by the AEC.

The AEC is not opposed to this broader scope but emphasises it has resulted in many entities being captured who, up until now, have had no engagement with this subject matter. Additionally, even for those that are engaged, this is a rapidly evolving area of law – as evidenced by the simultaneous publication of the ISSB Standards. Given this, a three-week consultation period has been problematic for the AEC and its members.

This is raised upfront because new and comprehensive reforms like this often have unintended outcomes that are not fully discoverable in a three-week period. The AEC is hopeful that the transition arrangements proposed will mitigate some of these risks for captured entities.

That aside, the AEC generally supports the proposals made in the Consultation Paper. Our overarching message is one of proportionality: the level of reporting required should be proportionate to the materiality of the emissions and how closely related an entity's core business is to material climate risk. It

[1] While the first Consultation Paper invited stakeholder feedback on the inclusion of other entities, it stated: "*as a starting point in Australia, it is proposed that standardized climate-related financial disclosure requirements would initially apply to certain listed entities covered by the Corporations Act 2001*".

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is pleasing to see that proportionality has been included in Treasury's reform principles and the AEC believes it should be enshrined in the eventual legislation.

Treasury should bear in mind that there is some tension between the economy-wide action needed for Australia to meet its climate targets, and the requirement for individual corporate reporting. These tensions are especially pronounced in the electricity sector where companies, although independent in their corporate structure and commercial activity, must coordinate through the Australian Energy Market Operator ('AEMO').

AEMO planning is central to the transition of the electricity sector. The commissioning and decommissioning of generation assets are planned through AEMO with there being tight rules particularly around when a plant can retire. The culmination of AEMO's planning is the Integrated System Plan ('ISP') which maps various decarbonisation pathways for the electricity sector. The AEC would expect that electricity reporting entities can refer to the ISP for scenario analysis.

## Purpose of Climate-Related Financial Disclosure

During the stakeholder roundtables and briefings for the first consultation, Treasury stated that the objective of these reforms was to facilitate the efficient allocation of capital for Australia's transition to net-zero. This was not mentioned explicitly in the first consultation paper, though it did note the "immediate focus of this reform is improving transparency for investors" with respect to publicly listed companies.

Treasury has now presented additional objectives through its listing of "reform principles", namely:

- Better management of climate risks across the financial system.
- Improving transparency of the financial system to better inform investors.
- Ensure Australia's international reputation is maintained through a credible financial disclosure regime.

The AEC considers the first and third of these principles to be somewhat beyond previous expectations. Nevertheless, it is not opposed, and suggests these reform principles be embedded in the legislation to maintain transparency of the intent and scope.

## Reporting Entities

*That all entities that meet prescribed size thresholds and that are required to lodge financial reports under Chapter 2M of the Corporations Act 2001 (Cth) (Corporations Act) would be required to make climate-related financial disclosures.*

Treasury has proposed to majorly expand the Group 1 reporting entity classification in response to stakeholder feedback. From the AEC's interpretation, the newly proposed thresholds will result in some inadvertent capture of electricity generation facilities.

This is because electricity generation facilities, regardless of their emissions, automatically trigger the NGER publication threshold through section 24(1AF) of the *National Greenhouse and Energy Reporting Act 2007* ('NGER Act'). Consequently, some electricity generation facilities that are 100 per cent renewable are being captured under Group 1.

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There are also some retailer entities that appear to be inadvertently captured through their operation of low emitting, cogeneration plants. These entities fall short of the Group 1 financial criteria and would not meet the NGER threshold except for the automatic triggering of electricity generation facilities (despite this being peripheral to their predominant operation as a retailer).

For these entities, the AEC considers the administrative burden of being classed as Group 1 is not proportionate to the materiality of their emissions or their exposure to material climate risk. While the scheme does also seek to compel disclosure of opportunities, these are unlikely to be material given their business size and focus.

This outcome, presuming it is unintended, can probably be remedied through including a specific emission threshold which the AEC understands is intended to be 25,000 tonnes per annum.

### Phasing of Reporting Requirements

Treasury's expanded scope for reporting entities has increased the importance of a fair and reasonable transitional period and modified liability. Some entities have had no engagement with this subject matter and did not participate in the first consultation stage due to the impression it was targeting publicly listed companies.

## Materiality

*Principles of financial materiality would apply.*

The AEC agrees with the proposal to contain materiality to financial materiality via alignment with the ISSB benchmark. We note there have been some stakeholder proposals for non-financial or double materiality to be included. The disclosure framework should be built with enough flexibility to ensure Australia can smoothly adapt to international practice as it evolves.

In this sense, the AEC highlights that metrics required to fully leverage the value from double materiality have not been agreed or are immature. The forthcoming Taskforce on Nature-related Financial Disclosures (TNFD) final recommendations will add appropriate guidelines and robustness to these efforts. Until these are finalised, understood and implemented widely, it would be premature to require full double materiality application, especially given the additional administrative burden it would place on smaller, less sophisticated reporting entities.

## Governance

*From commencement, companies would be required to disclose information about governance processes, controls and procedures used to monitor and manage climate-related financial risks and opportunities.*

Disclosure of governance arrangements is important to provide transparency and accountability over whether investor and shareholder expectations are being met. However, Treasury's proposal for reasonable assurance from commencement is challenging and will require operational guidance beyond the ISSB about what level of specificity is needed.

For those companies with no prior experience in governance disclosures, the AEC is concerned this learning curve would be a steep and costly one with increased exposure to legal risk. Sufficient time and additional transitional relief to allow smaller entities and those less familiar with governance reporting and assurance requirements should be considered to reduce regulatory burden.

## Scenario Analysis

*From commencement, reporting entities would be required to use qualitative scenario analysis to inform their disclosures, moving to quantitative scenario analysis by end state.*

While the phasing from qualitative to quantitative makes sense, it is not clear from the Consultation Paper and ISSB Standards what the regulatory expectations are for companies with potentially material climate risks, but minimal experience in climate scenario analysis. On the one hand, the ISSB says:

> *This means that—with all else being equal—the greater the entity's exposure to climate-related risks or opportunities, the more likely it is the entity would determine that a more technically sophisticated form of climate-related scenario analysis is required.*[2]

Then on the other hand:

> *For example, if an entity has only just begun to explore the use of climate-related scenario analysis to assess its climate resilience, it might be unable to use a quantitative or technically sophisticated approach to climate-related scenario analysis without undue cost or effort.*[3]

The Consultation Paper does not address this tension other than to say the reporting entity must consider its experience of reporting and its exposure to climate-related risk. For those new entities with material climate risk, the AEC favours a grace period that scales with proportionality – in other words, the transitional period is there to build capability, and following that transitional period, the level of capability built should be proportionate to the level of material climate risk.

*From commencement, reporting entities would be required to disclose climate resilience assessments against at least two possible future states, one of which must be consistent with the global temperature goal set out in the Climate Change Act 2022.*

Greater clarity over the meaning of climate resilience is needed, as the Consultation Paper only refers to it in the context of international developments. For entities that are not internationally trade exposed, like electricity generation, changes in other countries' emissions pathways are not directly consequential.

The ISSB Standard is more general, defining climate resilience as an entity's strategy to climate developments and uncertainties. This does invite some political sensitivities for electricity generation facilities given uncertainties predominantly relate to the ability of governments to implement their electricity policies and renewable energy targets. Furthermore, the climate trajectory of electricity generation facilities is influenced by decisions from other market participants and AEMO, such as a delay in plant closure.

While entities can report on these forward-looking uncertainties in general terms, they face political and commercial sensitivities in providing the detailed contingency analysis that investors might expect. The ISSB Standards do provide for omission in limited circumstances where there is commercial sensitivity, though this still invites a degree of legal risk for reporting entities if the regulator interprets differently.

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[2] IFRS S2, 'Climate-Related Disclosure', June 2023, B4.

[3] IFRS S2, 'Climate-Related Disclosure', June 2023, B6.

With respect to scenario reporting, the AEC is broadly comfortable with Treasury's reasoning to opt against mandating both scenarios. Providing some flexibility allows for industry-specific and Australia-specific challenges to receive attention.

This is particularly important for entities in the electricity sector where the existence of a system operator (AEMO) means electricity companies operate in unique circumstances. Electricity sector companies cannot operate wholly independently from each other – e.g. a coal-fired power station cannot announce it is closing tomorrow simply to meet a company carbon target. The commissioning and decommissioning of generation assets are instead coordinated and planned through AEMO, which is forecast through its Integrated System Plan. As such, the AEC expects many electricity companies to use scenarios from the ISP to meet the disclosure regime.

The AEC supports prescribing the other scenario to the Paris Agreement temperature goals, as this ensures alignment with international best practice. However, as far as taking into account Australian circumstances, this prescription could be aided through the Federal Government or Treasury producing a carbon budget that shows the type of NDC aligned with 1.5 and below 2 degrees pathways.

Doing so would give investors greater confidence in the scenario analysis because it would provide a baseline reference point for each scenario. Furthermore, it would help remove some of the uncertainty for reporting entities with respect to how the Federal Government's current NDC aligns with the Paris Agreement temperature goals and unknowns about the 2035 NDC, which is not expected to be announced until late 2024.

## Transition Planning

*From commencement, transition plans would need to be disclosed, including information about offsets, target setting and mitigation strategies.*

Treasury will need be to be mindful about how sophisticated transition plans must be as this will determine the level of regulatory burden. For some illustration, two AEC members – AGL and Origin – already publish Climate Action Transition Plans as part of the 'Say on Climate' initiative.[4] These plans are detailed and subject to limited assurance, but also had the benefit of a longer lead time to prepare.

Given the day one nature of this proposal, there may be ways to reduce the burden on reporting entities:

- Allow reference to AEMO's ISP as a whole-of-system transition plan for companies with electricity generation assets.
- Allow reference to government policy (e.g. NSW Electricity Infrastructure Roadmap, QLD Energy and Jobs Plan).
- Enforcing an emissions threshold (likely 25,000 tonnes per annum) to exempt electricity generation companies with low climate risk.
- Consistent with international best practice, full transition plans should be required not more than once every three years with updates or revisions only when material changes in corporate strategy or the electricity market occur. Similarly, once reasonable assurance has been undertaken on a particular transition plan, that audit finding should have future application until there is a material change in corporate strategy or the electricity market.

[4] Origin Climate Transition Action Plan 2022. AGL Climate Transition Action Plan 2022.

*From commencement, all entities would be required to disclose information about any climate-related targets (if they have them) and progress towards these targets.*

The AEC supports this requirement, though it seems to duplicate the existing voluntary *Corporate Emissions Reduction Transparency* ('CERT') report. The AEC's view is that Treasury should work with the Clean Energy Regulator to wind down the CERT scheme in favour of the Climate Disclosure Rules, which are broader in scope, mandatory for captured entities, and have a more enduring reporting regime.

Consistent with earlier comments, the AEC notes the ability to report on progress towards a target is uniquely difficult for electricity generation because of the whole-of-industry element of electricity emissions reduction. That is, it is harder for individual companies to predictably and gradually forecast and reduce a plant's emissions over time because it is impacted by the actions of other market participants. For example, unexpected outages, unseasonal weather, fuel supply issues, market dynamics and technical limitations all influence the life of a plant, which can contribute to fluctuations in its emissions trajectory.

## Risks and Opportunities

*From commencement, entities would be required to disclose information about material climate-related risks and opportunities to their business, as well as how the entity identifies, assesses and manages risk and opportunities.*

It is hard to comment on this proposal given specific information about the types of risks and opportunities entities are expected to disclose will be provided in the Australian Accounting Standards Board ('AASB') consultation stage. Repeating a concern raised earlier, there may be some commercial sensitivity regarding the publication of opportunities depending on how it is defined – e.g. if entities are expected to disclose contingency analysis or strategic planning relating to long-term solutions to the energy transition. The ISSB Standard does provide some omission for commercial sensitivity, but again this is in limited circumstances and still invites some legal risk.

Depending on how the AASB defines opportunities, ASIC guidance may be helpful in this area.

## Metrics and Targets

*From commencement, scope 1 and 2 emissions for the reporting period would be required to be disclosed.*

The AEC supports this requirement to the extent that Scope 1 and 2 emissions are already reported through the NGER Act. NGER data is subject to the Clean Energy Regulator's oversight, which can commission an audit if there are concerns about accuracy. Noting this, the AEC does not consider there is good reason to also require market-based accounting methods for Scope 2 emissions by end state. Any inclusion of a market-based method should only be required once it is mandatory and embedded in NGER reporting practices.

Aside from that, there is an issue with respect to the timing of NGER reporting (31 October deadline) and annual reporting, which varies depending on the structure of the entity as public (30 September) or private (31 October). Additionally, any NGER data will need to go through a reasonable assurance process before it is included in a financial statement. To resolve the time lag, the AEC suggests that entities be allowed to submit the most up-to-date data they have at the time the financial report is due, and then provide any true-up later once assurance is complete.

Lastly, Group 1 entities will be required to provide reasonable assurance of Scope 1 and 2 emissions from 2025-26 onwards. Consistent with the materiality threshold, the AEC considers this should only apply to the components of Scope 1 and 2 emissions which are material to climate risk rather than applying the NGER reporting threshold of all emissions sources that constitute 2.5 per cent of total emissions or more. Requiring entities to assure all components of their emissions will add significant time and expense, as well as absorb audit capacity, for little overall benefit.

*Disclosure of material scope 3 emissions would be required for all reporting entities from their second reporting year onwards. 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.*

Some electricity companies do have material Scope 3 emissions, though this usually comes through activity that is ancillary to generation (e.g. retailing commercial gas). The AEC is comfortable with that disclosure to the extent it is material.

However, for some electricity generation companies "only", Scope 3 emissions are often very small. For clarity, the AEC would welcome Treasury or the AASB producing some guidance or benchmark about what might constitute *material* Scope 3 emissions (presumably an absolute number or range).

Treasury should also consider the value in requiring limited assurance from 2025-26 for Group 1 entities. Noting that auditors are still building competence in the field of climate disclosure, and the interrelated nature of Scope 3 emissions reporting (fully accurate disclosures require all upstream and downstream entities to have a deep understanding of their emissions), very few auditors will be able to reliably assure any entities' submitted Scope 3 emissions. It may, therefore, be preferable to allow for voluntary or self-assurance in the initial year (2025-26) or until such time as appropriate sophistication in Scope 3 emissions measurement and reporting develops.

## Industry-Based Metrics

*By end state, reporting entities would be required to have regard to disclosing industry-based metrics, where there are well-established and understood metrics available for the reporting entity.*

The ISSB has so far opted against mandating industry-based metrics because they were seen as complicated and difficult to define. Treasury has indicated its intent to not mandate requirements beyond the ISSB standards to ensure Australian companies are not unfairly burdened compared to their international competitors.

The AEC agrees with this direction, though notes the ISSB is still working to internationalise industry-specific metrics and some companies may choose to voluntarily disclose industry-based metrics in anticipation of future compliance.

The disclosure of industry-based metrics can be an important differentiation point for companies seeking to attract global investment. However, there are also some risks for Australian electricity companies if the ISSB eventually adopts operational emissions intensity as an industry-based metric. This is because other countries have higher shares of hydro and/or nuclear energy in their energy mix, which makes it seem like they are reaching sectoral carbon targets much faster than Australia.

If this metric is adopted at some future point, Treasury should ensure there is discretion for electricity companies to explain Australian circumstances.

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## Reporting Framework

The AEC agrees that climate-related disclosures must be published in the annual report, both the director's report and financial report, but encourages Treasury to:

- Allow cross-referencing to prior annual reports or other sustainability reporting standards to avoid information repetition and lengthy annual reports.
- Exempt subsidiary entities from stand-alone climate reporting where subsidiary data has been reported in an Australian parent's consolidated report. To reduce duplication, the subsidiary entity should instead be required to reference the parent entity's reporting.
- Consider the inconsistency between lodgment due dates for ASIC and NGER reporting. In addition to the time misalignment mentioned earlier, some entities choose to report their financial statements early to maintain good governance and send early signals to the market. This creates added complication with respect to meeting the level of assurance within the timeframes. The AEC believes the best solution here is to allow entities to submit the most current data they have at the time the financial report is submitted, and then provide any true-up later once assurance is complete.
- Ensure there are no inconsistencies between existing ASIC reporting requirements and the proposed publication requirements. For example, making mandatory climate disclosures in annual reporting publicly available may be confusing for private companies given the current practice requires paying an ASIC fee to access their annual reports.
- Delay digital reporting requirements to avoid additional burden on reporting entities.

## Assurance

While the AEC agrees with the intent to scale assurance requirements over time, we remain concerned about audit access and capacity. The proposed thresholds will see many more entities included than previously anticipated. Adding to this is that Group 1 entities – the largest financial and/or emitting companies – will demand significant time and resources, presumably from those auditors with the most capability.

The AEC considers there are some areas where there are good reasons to relax assurance requirements. This will have the ancillary effect of opening up audit capacity.

- Any assurance requirement should only apply to material disclosures. This is consistent with the ISSB's *materiality* 'conceptual foundation' that *an entity shall disclose material information about the sustainability-related risks and opportunities that could reasonably be expected to affect the entity's prospects.*[5] While Treasury has indicated there is an overarching materiality threshold, parts of the Consultation Paper also refer to assurance over climate disclosure requirements generally.
- Reasonable assurance of governance disclosure should be phased in from the second year of an entity's reporting.
- Reasonable assurance of Scope 1 and 2 emissions should only apply to components of Scope 1 and 2 emissions which are material to climate risk rather than applying the NGER reporting threshold of all emissions sources that constitute 2.5 per cent of total emissions or more.
- Limited assurance of Scope 3 emissions should commence from an entity's second year of required Scope 3 reporting (e.g. for Group 1 entities, this is 2026-27) or until such time as sophisticated Scope 3 emissions and reporting capability is evidenced across captured entities.

[5] IFRS S1, 'General Requirements for Disclosure of Sustainability-Related Financial Information', June 2023, 17.

While the reasons for strong assurance are easily made, Treasury should also be mindful that requiring assurance for disclosures where auditors do not have the capability and/or knowledge may inadvertently enable greenwashing. It is important that data limitations are acknowledged rather than given false authenticity.

## Liability and Enforcement

*Climate-related financial disclosure requirements would be drafted as civil penalty provisions in the Corporations Act. 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.*

Consistent with what has been said in this submission, the AEC considers the expanded scope and subsequent capturing of many new entities necessitates a rethink of whether the proposed modified liability approach is sufficient. The requirement for forward-looking statements, while supported, is inherently uncertain, particularly so for the electricity sector where emissions reduction is achieved through a whole-of-industry approach. Likewise, Treasury has acknowledged that there are currently data availability limitations with respect to Scope 3 emissions reporting. These uncertainties bring a degree of legal and reputation risk that may lead to overly cautious statements under the proposed liability framework. The AEC encourages further consultation on this proposal.

Furthermore, Treasury should clarify and/or consider that:

- There is no possibility for retrospective litigation (i.e. third party litigation cannot be taken after the three years have passed for an act or omission within the first three years).
- The three-year grace period applies from when an entity is required to commence reporting (e.g. for Group 2 entities, the three-year period starts from 2026-27).
- Modified liability for Scope 3 emission reporting should only start once the requirement for limited assurance commences (i.e. for Group 1 entities, modified liability would last from 2025-26 to 2028-29). The ending of modified liability should be dependent on reliable and established data for Scope 3 emissions being available.

Any questions about this submission should be addressed to Rhys Thomas, by email Rhys.Thomas@energycouncil.com.au or mobile on 0450 150 794.

Yours sincerely,

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