

## FairSupply's Response to Australian Government (The Treasury's) Climate-Related Financial Disclosure Consultation Paper (December 2022)

FairSupply is pleased to present this submission in response to the Treasury's request for initial input on climate-related financial disclosure. We agree that the prompt introduction of mandatory climate-related financial disclosures is an important step in Australia's transition to net zero emissions by 2050.

FairSupply is an Australian-founded, cutting-edge global ESG data provider and consultancy firm. Through world-leading proprietary technology, we provide our business and institutional investment clients with unparalleled visibility of ESG risk by quantifying greenhouse gas emissions (including Scope 3), modern slavery risks, and biodiversity loss within entities' supply chains and investment portfolios.

Our experience of working with Australian businesses provides unique insight into the challenges and opportunities associated with reporting regimes (both mandatory and voluntary). Our responses below have been limited to those areas where our actual experience enables us to provide meaningful input.

An overarching viewpoint that we advance in this submission is that, beyond consideration of existing (primarily economic) reporting requirements that large entities have under Australian financial laws, potential climate-related disclosure should also be considered in the context of existing ESG reporting legislation, most notably, the *Modern Slavery Act 2018* (Cth). Whilst there are numerous reasons that we believe justifies such an approach, first and foremost is that it will promote consistency across ESG-related reporting regimes within Australia.

### **Key consultation questions and FairSupply's response**

**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?*

#### **FairSupply's response:**

Timely alignment with international practice on climate-related disclosure will help ensure Australian businesses maintain global relevance in one of the most rapidly evolving and important areas of good corporate governance. Failing to do so will, inevitably, make Australian businesses seem backward and less-than-proactive in meeting one of the greatest challenges currently facing humanity.

For Australian businesses seeking to operate in international markets, it will also ensure ongoing compatibility and ability to compete on equal footing.

In terms of costs, companies will, of course, need to dedicate appropriate resources to compile, analyse and disclose the required information under a mandatory reporting regime. However, such costs should, through proper corporate citizenship, be fully offset by the reciprocal benefits of a more realistic picture of overall business risks (and opportunities), coupled with the significant reputational boost that entities who report thoroughly and accurately can be expected to receive. Further, aligning Australian reporting requirements with international practices would simplify reporting on climate-related financial disclosures by reducing the number of regimes business are required to report under. In the long term, this could help to manage the costs associated with reporting.

We do not consider there to be any appreciable or significant benefits in failing to align with emerging international practice on climate related disclosure, particularly in the long term. Australia should not ignore the opportunity to be towards the leading edge of such an important emerging trend in global financial reporting and accountability.

**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?*

**FairSupply's response:**

The sooner Australia moves towards a regime of regulated and mandatory climate-related disclosure, the better. We support the introduction of the first round of reporting being for FY2425, on the basis that we understand this to be considered the earliest commencement that can be practically achieved.

In terms of phasing, whilst we recognise the approach being taken in other jurisdictions (e.g. New Zealand), our primary position is that rather than having significant categories of large entities that are initially exempt, the preferable approach is to impose broad application from the outset (e.g. reporting entities are all those with annual revenue of at least \$100m – see below, including our discussion on the limitation of reporting to listed entities).

Rather than staged application to large companies operating in different industry categories, we suggest that the appropriate tolerances inherent in “phasing” can be better achieved through a considerable and appropriate degree of accommodation in relation to the quality of the reporting in the earliest (i.e. first one or two) reporting periods. Rather than an enforcement-based approach, these periods can be used as an appropriate progression for awareness-raising, capability-building, and active collaboration between private reporting entities, government, and other interested stakeholders (such as civil society groups and researchers).

**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?*

**FairSupply's response:**

We support the introduction of a simple, bright-line, mandatory reporting threshold such as the \$100m annual revenue trigger under the *Modern Slavery Act 2018* (Cth).

Such an approach will ensure a consistent scope for all sustainability-related reporting across Australia, rather than create a disjointed reporting regime depending on the element of sustainability reported on.

We note that the Consultation Paper appears to focus primarily on "*large, listed entities*" (**emphasis added**). From our perspective, the additional threshold that mandatory reporting entities be publicly listed may be an unnecessary narrowing of the scope of the proposed regulatory framework's operation. For example, it would exclude the large number of member-owned superannuation funds that are currently mandatory reporting entities under the *Modern Slavery Act 2018* (Cth). Such entities are significant from a climate-related disclosure perspective, particularly in light of the relatively large investment portfolios that they manage (and the climate-related implications of such funds management falling outside the purview of a mandatory reporting regime).

As per our response above, we have concerns in relation to a more industry-based, phased mandatory disclosure approach. In addition to the delays associated with achieving comprehensive coverage of all major Australian industries (something that is essential when considering national Net Zero goals), another major downside of this approach is the inevitable variances between the overall quality of disclosure between entities that have been

reporting since the outset compared to those who are phased-in to start in later reporting periods. Widespread coverage is more effective from the outset, provided that, as we have noted above, due consideration is given to allowing entities to 'learn and continuously improve', particularly through the earliest stages of their reporting journey.

After an initial period of 'blanket' implementation of the kind we have proposed above, depending on international trends and other current assessments of the effectiveness of the existing level of reporting coverage, it may be appropriate to consider extending mandatory disclosure to entities that do not meet an annual revenue threshold, but are nonetheless operating in recognised carbon-intensive / high-priority industries.

**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?*

**FairSupply's response:**

FairSupply supports the general alignment of climate reporting requirements to regimes that are introduced (or proposed to be introduced) in other countries and markets. Applying a global framework will streamline the internal operations required for an entity that is operating internationally to meet its obligations in multiple reporting jurisdictions. Such broad consistency will also give reporting entities opportunities to leverage and reapply successful risk mitigation or adaption approaches that are initially developed and implemented in other markets.

The ISSB standards represent an appropriate and logical touchstone for potential Australian regulation of the kind presently under consideration. However, given the speed at which regulation is moving in this area on the global stage, including the current stage of the ESG reporting proposals in the EU, the inclusion of the specific standards against which entities should report should be considered an open issue as close as practicable up to the point of the commencement of the inaugural reporting period (and, of course, should regularly be reviewed and updated beyond that point).

**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)?*

**FairSupply's response:**

Clarity in expectations is of paramount importance. Clarity is essential in relation to organisational and operational boundaries that each entity must address in reporting. For example, the difference between scope 1 and scope 3 GHG emissions is typically determined by the definition of operational boundary. (As per the discussion in Chapters 3 & 4 of the [GHG protocol](#).)

Another important area where clearly defined expectations can materially impact upon the broader reception (and acceptance) of ESG reporting legislation is in the articulation of key statutory objectives. First and foremost, a central consideration for the design of the regulatory framework should be the qualitative difference between a framework that only requires entities to accurately report climate-related risks and data, versus more expansive obligations that require an entity to take steps to actually address and mitigate climate-related risks.

Once again, on this issue, we suggest that real insight can be gained through consideration of the *Modern Slavery Act 2018 (Cth)* and the broader response to the Act's administration to date. Undoubtedly one of the most persistent criticisms of the Act, particularly amongst broader public interest groups, has been that it does not require reporting

entities to actually carry out any kind of substantive due diligence to reduce modern slavery risk. If the proposed climate-related regulatory framework is to be similarly limited in terms of only mandating reporting and disclosure, then this should be communicated with utmost clarity. To also avoid confusion as to what the regulatory framework implicitly requires, it should be a determinative factor in defining the nature and extent of all overarching disclosure obligations – whether related to strategy, governance, risk management, targets or otherwise.

**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?*

**FairSupply's response:**

We suggest that the annual reporting requirements culminate in the form of entities being required to annually lodge a standalone statement with the responsible government agency. As with the *Modern Slavery Act 2018* (Cth), all lodged statements would be made available for public review on a searchable online official register.

This approach also aligns with the practical reality that, in many organisations, the team responsible for meeting reporting obligations under this Act are often responsible for all sustainability-related reports. Providing consistency across the threshold and timing of all sustainability-related reporting requirements would help to streamline the resources and effort required by reporting entities to deliver their obligations.

We do not support an approach where disclosure obligations might be met through the inclusion of a specific part within an entity's general annual reporting under corporation law (cf: Consultation Paper at p.10). Such an approach is likely to adversely impact on the practical effectiveness of the reporting measures as a means of increasing corporate transparency and will unnecessarily complicate the process of scrutinising and comparing the approach and results of multiple entities.

**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)?*

**FairSupply's response:**

Our position in relation to the introduction of a 'blanket' reporting requirement for entities over a specified annual revenue threshold is stated above.

However, we also acknowledge that, beyond the gateway threshold for being a mandatory reporting entity, materiality considerations (including, potentially, the nature and extent of disclosure obligations) should primarily be based on the size of the emissions rather than financial considerations such as enterprise value. Again, such an approach aligns with the experience of mandatory modern slavery reporting in Australia where there has proven to be an immediate, persistent, and now almost axiomatic, expectation that entities operating in high-risk industry categories and/or geographies (e.g. apparel brands that manufacture cotton clothing in China) undertake a more vigorous approach in all areas, including risk identification, assessment and mitigation measures. Such varying materiality expectations exist notwithstanding the lack of differentiation in the Act itself.

If the ultimate intent of this reporting is to help meet the goal of net-zero emissions by 2050, then it's the size of an entity's attributable emissions, and therefore their impact on the delivery of this goal, that may be the most pressing factor. 'Financial materiality' and 'carbon materiality' should not be capable of being used interchangeably. Different industries having very different carbon profiles.

**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?*

**FairSupply's response:**

Having regard to current status of all mandatory ESG-related reporting regimes, we consider that the most practical approach may be one where the introduction of external assurance for the quantitative elements of climate disclosures is necessarily something that is phased in once the reporting regime is implemented. Again, this would involve recognition that initial reporting periods will be more about capability building, awareness-raising and resource development, rather than government enforcement.

Another option worthy of exploration is establishing assurance systems that primarily operate through the engagement of approved third-party experts to complete (or certify) the quantitative elements of an entity's disclosures.

**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?*

**FairSupply's response:**

[Research](#) has shown that for industry sectors other than energy and transport, Scope 3 emissions make up the greatest proportion of total greenhouse gas emissions. Accordingly, our recommendation is that any climate-related financial disclosures should include Scope 1, 2, and 3 emissions. This will enable all entities to obtain and disclose a comprehensive picture of their overall emissions profile, which is an essential starting point in the development of viable plans to reduce emissions.

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

**FairSupply's response:**

Our recommendation is that a common baseline of metrics be defined, and that these metrics include both quantitative measures (such as emissions in kg CO<sub>2</sub>-e) and qualitative measures (such as those aimed at assessing an entity's reported risk management systems).

**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?*

**FairSupply's response:**

We note significant efforts that are currently underway, both in Australia and internationally, to address the problem of 'greenwashing', including in the context of climate-related disclosures (most notably, entities making 'Net Zero' commitments).

In our view, the legislative development of new and additional enforcement provisions (whether civil or criminal) is largely superfluous and redundant. This is because existing legal concepts such as misleading/deceptive conduct, the criminal offence of not making false or misleading statements (including by omission) to Commonwealth agencies / officials, and the existing suite of Director's duties under the *Corporations Act* are all sufficiently robust to ensure that covered entities provide transparent information about how they are managing climate related risk.

Whilst we acknowledge there may well be room for significant improvement and refinement in this legal and regulatory space, our primary position is that the introduction of a climate-related disclosure framework should not be delayed due to a perceived need to create some kind of additional enforcement mechanism to ensure covered entities provide transparent information. Such mechanisms already exist and are available for regulators to rely upon in appropriate cases.

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

**FairSupply's response:**

We do not have any specific comment on this question beyond our response to Question 11, above.

**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?*

**FairSupply's response:**

As a provider of data that can be used to assess the full supply chain associated with an entity's procurement or investments, we specifically wish to point out the suitability of input-output methodology for quantification of Scope 3 emissions. This methodology is widely used in the research community for the calculation of carbon footprints and provides full supply chain transparency, well past an entity's direct suppliers or investee companies. See, for example, [Huang et al., 2010](#), [Malik et al., 2018](#), [Malik et al., 2021](#), , [Minx et al., 2010](#), [Wiedmann et al., 2020](#).

**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?*

**FairSupply's response:**

We do not have any specific comment on this question beyond our response to Question 11, above.

**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?*

**FairSupply's response:**

The obligations relating to the sufficiency of grounds needed for companies to justify 'future facing' statements is an area of corporate conduct that is coming under ever-increasing scrutiny by regulators and other stakeholders concerned with the overall integrity of ESG-reporting. Undoubtedly, there will be further developments, including enforcement actions relating to 'greenwashing' in Australia and/or internationally, in the period between now and when the proposed climate-related framework is introduced.

As noted above, we do not consider that the proposed climate related reporting framework should either be delayed or necessarily have to break new legal ground (in terms of the imposition of novel legal definitions and requirements) in order to be implemented with due efficacy. We consider that pre-existing concepts (including 'reasonable grounds') are sufficiently elastic to accommodate the prompt introduction of such a reporting scheme as is being considered.

**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?*

**FairSupply's response:**

As noted above, we believe that the *Modern Slavery Act 2018 (Cth)* should be carefully considered when investigating interactions with proposed climate-related reporting requirements. Modern slavery and climate-related reporting fall under the umbrella of ESG and Sustainability reporting in many organisations, and most Standard frameworks. In many organisations, reporting against these areas is managed by the same team of people, which may not necessarily be the same team responsible for more traditional forms of financial reporting (e.g. the preparation of Annual Reports).

**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?*

**FairSupply's response:**

We strongly support a flexible approach so that any reporting framework can be extended to, or operate in conjunction with, other reporting areas related to sustainability.

Based on our interactions with organisations outside of Australia, particularly in Europe, we believe that nature-related risks such as biodiversity loss will quickly rise in prominence. Introducing a streamlined reporting approach to all areas of sustainability will minimise the administrative burden for reporting entities as new expectations materialise in the global landscape.

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

**FairSupply's response:**

Our position is that digital reporting should be made compulsory for all sustainability risk reporting. Leading critiques of the quality of statements lodged by mandatory reporting entities under both Australian and UK modern slavery legislation have consistently advocated for fully searchable electronic lodgement of statements so as to facilitate ease of comparison, and maximise transparency of content (e.g. screening for holistic 'cutting and pasting' of whole statements or key parts of statements across successive reporting periods).

**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?*

**FairSupply's response:**

We consider the best approach to be **Potential Structure 2 – Establish a separate Sustainability Standards Board**. Subordinating sustainability reporting to financial reporting under a financial reporting body sends a strong signal that sustainability considerations are subordinate to financial ones. It also reduces transparency, as discussed above.

Sustainability is a broad field that includes financial, environmental, and social elements and the establishment of a separate governing body for sustainability-related standards will facilitate a consistent approach to all risks which may pose a threat to financial institutions, and to society in general.

Creating a Sustainability Standards Board could also present an opportunity to integrate modern slavery reporting, currently the remit of Australian Border Force, into this structure.