



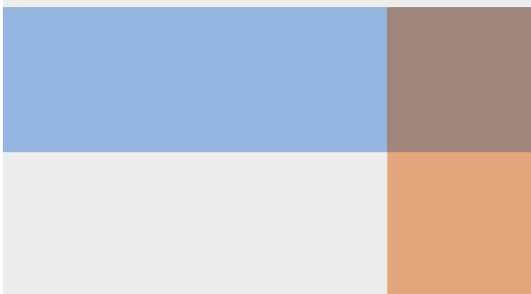
**Australian Government**  
**The Treasury**



# **Policy Impact Analysis**

## **Climate-related financial disclosures**

September 2023



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## Key terms

<b>AASB</b>	The Australian Accounting Standards Board (AASB) is an independent, non-corporate Commonwealth entity of the Australian Government that develops, issues and maintains accounting standards applicable to entities in the private and public sectors of the Australian economy.
<b>ASIC</b>	The Australian Securities & Investments Commission (ASIC) is Australia's integrated corporate, markets, financial services and consumer credit regulator.
<b>APRA</b>	The Australian Prudential Regulation Authority (APRA) is Australia's prudential regulator of banks, insurance companies and most superannuation funds.
<b>AUASB</b>	The Auditing and Assurance Standards Board (AUASB) is an independent, non-corporate Commonwealth entity of the Australian Government, responsible for developing, issuing and maintaining auditing and assurance standards.
<b>IFRS</b>	<p>The International Financial Reporting Standards (IFRS) Foundation is a not-for-profit established to develop globally accepted accounting and sustainability disclosure standards.</p> <p>The Standards are developed by their two standard-setting boards, the International Accounting Standards Board (IASB) and the International Sustainability Standards Board's (ISSB).</p>
<b>ISSB</b>	The International Sustainability Standards Board (ISSB) was established in 2021 to develop a comprehensive global baseline of sustainability disclosures for capital markets.
<b>NGER Reporting Entity</b>	An entity required to lodge financial reports under Chapter 2M of the <i>Corporations Act (2001)</i> (Cth) that is registered as a 'Controlling Corporation' reporting under the <i>National Greenhouse and Energy Reporting Act 2007</i> (Cth).
<b>Scope 1, 2 and 3 (emissions)</b>	Scope 1 covers direct greenhouse gas emissions from owned or controlled sources. Scope 2 covers indirect greenhouse gas emissions from the generation of purchased electricity, steam, heating and cooling consumed by the reporting company. Scope 3 includes all other greenhouse gas emissions that occur upstream and downstream in a company's value chain.
<b>TCFD</b>	The Task Force on Climate-Related Financial Disclosures (TCFD) was created by the Financial Stability Board (FSB). In 2017, the TCFD released climate related financial disclosure recommendations.
<b>Listed company</b>	An organisation that is publicly owned entity whose shares can be traded on a stock exchange.
<b>Unlisted company</b>	A privately owned entity.

# Executive Summary

The Government has legislated Australia's commitment to reduce emissions by 43% by 2030 and achieve net zero emissions by 2050. Financial markets will be critical in financing the substantial investment<sup>1</sup> required to meet these targets.

To appropriately price climate-related risks and opportunities, value assets and allocate capital efficiently, investors need information on climate risks and opportunities and the actions being taken by individual companies to meet their climate change targets. Climate-related financial disclosures are an important mechanism through which companies can communicate this information to investors. Effective disclosures will ensure the financial effects of climate change are routinely considered in business and investment decisions.

In 2017, the Taskforce on Climate-related Financial Disclosures (TCFD) established a global, voluntary framework for disclosing climate risks. However, while voluntary take up is increasing over time, it has been limited to companies with the most resources<sup>2</sup>. Given this, jurisdictions globally have commenced implementing mandatory climate risk disclosure regimes (for example, New Zealand, United Kingdom and the European Union). In addition, the quality of climate disclosures has not provided useful information to investors. The approach to disclosure has varied across companies and jurisdictions and disclosures have tended to be qualitative in nature.

In response, the International Sustainability Standards Board (ISSB) was formed to improve the quality of sustainability and climate disclosures in an attempt to provide more useful information to investors and regulators. The ISSB built on the foundations of the TCFD and developed more detailed disclosure standards. The ISSB standards provide a global baseline for sustainability and climate disclosure standards that will improve the identification, measurement and disclosure of climate risks and opportunities.

As part of the *'Powering Australia'* policy, the Government has committed to introducing standardised, internationally aligned requirements for mandatory disclosure of climate-related financial risks and opportunities in Australia for large businesses. This policy will ensure that Australia has a rigorous and credible climate disclosure regime. This is necessary to sustain Australia's reputation as a destination for the international capital that will be inevitably needed in the transition to net zero.

The Impact Analysis assesses three options to implement the Government's election commitment.

- **Option 1**, consistent with the approach proposed in Treasury's design consultation, would mandate climate disclosures for large listed and unlisted companies from 2024-25 financial year. These entities will be phased-in depending on their size (and split across Groups 1, 2 and 3). Entities would be required to report on their climate strategy and governance processes as well as scope 1 and 2 emissions from commencement, with scope 3 reporting being required as the reforms mature. Entities will also be required to conduct scenario analysis from commencement. Assurance requirements would also be phased in and scaled up over time to allow for capability and capacity uplift.
- **Option 1a** is a variation on Option 1 and amends the breadth of coverage of these reforms. Under this option, entities captured under Group 3 would be required to do a materiality assessment. Only where the entity has material risks, disclosure would be required in line with

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<sup>1</sup> The International Energy Agency (IEA) projects that globally, by 2030, investment of just over \$US 4 trillion per year will be needed for this transformation. Financial markets will be critical in financing this investment.

<sup>2</sup> <https://kpmg.com/au/en/home/insights/2022/10/sustainability-reporting-survey-2022.html>

the relevant Australian standard as per entities in Groups 1 and 2. Additionally, a specific 'assets under management' threshold would be applied to significant financial institutions.

- **Option 1b** is a variation on Option 1a and amends the assurance framework, not mandating a roadmap for the phasing in and scaling up of assurance requirements over time. Under this option, all disclosures in reports issued after 1 July 2030 must be assured with a flexible pathway to achieve this being set by the Auditing and Assurance Standards Board (AUASB). A modified liability regime will operate for the first three reporting years.

Treasury recommends the Government adopt Option 1b.

Treasury conducted two consultation process in developing these reforms. Our recommendation reflects the feedback received from over 200 respondents. Treasury will continue to monitor the implementation of this policy, in collaboration with the Australian Accounting Standards Board (AASB), ASIC and Australian Prudential Regulation Authority (APRA). The Government will review this policy in 2028-29, four years after climate-related financial disclosures are made mandatory. Among other things, this review will consider the operation of the coverage and assurance aspects of the policy.

All things being equal and comparing with a baseline option of continuing to operate under the status quo, under Treasury's recommended approach (option 1b), this policy is expected to add between \$1.0 million to \$1.3 million per year per entity in initial transition costs to the regulatory burden of captured entities and have a number of benefits that are difficult to quantify, including reducing the cost of capital for these entities. Costs are expected to stabilise and fall over time, resulting in ongoing costs of between \$500,000 to \$700,000 per year per firm. This is broadly in line with costs estimated for implementing the International Financial Reporting Standards (IFRS). Costs for implementing IFRS for firms in Australia have been estimated to be between \$750,000 and \$1.6 million.<sup>34</sup>

Treasury expects approximately 1800 entities will be captured and costs will vary depending on the size of the company. However, it should be noted that companies would be incurring costs for disclosing their climate risks in the absence of a new, mandatory, internationally aligned regime. This is because they are obliged under the *Corporations Act (2001) (Cth)* (Corporations Act) to disclose all material risks. Climate is increasingly considered a material financial risk for many companies. For example, disclosing climate risk under the less prescriptive Taskforce for Climate-related Financial Disclosure framework is costing between \$250,000 to \$400,000 per year per firm and provides firms with less assurance that they are adequately reporting on material risks.

Successful implementation of the mandatory climate risk disclosure regime will lead to comprehensive identification of climate-related financial risks within entities and across the economy, drive better risk management practices, improve the transparency of entities' decarbonisation strategies, and enable more accurate pricing of risks and opportunities. This will lead to a more efficient allocation of capital, aligned with the need to transition to net zero. While not accurately quantifiable, these benefits are anticipated to far outweigh the costs over the medium term.

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3 Morris, R. D., Gray, S. J., Pickering, J., & Aisbitt, S. (2014). Preparers' perceptions of the costs and benefits of IFRS: Evidence from Australia's implementation experience. *Accounting Horizons*, 28(1), 143-173.

4 Collett, P., Godfrey, J., & Hrasky, S. (1998). Standard-setting in Australia: Implications of recent radical reform proposals. *Australian Accounting Review*, 8(16), 9-17.

## Background

Climate change is increasingly driving changes in the economy, the financial system and society more broadly both in Australia and internationally. Climate change itself and the actions taken in response to it introduce risks and opportunities for Australia.

There are three broad channels through which climate change affects financial performance and stability, these can be described as:

- Acute physical risk which is the risk of financial losses occurring as a result of severe weather events, such as flooding, storms or bushfires. The magnitude of losses depends on the location of physical assets – for example, more frequent and severe flooding will have greater impact if dwellings continue to be built in low-lying flood-prone areas.
- Chronic physical risk which is the risk that persistent effects of climate change will influence the value of assets because of changes in their productivity or desirability.
- Transition risk which is the financial risks which could result from the process of adjustment towards a lower-carbon economy. Changes in markets, technology and physical risks could prompt a reassessment of the value of a large range of assets as costs and opportunities become apparent.

### Addressing climate change risks

Governments are already playing a primary role in reducing emissions and taking action to mitigate the impact of climate change, for example, by pricing externalities and providing incentives for the transition to a low-carbon economy.

By mobilizing capital and resources needed for investments in climate mitigation and adaptation the financial sector can play a complementary role in achieving these goals efficiently. The International Energy Agency estimates around 70 per cent of clean energy investment required for the transition to net zero would need to be carried out by private developers, consumers and financiers<sup>5</sup>. Most of these investments are likely to be intermediated through the financial system. From this point of view, climate change presents opportunities as well as risks to investors and the financial system.

To allocate capital efficiently, financial markets must integrate climate risks into capital allocation decisions. Investors rely on information published in annual reports and financial statements to understand risks and opportunities and in doing so, determine how to allocate their capital. Conveying climate risks and opportunities to users of general-purpose financial reports and other stakeholders thus improves market-based evaluations of the reporting entity, improving the efficiency of capital flows.

A common and important tool to manage both individual and systemic climate-related financial risks is disclosure of those risks. However, existing climate risk disclosures are often inconsistent or contain insufficient information to support decision-making. Investors also note the lack of standardisation makes disclosures difficult to compare, which impacts their decisions. This Policy Impact Analysis considers the impact of implementing a requirement for large Australian businesses and financial

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<sup>5</sup> <https://www.iea.org/reports/world-energy-outlook-2021/mobilising-investment-and-finance>



institutions to disclose their climate-related financial risks to financial markets by expanding existing reporting frameworks.

## The problem

Climate change is having an impact on the financial prospects of companies, for better and for worse. It is increasingly recognised that companies need to manage and disclose those risks. This is becoming a mainstream part of corporate governance and strategy. To do this effectively, the financial impacts of climate change need to be identified and disclosed to the market.

Physical risks are projected to increase in Australia, with CSIRO and the Bureau of Meteorology modelling suggesting there will be an increase in the frequency and intensity of heat waves and rainfall events, rising sea levels, increased acidity of oceans and decline in snow depths.<sup>6</sup> The impact of natural hazards on physical assets could lead to destruction of a firm's physical assets, lower productive capacity and output, and lower the value of a firm's financial contracts. This in turn will have a negative impact on the value of any financial portfolios that hold the asset, whether individuals or institutions. For example, a firm whose productive capacity is destroyed by severe floods and has borrowed from a bank may not be able to make interest and principal repayments, impacting the bank's balance sheet.

Transition risks are also becoming more acute as markets respond to changing consumer demands and more countries commit to policies to meet net zero targets by 2050. In this context, investors have to consider which companies and assets will have the most challenges in transitioning to net zero. Some industries will need to change business models and practices to fit within a low carbon economy. Consideration would also need to be given to those assets that lose value or become 'stranded' due to an inability to adapt to these changes. Stranded assets can lead to large (downward) adjustments in asset values, with potential implications on economic and financial stability. This has led to heightened demand from investors, regulators and firms for greater information in order to understand and respond to these risks.

These growing financial risks around climate change have led to a heightened demand for quality climate disclosures by financial markets and regulators. Many Australian businesses face significant physical and transition risks as well as opportunities stemming from climate change<sup>7</sup>. To unlock investment in emissions mitigation and climate risk adaptation, businesses and investors need to understand and price both the opportunities and risks of climate change. Poor investor understanding of climate-related risks and opportunities could lead to inefficient allocation of capital. Also, Australian firms could be less competitive in global capital markets if our climate disclosure regime did not align with international best practice.

Treasury consultation<sup>8</sup> suggests information asymmetry between firms and investors is a major barrier to efficient capital allocation. Ernst and Young's 2022 Global Climate Risk Barometer, which analysed disclosures by over 1500 companies across 47 countries (including 103 Australian companies), found that there is currently a mismatch between the depth and quality of information sought by investors and the information that firms have the capacity and willingness to provide<sup>9</sup>.

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6 Chapter 2 - Carbon risk: a burning issue – Senate Economics References Committee Report (2017):

[https://www.aph.gov.au/Parliamentary\\_Business/Committees/Senate/Economics/Carbonriskdisclosure45/Report](https://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Economics/Carbonriskdisclosure45/Report)

7 Ibid.

8 Page 5 - <https://treasury.gov.au/sites/default/files/2023-04/c2022-314397-acsi.pdf>

9 Page 5 - [https://www.ey.com/en\\_gl/climate-change-sustainability-services/risk-barometer-survey-2022](https://www.ey.com/en_gl/climate-change-sustainability-services/risk-barometer-survey-2022)

Treasury's consultations also revealed strong support for a more robust climate disclosure regime. It is critical that investors have access to relevant information about climate-related risks for prudent management of the capital they invest. Adapting to this heightened demand for quality climate disclosures will ensure Australia stays aligned with global best practice. It will also ensure that markets are well placed to fund the transition to net zero.

## Current reporting trends in Australia

As the financial risks and opportunities associated with climate change have become more apparent, investors have sought better disclosure of these risks in relation to their investments. Since the TCFD made its recommendations in 2017, jurisdictions have begun mandating TCFD-aligned disclosures. While not separately mandated in Australia, financial regulators including ASIC<sup>10</sup> and the ASX<sup>11</sup> have issued guidance that climate-related financial risks must be disclosed as part of existing obligations to disclose material risks, recommending TCFD as a framework for disclosure.

According to a 2022 survey by the TCFD, 90 per cent of users of general-purpose financial reports and other users considered climate-related disclosures in financial decision-making, with 66 per cent factoring in these disclosures when pricing financial assets<sup>12</sup>. A 2023 KPMG report into Australian companies found that out of 94 ASX100 companies that report sustainability, 88 per cent companies recognise climate as a financial risk, yet only 78 per cent are voluntarily reporting against TCFD<sup>13</sup>. This asymmetry shows that there is climate risk in the system that is not being adequately disclosed and therefore addressed. Furthermore, the proportion of companies reporting against the TCFD framework drops to 67.5 per cent of the ASX200<sup>14</sup>, and drops even further beyond the ASX200.

Even among those companies that report voluntarily, not all are reporting in accordance with the full TCFD requirements, and some entities have chosen to only partially report against the requirements.

A 2023 Australian Council of Superannuation Investors (ACSI) report<sup>15</sup> provides a sector comparison of ASX200 companies' use of the TCFD framework (Chart 1). Full reporting under the TCFD framework is not necessarily sufficient, as the TCFD does not specify the level of quantitative or qualitative detail required or disclosure of how the company identifies risks. As a result, entities are able to make broad, qualitative statements in order to comply.

As a result of the slow uptake and varied information being published, the frontier of global best practice continues to shift outward as capital markets and users of general-purpose financial reports are increasingly demanding better quality, internationally comparable disclosures. In response to this, several jurisdictions are contemplating or have already introduced mandatory requirements for large businesses to disclose their climate-related risks.

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10 <https://asic.gov.au/about-asic/news-centre/articles/asic-s-current-focus-what-are-the-regulator-s-expectations-on-sustainability-related-disclosures/>

11 Page 27 and 28 - <https://www.asx.com.au/documents/asx-compliance/cgc-principles-and-recommendations-fourth-edn.pdf>

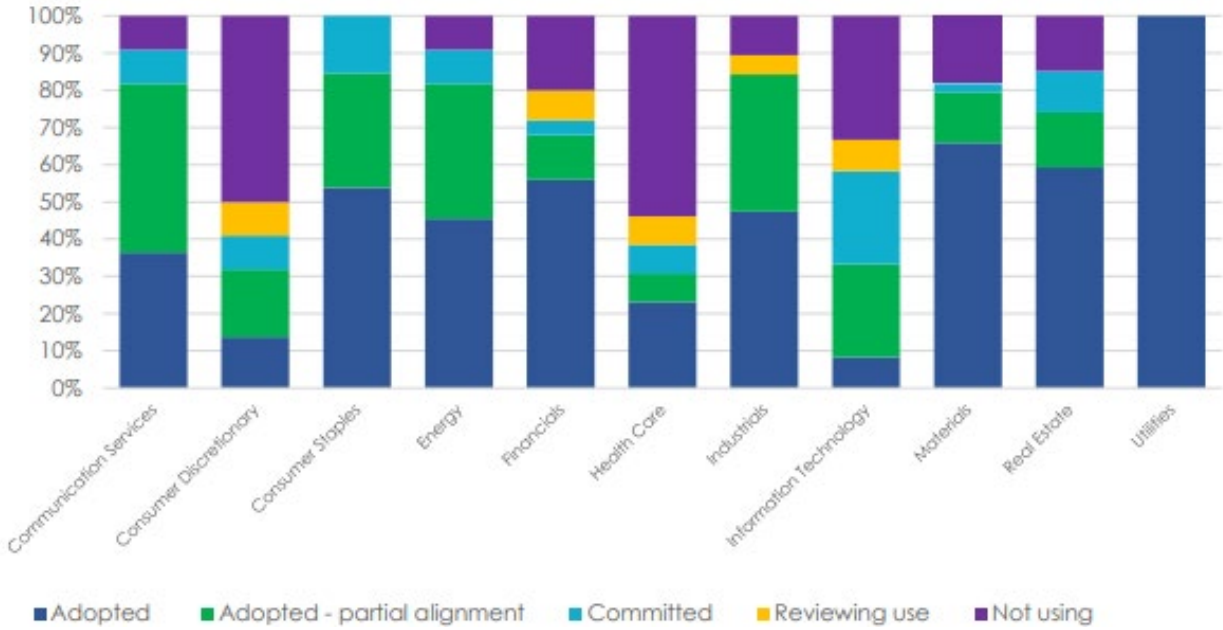
12 Page 5 – Table ES1 - <https://assets.bbhub.io/company/sites/60/2022/10/2022-TCFD-Status-Report.pdf>

13 Page 2 - <https://assets.kpmg.com/content/dam/kpmg/au/pdf/2023/australian-sustainability-reporting-trends-june-2023-update.pdf>

14 Page 6 - <https://acsi.org.au/wp-content/uploads/2023/08/Promises-Pathways-Performance-Climate-reporting-in-the-ASX200-August-2023.pdf>

15 Page 7 – Figure 2 - <https://acsi.org.au/wp-content/uploads/2023/08/Promises-Pathways-Performance-Climate-reporting-in-the-ASX200-August-2023.pdf>

Chart 1: Sector comparison of ASX200 companies' use of the TCFD framework



Source: ACSI – Climate Reporting in ASX200 Companies: August 2023

For example, both New Zealand and the United Kingdom (UK) passed legislation that made climate-related disclosures mandatory for a subset of businesses. Both New Zealand and the UK have mandated that companies report against standards that are TCFD aligned. On 2 August 2023, the UK Government announced that it would develop its own UK specific sustainability standards, based on the final ISSB standards, for companies to report sustainability-related risks and opportunities by July 2024. The United States of America (US), Switzerland and Singapore are also developing mandatory climate disclosure requirements. Singapore has recently announced that it will require listed entities to report against the ISSB climate standards, starting from 2025. Reducing information asymmetry for investors through improved climate disclosure practices remains key to ensuring Australia remains an attractive destination for global capital.

**Lack of comparability in current reporting formats**

The use of multiple frameworks, some voluntary and some mandatory, alongside different reporting formats without any benchmark for quality, means that users face a harder task in analysing sustainability information. This ultimately leads to increased costs for users and introduces inefficiencies into processes and eventually the market – leading to misallocation of capital. Below are some key issues that act as barriers for comparability.

**Multiple frameworks**

Globally, TCFD is not the only framework that is used in climate-risk reporting. In Australia, the TCFD framework, Sustainability Accounting Standards Board (SASB) standards, GRI standards and sustainable development goals (SDG) are used to varying levels.<sup>16</sup> Maintaining understanding of multiple frameworks and methodologies is cost intensive for investors and reduces comparability of disclosures between companies and/or industries. Table 1 below illustrates the differences in information published by two Australian mining companies.

16 [https://ifacweb.blob.core.windows.net/publicfiles/2023-02/IFAC-State-of-Play-Sustainability-Assurance-Disclosures\\_0.pdf](https://ifacweb.blob.core.windows.net/publicfiles/2023-02/IFAC-State-of-Play-Sustainability-Assurance-Disclosures_0.pdf)  
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Table 1: Comparison of climate risk information released by two Australian companies.

	Company A	Company B
<b>Disclosure Frameworks</b>	TCFD framework GRI standards SASB UN Global Compact	TCFD framework GRI standards Sustainable Development Goals
<b>Reporting format</b>	Annual report Climate Targets and Goals Report Climate transition action plan GHG Emissions Calculation Methodology report Modern Slavery Statement Release date - August	Annual report Sustainability report Climate Change report Modern Slavery Statement Release date - August
<b>Disclosure content</b>	Annual report – Has a full report as part of the operating and financial review (OFR). Includes all aspects of sustainability, disclosed using materiality assessments and under the TCFD. Climate Targets report – Separated out clear targets. Climate Transition action plan – Separated out transition plan.	Annual report – short statement on each sustainability area. Sustainability report – uses SDGs to discuss all sustainability areas except climate. Climate-change report – Uses TCFD to discuss climate risk and plans.
<b>Assurance of disclosed information</b>	Independent limited assurance by audit firm	Independent assurance by audit firm – level of assurance unspecified.

Source: Treasury analysis 2023

In response, multilateral regulatory bodies, such as the Financial Stability Board (FSB) and the International Organisation of Securities Commissions (IOSCO), have increased their focus on the quality and standardisation of disclosures. Reflecting this, the International Sustainability Standards Board (ISSB), in June 2023, released standards that are considered to be the global baseline for climate-risk reporting. The ISSB standards were developed after extensive market feedback and are supported by the G20, the FSB and the IOSCO.<sup>17</sup>

### Quality of disclosures and greenwashing

Further, the multitude of frameworks and ambiguity around voluntary disclosures contribute to lower-quality disclosures. In a recent internet sweep, the Australian Competition & Consumer Commission (ACCC) found that over 57 per cent of 247 businesses reviewed, contained false, misleading, unclear or unsubstantiated ‘green’ or ‘sustainable’ claims<sup>18</sup>. From an investor point of view, the EY’s 2022 Global Corporate Reporting and Institutional Investor Survey of 320 investment professionals found that while 99 per cent of investors considered ESG in their investment decision making, 76 per cent

<sup>17</sup> Quote from Erkki Liikanen, Chair of the IFRS Foundation Trustees: <https://www.ifrs.org/news-and-events/news/2023/06/issb-issues-ifrs-s1-ifrs-s2/>.

<sup>18</sup> <https://www.accc.gov.au/media-release/accc-greenwashing-internet-sweep-unearths-widespread-concerning-claims>

believed current corporate disclosures were likely to have some degree of greenwashing.<sup>19</sup> This results in users of general-purpose financial reports placing less value on sustainability disclosures relative to other information. This uncertainty has ramifications for how investors (global and domestic) price climate risk, likely favouring destinations with greater transparency achieved through better disclosure practices.

A major concern with current corporate sustainability disclosure practices is the lack of assurance, which the PwC survey suggests is a reason for the mistrust in such disclosures. In 2021, the International Federation of Accountants (IFAC) released a study finding that 56 per cent of companies obtained sustainability assurance for the disclosure of ESG data.<sup>20</sup> This assurance only reached the 'limited' level, with audit firms contributing 100 per cent of the assurance.<sup>21</sup> In contrast to this, the AASB and AUASB released joint research finding that only 5.2 per cent of companies referenced a third-party assurance engagement in their annual report in 2021.<sup>22</sup> This number may underestimate the total amount of assurance engagements, given it only analysed annual reports and only counted times when this assurance was self-reported. In the absence of a mandate, disclosures can happen in any format outside of the annual report and practices for revealing assurance engagement may vary. Despite this, Australia could be underperforming in providing assurance for disclosures, which may affect the quality of disclosures.

Users of general-purpose financial reports report that disclosures still do not meet their needs as they tend to be either qualitative in nature or use metrics which are not comparable across companies or jurisdictions. A 2022 ACSI report<sup>23</sup> highlighted the key areas of disclosure in which users of general-purpose financial reports face these challenges, including:

- Varied disclosure of Scope 1, 2 and 3 emissions in particular the limited focus on Scope 3 emissions.
- Limited evidence of whether and how climate change-related assumptions are integrated into capital allocation decisions.
- Few companies provide disclosure on physical risk analysis; how adaptation and risk mitigation strategies are integrated into assets; and the cost the company bears from climate inaction.
- Variation in scenario analysis disclosure, and limited transparency on the assumptions and inputs driving scenarios.
- Difficulty in assessing the alignment of company targets to global efforts to limit warming to 1.5 degrees.

### Reporting location and format

As it stands, there is no consistency required in the timing or location of sustainability disclosures. Disclosures can be found in any format, from annual reports, to integrated reports or separate sustainability reports. Similarly, reporting can be made on a calendar or financial year basis, or other alternate period for voluntary disclosures. The IFAC report highlights this lack of consistency in

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19 [https://assets.ey.com/content/dam/ey-sites/ey-com/en\\_gl/topics/assurance/assurance-pdfs/ey-global-reporting-survey-report-2022.pdf](https://assets.ey.com/content/dam/ey-sites/ey-com/en_gl/topics/assurance/assurance-pdfs/ey-global-reporting-survey-report-2022.pdf)

20 Page 25 - <https://www.ifac.org/system/files/publications/files/IFAC-Benchmarking-Global-Practice-Sustainability-Assurance.pdf>

21 Page 7 - <https://www.ifac.org/system/files/publications/files/IFAC-Benchmarking-Global-Practice-Sustainability-Assurance.pdf>

22 Page 19 - AASB-AUASB Research Report Climate Related Disclosures (12/22)

23 Page 8 - <https://acsi.org.au/wp-content/uploads/2022/08/WEBSITE-VERSION-ACSI-Climate-Change-Disclosure-in-ASX200-designed-1.pdf>

reporting formats, with a majority reporting in separate sustainability reports, and a large number reporting as part of the annual report. The IFAC report shows that there is a trend toward integration of sustainability information into the annual report and away from separate sustainability reports.<sup>24</sup> This is consistent with stakeholder feedback received in Treasury's first round of consultation on climate-related financial disclosures. During the discovery consultation, Treasury asked stakeholders about their ideal reporting location and 59 per cent agreed that it would be beneficial to have disclosures as part of the annual report, while 32 per cent wanted flexibility and 7 per cent wanted this reported in a separate report.

## Impact of not transitioning from investor and regulator perspective

Companies with material climate risks would still be obliged to report on these risks under the Corporations Act. The Corporations Act requires Australian firms to disclose information that a 'reasonable person' would expect to have a 'material' effect on the price of a financial product. Australian listed entities reporting on their climate risks to date have generally done so either through the directors' report or in a separate sustainability report. ASIC regulatory guidance *RG 247 Effective disclosure in an operating and financial review* was updated in 2019 to recommend that, where climate change represents a material risk, it should be disclosed in the directors' report as part of an operating and financial review, as required under s299(1)(a)(c) of the Corporations Act.

Depending on the circumstances, disclosure of climate risk may also be required by the law in other contexts, such as a prospectus or continuous disclosure announcement. Boards should ask if material climate-related disclosures have been made and updated where necessary and appropriate.

While these provisions have worked well in the past, they:

- Lack the granularity that produces decision-useful information to users of general-purpose financial reports.
- Lack the certainty that allows our regulators to act and manage systemic risks.

In the absence of a tailored framework:

- It would be costly for companies to design their own reporting standards to align with well-designed international standards. It would also result in standards that may not have all the useful information demanded by investors and that would assist regulators in assessing systemic risk. It would also result in Australia having a fragmented and inconsistent set of corporate climate disclosures. This may be reflected in a higher risk premium embedded in capital relative to international counterparts.
- Poor quality disclosures also increase the risk of greenwashing. This would inhibit ASIC and potentially lead to an inappropriate allocation of capital. As noted above, ASIC is currently relying on guidance and broadly drafted provisions. This makes enforcement more difficult as the regulator has to spend additional resources to reach its outcome. ASIC has recently begun ramping up investigations into greenwashing, finding it had to intervene in 35 cases in a 9-month period to ensure companies met their disclosure obligations.<sup>25</sup>
  - The same could be said about 'greenhushing' whereby firms claim they have good ESG credentials but refuse to disclose them, citing greenwashing risks. ASIC describes this phenomenon as "just another form of greenwashing; an attempt to garner a 'green halo'

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<sup>24</sup> Page 3 - IFAC-State-of-Play-in-Sustainability-Reporting-and-Assurance-2019-2020-date.pdf

effect without having to do the work.” Taken together, greater levels of greenwashing can lead to misallocation of capital, reducing benefits for stakeholders.

- Climate change is a systemic risk to the financial sector that warrants heightened scrutiny. Inadequate disclosure requirements would make it difficult to identify and manage risks in individual entities and in the system, potentially leading to violations of the existing requirement for companies to report material risks and negative consequences for the real economy. Treasury consultation has revealed strong support for the new regime because of the benefits it would bring and the costs of not aligning. Not mandating climate-related financial disclosures would lead to significant disappointment in the corporate sector and financial markets.
- As discussed above, some Australian entities are already reporting under their Corporations Act obligations. However, Treasury consultation suggests deficiencies remain in corporate disclosure on the risks and opportunities faced from climate change. Investors have noted they need more in-depth information on a broader range of parameters to make efficient capital allocation decisions.

## Case for government action

As noted in the sections above, while existing guidance from regulators in Australia has led to an increase in the number of companies disclosing climate-related risks it has not produced disclosures that are useful for investors; consistency in reporting across companies; and take up across majority of corporates. Without Government intervention, entities will continue to use different frameworks or report in ad-hoc ways, hampering investor ability to compare and make informed capital allocation decisions. The primary purpose of this proposed regime is to:

- Provide a consistent reporting framework to partially correct a market failure that results in information asymmetry. Such information asymmetry results in the costs of climate change not being internalised in businesses’ financial analysis and are therefore not considered in business and investment decision-making.
- Improve the quality of climate-related financial disclosures and align Australia’s approach with global practices, which will allow the market to operate more efficiently.

The Government is well placed to give effect to this objective through primary legislation and by empowering standard setting bodies to set a tailored Australian standard that meets the global baseline set by the ISSB.

## Policy options

Given the proposed policy intervention is an election commitment, Treasury has only considered the option of retaining the status quo and different options to implement the proposed policy reform. This is consistent with guidance from the Office of Impact Analysis.

### Status Quo

The status quo will continue to use the Corporations Act, regulatory guidance and market discipline to achieve transparency goals. In this case, Australian companies will continue to disclose their material climate risk, as per ASIC guidance and s299(1)(a)(c) of the Corporations Act. Under the status quo, firms have flexibility to choose which climate risk disclosure framework to use and the content,

location and parameters disclosed. Firms would incur costs under the status quo, with the extent of the costs determined by what individual firms decide are appropriate disclosures. It is possible that market discipline would result in the need for more rigorous disclosures than currently produced, increasing the costs for firms. As a result, retaining the status quo is not a costless option.

Presently, ASIC and the ASX provide guidance to organisations that they should follow TCFD recommendations. There has been steady uptake of TCFD in Australia. However, the TCFD framework is flexible, firm capabilities vary, and Australia's legal framework allows considerable variation in how risks are reported. As a result, there are shortcomings with the quality of analysis, consistency, depth, and comparability of disclosures.

Investors would receive some information on 'material' climate risk but incur costs associated with lack of consistency or comparability of that information. Investors may not receive enough information to make fully informed capital allocation decisions. While take up of disclosure against TCFD guidelines has been good, a large number of firms still do not disclose their climate risks in sufficient detail. This means that investors are not informed about the climate risks across the breadth of the Australian corporate sector.

## Implementation Options

Treasury sought initial views on key considerations for the design and implementation of the Government's commitment to standardised, internationally aligned requirements for disclosure of climate-related financial risks and opportunities in Australia between December 2022 and February 2023.

In considering implementation options for the Government's election commitment, Treasury considered four key design criteria:

- The appropriate coverage of entities that would be captured by these requirements.
- The reporting content of these disclosures
- The assurance framework
- Appropriate timeframes for introducing mandatory disclosures.

### Option 1: Design Consultation Policy

**Timeframe of introduction:** This option proposes a three-phased approach, starting with a relatively limited group of very large entities that expands over two years to apply to progressively smaller entities.

**Coverage:** This option would include large, listed and unlisted entities (including financial institutions) phased-in over time. This removes any perverse incentives to list or delist for regulatory arbitrage. Entities covered by this reform would be grouped into three phases. Group 1 would commence reporting from 2024-25, Group 2 from 2026-27 onwards and Group 3 from 2027-28 onwards.

Under this option, approximately 723 entities would be included initially. These requirements would include 755 entities in the second phase and an additional 362 NGER reporters and could be expanded to as many as 4,555 entities in the third phase by 2027, based on currently available data. There is significant uncertainty in entities in the third phase due to a lack of available data.

By 2027-28, this option would cover all entities (including financial institutions) that lodge financial reports under Chapter 2M of the Corporations Act and that meet two of the following criteria:

- the consolidated revenue for the financial year of the company and any entities it controls is \$50 million or more.
- the value of the consolidated gross assets at the end of the financial year of the company and any entities it controls is \$25 million or more.



- the company and any entities it controls have 100 or more employees at the end of the financial year.
- In addition, all entities that are required to report under Chapter 2M of the Corporations Act that are registered as a 'Controlling Corporation' reporting under the *National Greenhouse and Energy Reporting Act 2007* (Cth) would be covered under climate-related risk disclosures requirements, even if they do not meet the threshold criteria above.

**Reporting content:** Requirements would aim to provide clarity to reporting entities about the types of information to be disclosed and to ensure the requirements improve access to decision-useful information for users of financial reporting. Reporting entities would be required to:

- Disclose information about governance processes, controls and procedures used to monitor and manage climate-related financial risks and opportunities.
- Use qualitative scenario analysis to inform their disclosures, moving to quantitative scenario analysis by end state.
- 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)*.
- Disclose transition plans, including information about offsets, target setting and mitigation strategies.
- Disclose information about any climate-related targets (if they have them) and progress towards these targets.
- 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.
- Disclose scope 1 and 2 emissions for the reporting period.
- Disclose material scope 3 emissions 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.
- Have regard to disclosing industry-based metrics, where there are well-established and understood metrics available for the reporting entity.

**Assurance framework:** Assurance requirements would be phased in and scaled up over time to allow capability and capacity uplift in the audit and assurance industry. Phasing would occur based on when the entity commenced reporting, and the gradual scaling up of requirements would occur based on the complexity of the underlying disclosures and the ability to undertake assurance on those disclosures. This option proposes:

- Year 1 of reporting: Limited assurance of scope 1 and 2 emissions. Reasonable assurance of governance disclosures
- Year 2 of reporting onwards: Reasonable assurance of scope 1 and 2 emissions and governance. Limited assurance of scope 3 emissions, scenario analysis and transition plans (specific requirements – process/ methodology/assumption assurance)
- Year 3 of reporting onwards: Reasonable assurance (except for items specified as limited assurance). Limited assurance of scope 3 emissions, scenario analysis and transition plans (full quantitative assurance).
- Year 4 of reporting onwards: Reasonable assurance of all climate disclosures.

Options 1a and 1b discussed below are variations on this option.

### Option 1a – Narrower coverage with Group 3 only required to report if there are material climate risks and specific thresholds for asset owners

This option is a variation on Option 1 in that it amends the breadth of coverage of these reforms. Under this option, only entities in Groups 1 and 2 would be mandated to disclose their climate risks. Compared with option 1, this option does not propose changes to the timing of introduction, the reporting content, or the assurance framework. The option will have the following coverage thresholds:

**Coverage:** As with option 1, this option includes large, listed and unlisted entities (including financial institutions) phased-in over time. This removes any perverse incentives to list or delist for regulatory arbitrage. Entities covered by this reform would be grouped into two phases. Group 1 would commence reporting from 2024-25, Group 2 from 2026-27 onwards.

Under this option around 1,800 entities would be included. This would include the same amount of Group 1 and Group 2 entities but significantly less Group 3 entities. Group 2 in this option would include the balance of remaining NGER reporting entities.

By 2026-27, this option would cover all entities (including financial institutions) that lodge financial reports under Chapter 2M of the Corporations Act that meet two of the following criteria:

- the consolidated revenue for the financial year of the company and any entities it controls is \$500 million or more.
- the value of the consolidated gross assets at the end of the financial year of the company and any entities it controls is \$200 million or more.
- the company and any entities it controls have 250 or more employees at the end of the financial year.

In addition, all entities that are required to report under Chapter 2M of the Corporations Act that are registered as a 'Controlling Corporation' reporting under the National Greenhouse and Energy Reporting Act 2007 (Cth) would be covered under climate-related risk disclosures requirements, even if they do not meet the threshold criteria above.

Further from 2027-28, entities that would be captured by Group 3 would be required to do a materiality assessment. If the entity determines it does not have material climate-related financial risks or opportunities, they would be required to include a statement in their annual report attesting this. Where the entity does have material risks, disclosure would be required in line with the relevant Australian standard as per entities in Groups 1 and 2.

This option also introduces a specific threshold for asset owners.

### Option 1b - Narrower coverage and changes to assurance framework

This option is a further variation of Option 1a. It amends the assurance framework such that the Government would not mandate a roadmap for the phasing in and scaling up of assurance requirements for climate disclosures. Instead, the Government would require limited assurance of Scope 1 and 2 emissions from commencement of the reform and reasonable assurance of climate-related financial disclosures by 2030, with the roadmap to reasonable assurance to be flexibly determined by the AUASB.

Limited assurance of Scope 1 and 2 emissions would be required as a minimum requirement. This requirement would increase the credibility of Scope 1 and 2 emissions disclosures, while being in line with market capability. Currently, voluntary assurance of climate-related information is predominantly

at the limited assurance level, however some entities have obtained reasonable assurance on Scope 1 and 2 emissions<sup>26</sup>.

This option recognises the capability uplift required in the assurance and audit industry and the uncertainty in determining how long this could take. It also considers the timing of international assurance standards. Development of an international standard on sustainability assurance<sup>27</sup> is currently underway, however this is not expected to be finalised until the end of 2024.

## Cost-benefit analysis

This cost-benefit analysis assesses the likely benefits and costs to preparers, users of general-purpose financial reports and the wider market. The analysis will look at the 'likely' costs and benefits rather than actual costs and benefits as many of these effects cannot be known or reasonably estimated at this time. The costs and benefits of these mandatory climate disclosures will be spread unevenly across the economy, with some companies and sectors experiencing greater costs and/or benefits than others. Quantification of costs and benefits (which occur over a larger time horizon) is inherently difficult as this is influenced by the size of individual entities, their exposure to climate risks and opportunities as well as their readiness in engaging with this level of reporting (for example, if the entity is an early adopter of TCFD standards, it may cost less to establish system and governance changes to comply with mandatory climate-risk reporting).

## Policy benefits

The presence of reporting standards provides a baseline for companies to disclose against, helping to improve comparability while also improving quality. Reducing information asymmetry between preparers and users of general-purpose financial reports aims to reduce uncertainty, in turn potentially reducing the cost of capital.

At a high level, the benefits of this policy will flow from a better-informed market. This may be reflected in a lower cost of capital faced by firms and a more efficient allocation of resources, aligned with the transition to net zero.

However, these benefits are hard to quantify. Due to these limitations, this discussion of policy benefits is based on academic studies that have found the impact of mandating disclosures (climate or other disclosure requirements in the economy) to be a net positive on entities.

For example, consider the benefits of using IFRS Accounting Standards, which are used in more than 140 jurisdictions. A literature review of close to 200 academic studies on the effects of mandatory adoption of IFRS Accounting Standards in the EU found that on average there were benefits to applying these global standards across jurisdictions. Some benefits included increased transparency and comparability, lower cost of capital, increased market liquidity, improved corporate investment efficiency and improved international capital flows.<sup>28</sup>

A number of academic studies have examined the impact of sustainability standards and mandatory reporting on disclosures and company actions. These studies found that following the release of the SASB standards, publicly traded companies in the US improved their disclosures of material sustainability information on average. Further, there were significant improvements in companies'

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26 Page 19 - [https://aasb.gov.au/media/xu5leeby/aasb-auasb\\_rr\\_climaterelateddisclosures\\_12-22.pdf](https://aasb.gov.au/media/xu5leeby/aasb-auasb_rr_climaterelateddisclosures_12-22.pdf)

27 <https://www.iaasb.org/focus-areas/understanding-international-standard-sustainability-assurance-5000>

28 Page 34 - ISSB Effects Analysis - <https://www.ifrs.org/content/dam/ifrs/project/general-sustainability-related-disclosures/effects-analysis.pdf>

sustainability performance among companies applying the SASB standards.<sup>29</sup> Analysis of sustainability disclosure mandates around the world found mandatory ESG disclosures have beneficial informational and real effects. The analysis included a sample of 17,680 companies across 65 countries and found that mandating ESG disclosures increases the availability and quality of ESG reporting (especially for poor performing companies) and reduces the likelihood of negative ESG-related incidents and the risk of a stock price crash.<sup>30</sup>

While this policy is likely to incur implementation costs, the alternative is the status quo where reporting is variable and inconsistent. Users of general purpose financial reports would have to continue sourcing and carefully analysing the information from numerous, differing reports.

In consultation, majority of stakeholders agreed there are benefits from climate-related financial disclosures, particularly for investors who would have better access to information, reducing costs, complexity and confusion. This would in turn improve access to capital or reduce the risk premium on capital. It would also level the playing field for companies who are and are not reporting.

The primary objective of this policy is to improve decision-useful information. In time, this will reduce the cost to investors of sourcing and analysing the information. Under current arrangements investors need to consider a range of sometimes inconsistent approaches to disclosure across companies.

Improving consistency, particularly in reporting formats, periods and styles could reduce the costs through automation of collection and analysis of data. Should one style of standard become the predominant force in Australia, greater investment could be made in that standard to internalise capability uplift, therefore reducing reliance on external providers. This is a view that was reinforced through consultation.

Treasury expects that mandating financial reporting will change the financial reporting system and will encourage firms to invest in the necessary skills to enhance the quality and efficiency of reporting.

## Estimated costs of implementation

The adoption of new standards for climate reporting will increase compliance costs as well as bringing benefits to reporting entities and the broader economy. For example, in Australia, converting to new accounting standards has been approximated to cost between \$784,648 and \$1,569,295 per company (1AUD = 0.64 USD). Additionally, a study using publicly traded Australian companies has shown that adoption of IFRS standards increased the mean level of audit costs by 23 percent<sup>31</sup>. As expected, this study finds that greater audit complexity leads to increases in compliance costs during the transition to new accounting standards. **Appendix A** provides an overview of costs estimated by other jurisdictions that are considering or have already mandated climate-related financial disclosures on a subset of reporting entities.

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29 See for example, K.Bochkay, J.Hales and G.Serafiem, 'Disclosure Standards and Communication Norms: Evidence of Voluntary Disclosure Standards as a Coordinating Device for Capital Markets', Miami, Florida, University of Miami Business School Research Paper no.3928979, 2021; K.Bochkay, S.Choi and J.Hales, 'Mere Puffery or Credible Disclosure? The Real Effects of Adopting Voluntary ESG Disclosure Standards', 2022.

30 P.Krueger et al., 'The Effects of Mandatory ESG Disclosure Around the World' European Corporate Governance Institute – Finance Working Paper no.754, Brussels, 2021, pp. 21-44

31 De George, E. T., Ferguson, C. B., & Spear, N. A. (2013). How much does IFRS cost? IFRS adoption and audit fees. The accounting review, 88(2), 429-462.

## Data sources

Data for entities captured under implementation options was sourced from the Australian Bureau of Statistics' Business Longitudinal Analysis Data Environment (BLADE), the Australian Tax Office's Pay as you go (PAYG), Business Activity Statement (BAS), Business Income Tax (BIT) and the Clean Energy Regulator's NGER data. Despite the number of data sources, there is still significant uncertainty in the number of covered entities as many of these data sets are incomplete. The thresholds for inclusion in Group 1 are broadly equivalent to the characteristics of the 200<sup>th</sup> company in the ASX200, while the thresholds for Group 2 are broadly equivalent to the characteristics of the 300<sup>th</sup> company in the ASX 300. For the purposes of this analysis, we extrapolate from ASX100 and ASX200 data to estimate the number of companies already voluntarily reporting and those that will be additional under a mandatory regime.

Regulatory burden estimates have been informed by submissions and consultation, the *UK Impact Analysis*, the *SEC's Proposed Rule: The Enhancement and Standardization of Climate-Related Disclosures for Investors* and various academic studies – underpinned by the *Regulatory Burden Measurement Framework*.

## Methodology

Much of the costs in this policy impact analysis are based on the 'UK Impact Analysis'<sup>32</sup>, which provides a more granular breakdown of initial and ongoing costs compared to more general costings provided in surveys, analysis and submissions to the US, NZ and to Treasury. Where relevant and available we have used data from submissions.

While the UK's analysis was based on mandating the recommendations by the TCFD, Australia's standards are expected to align most closely with the ISSB, going further in areas such as climate-related scenario analysis, while mitigating some of the burden through relief mechanisms described below. It is expected that Australia's requirements will be more costly to comply with than for the TCFD in the UK and this has been reflected in the breakdown of costs. While staffing requirements are at the analyst, manager and executive level, we have blended various salaries based on roles and responsibilities (this includes roles such as financial controller, finance manager, group accountant, commercial analyst, financial accountant, systems accountant etc.). The blended salary is close to \$140,000 according to the 2023 Hays Salary Guide<sup>33</sup>.

## Status quo

### Affected cohort

The number of affected entities varies depending on the option and also has an impact on the total regulatory burden. The sensitivity analysis at **Appendix B** tests the impact of higher and lower affected cohorts on regulatory burden under status quo and all three implementation options.

KPMG reports that 78 per cent of the ASX100 currently report using the TCFD and a 2023 ASCI report<sup>34</sup> shows that 135 of the ASX200 (62.5 per cent) are aligning climate disclosure to the TCFD framework. The number disclosing is likely to grow in the coming years, regardless of policy intervention. Without mandated disclosure standards, voluntary reporting results in varying levels of detail which makes

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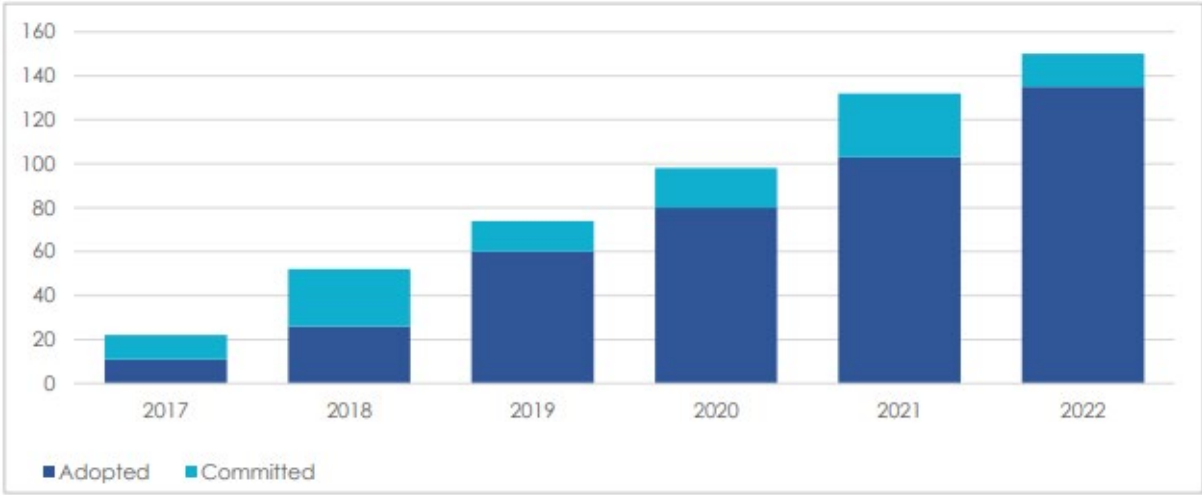
32 <https://assets.kpmg.com/content/dam/kpmg/au/pdf/2023/australian-sustainability-reporting-trends-june-2023-update.pdf>

33 <https://www.hays.com.au/documents/276732/1102429/Salary+Guide+2023.pdf>

34 ASCI Fact Sheet Climate 2023

comparison difficult. Research has shown there is a large gap between public-private environmental transparency, with reports that in the US, less than 1 per cent of private companies are reporting their climate risk<sup>35</sup>.

**Chart 2: ASX companies adopting, committing and reviewing the use of TCFD framework over time**



Source: 2023 ACSI report: Climate disclosure in the ASX200

To analyse the costs of status quo we split entities into two cohorts: those who are currently disclosing and those will start to disclose in the next 10 years (due to market discipline):

- For entities that are already disclosing against the TCFD, we assume:
  - The number of entities reporting under the TCFD framework falls as the size of the company decreases due to a lack of resources and incentives.
  - Following the trends described above, we assume 55 per cent (165 entities) of publicly listed companies in Group 1 and Group 2 (ASX300) are currently disclosing.
  - We assume 15 per cent (178 entities) of all unlisted companies in Group 1 and Group 2 are disclosing.
  - We assume no Group 3 entities are disclosing.
- For the cohort that we expect to begin disclosing due to investor demand and international expectations, we assume:
  - most companies in Groups 1 and 2 will begin disclosing and a large proportion of unlisted companies will also be disclosing over the next 10 years.
  - The balance of listed entities currently not disclosing (135 entities) in Group 1 and 2 will begin disclosing.
  - We assume that 50 per cent (an additional 414 entities) of Group 1 and Group 2 unlisted entities will begin disclosing.
  - We assume that 5 per cent (an additional 278 entities) of Group 3 entities begin disclosing.

Therefore, we expect 343 voluntarily disclosing entities and expect an additional 777 entities to begin disclosing in the next 10 years.

Given the recent release of final ISSB standards, we have assumed status quo to be further uptake of the TCFD framework. We analyse the ongoing costs that firms are already experiencing through the

35 Closing the Public-P...~<https://www.bain.com/insights/closing-the-public-private-environmental-transparency-gap/>

further uptake of TCFD. Earlier in the section, we estimated the number of Australian entities already disclosing the TCFD to be 343. Treasury also expects that in the next 10 years:

- an additional 777 entities will take up TCFD disclosure.
- made up of 549 from Groups 1 and 2 and 228 from Group 3.

We use the UK Impact Analysis costings of compliance with a TCFD disclosure regime. Converted to \$AUD (1 AUD = 0.527 GBP), this equates to \$361,443 per company in the first year of disclosing, falling to \$263,622 in subsequent years.

Under the status quo regime, we assume a proportion of companies reporting in each Group implement a subset of the proposed disclosures. To account for this, we discount the cost of implementation for Groups 1 and 2 by 10 per cent, and for Group 3 by 70 per cent. We assume that once a company has implemented climate-related reporting, they continue to report in all subsequent years.

**Table 3: Estimated costs of status quo disclosure in Australia**

	Transitional Cost (\$m)	Ongoing cost (\$m)
TCFD disclosure for Group 1 and 2 discounted at 10 per cent	178.72	211.64
TCFD disclosure for Group 3 discounted at 70 per cent	24.70	18.01
Total cost	203.41	229.65
Transitional costs amortised over 10 years	20.34	0

Source: Treasury analysis

The total ongoing compliance costs is the sum of the amortised transitional costs and ongoing costs equalling \$249.99 million. There is significant uncertainty in this figure as we assume continued disclosure and uptake of one framework (the TCFD framework). It is possible that several other frameworks could be used, particularly the recently released ISSB standards. It is expected that the cost for implementing ISSB would be marginally greater than the TCFD due to a higher degree of prescription in the requirements. This would increase the cost of the status quo.

Further to this, maintaining the status quo will also result in costs for investors. One report with surveyed US institutional investors, approximating the cost of collection and analysis of data to be US \$1,249,000 annually<sup>36</sup>, with costs split into collection of data, analysis of data and sustainability consultants. It should be noted that the sample size of this survey is relatively small and that costs may vary depending on several factors.

There are also a number of unquantified costs associated with the current reporting requirements, including a higher risk premium for investors, a higher cost of capital for companies and less efficient capital allocation across the economy. These costing assumptions are approximate only, and do not account for circumstances where companies would need to meaningfully increase climate risk reporting activities in order to remain compliant with existing obligations under the *Corporations Act 2001* to report on ‘material’ risks.

<sup>36</sup> SustainAbility Institute by ERM, Costs and Benefits of Climate-Related Disclosure Activities by Corporate Issuers and Institutional Investors, <https://www.sustainability.com/thinking/costs-and-benefits-of-climate-relateddisclosure-activities-by-corporate-issuers-and-institutional-investors/>.

**Table 4: Key drivers of costs to investors**

Activity	Cost (\$USD)
External ESG ratings, data providers, and consultants	\$487,000 average annual
In-house, outside counsel, and proxy solicitor analysis of shareholder voting for ballot items related to gathering climate risk management information	\$405,000 average annual cost
Internal climate-related investment analysis	\$357,000 average annual cost

Source: SustainAbility Institute

**Option 1: Design consultation policy**

*Affected cohort*

Option 1 has the broadest coverage out of all options. Treasury benchmarked the coverage parameters for inclusion on ASIC’s “large proprietary company” size threshold. Treasury analysis suggests that based on 2021 data, the size threshold for Group 1 will capture, at a minimum, 729 entities, Group 2 will capture, at a minimum, 755 entities and Group 3 will capture, at a minimum, 4,555 entities. Due to the lack of complete data sets, we consider these numbers marginally underestimate the total number of companies that are likely to be captured. Furthermore, we are unable to project the number of companies that would meet the size thresholds in the future (either due to movement between groups or due to entities falling below the Group 3 size threshold).

Based on 2021 NGER reporting] a total of 723 entities will be captured under the definition of an NGER ‘Controlling Corporation’. As at 2021, 361 NGER reporters are above the publication threshold, and will therefore be captured in Group 1. A large proportion of NGER reporters are likely to meet at least two of the three size thresholds for Group 1 and are therefore not ‘additional’ reporters in Group 1. We assume the remaining 362 NGER reporters that fall below the publication threshold will be captured in either Groups 2 and 3. As above, we consider this number likely overestimates the number of NGER reports in each group as we are unable to determine those NGER reporters that would have to report under this option due to the size thresholds.

*Costing assumptions*

To comply with mandatory climate-risk disclosure, we assume there to be two cost profiles for an individual entity – initial costs and ongoing costs.

Treasury expects most of the effort to transition will be significantly higher in the first year where extra costs are incurred by greater internal labour for systems development, familiarisation and educational costs as well as the initial preparation of the climate report. The costs for implementation of Australian standards have been scaled up compared to the TCFD benchmark used in the UK Impact Analysis given the greater specificity of ISSB disclosures.

As capability improves, it is expected fewer resources would be required. A discount of 33 per cent applies to staff collecting and maintaining/improving existing models and analysis. However, a greater discount applies to the preparation of the climate report as it is expected much of the work is repetitive. Assurance costs are expected to increase as companies move toward reasonable assurance. Initial costs

Tables 5 outlines the detailed breakdown of assumptions used to calculate initial costs at an entity level.



**Table 5: Assumptions for initial cost**

Transitional activity	Estimated efforts/costs (very broadly approximated)
<b>Familiarisation and educational costs</b>	<p>Familiarisation costs: The UK Impact Analysis and The Climate Financial Risk Forum guidance<sup>37</sup> assume an average climate reporting guidance of 125 pages, based off the TCFD framework. As Australian standards are expected to be significantly more detailed, we assume relevant regulatory guidance materials will be 200 pages. The analysis assumes 6 minutes reading time per page by 3 executives, 15 managers and 25 analysts. This aligns with research from the SEC that suggests development of a climate report can average 40 staff. As discussed earlier, we use an hourly that includes overhead costs at \$136/hour.</p> <p>Total hours = 860</p>
<b>Legal review</b>	<p>Legal review consisting of one-off costs for reviewing legal text and guidance in-house. We assume 2 solicitors conduct a one-week legal review and a senior legal professional reads and signs off in a day.</p> <p>Total hours = 77</p>
<b>Systems changes and initial data collection, scenario analysis and scope 3 modelling build-out</b>	<p>ICT systems, data collection and related systems upgrades for collecting and processing of climate-related data are expected to be significant. We expect that data collection will be more intensive given the prescriptive nature of the ISSB in mandating scope 3 and in our requirement for quantitative scenario analysis. We benchmark off the UK with the expectation that more resources are required in the initial year. It is expected to take 1 analyst and 1 manager to develop the system.</p> <p>Scenario analysis: While the UK expects one analyst to develop and maintain climate scenarios, full time for 6 months. We expect it will be double this as we expect the greater requirement for eventual quantitative scenario analysis will require extra resources and investment.</p> <p>Scope 3 assessment: We expect that the mandatory inclusion of scope 3 will take one analyst full time for the first year to develop boundaries, modelling and estimation. As discussed earlier, we use a FTE salary including overheads of \$245,000.</p> <p>Total FTE = 4</p>
<b>Preparation of initial climate report</b>	<p>The expected length of a TCFD report is 18 pages<sup>38</sup>. It is expected that the requirements of the Australian standards will result in a lengthier report of 20 pages. We assume that 5 analysts, 3 managers and 3 executives will be involved in the collating, proofing, drafting and signing off the report. Each page is expected to take 5 hours to prepare.</p> <p>Total hours = 1100</p>

37 Climate Financial Risk Forum Guidance on Non-Financial Risk Reporting, 2020, [www.fca.org.uk/transparency/climate-financial-risk-forum](http://www.fca.org.uk/transparency/climate-financial-risk-forum)

38 [https://assets.bbhub.io/company/sites/60/2021/07/2021-TCFD-Implementing\\_Guidance.pdf](https://assets.bbhub.io/company/sites/60/2021/07/2021-TCFD-Implementing_Guidance.pdf)

Transitional activity	Estimated efforts/costs (very broadly approximated)
<b>Assurance of initial report</b>	<p>Third-party assurance is the norm in Australia. An academic study suggests assurance costs for sustainability reports (where climate-related information is normally disclosed) ranges from 5 per cent to 10 per cent of audit fees<sup>39</sup>, which ASIC suggests is 0.03 per cent of ASX300 market capitalisation<sup>40</sup>. We expect this number fluctuates depending on size of the company, with a higher percentage for smaller companies. We discount this cost because climate is only one part of the sustainability report and apply a 23 per cent premium for instituting new standards, discussed above<sup>41</sup>.</p> <p>This would put the median ASX300 company with a market capitalisation of \$2.4bn with limited assurance costs between \$33,211 and \$66,420. It is likely that these estimates underestimate actual costs given they are based on assurance of financial statements and assurance of emissions and other climate information is expected to be more complex, at least initially.</p>

Source: Treasury analysis

### Ongoing costs

We have internalised the costs of consultants, which surveys and research suggest can average US \$50,000 to \$460,000<sup>42</sup>. The cost for consultants is uncertain, with costs varying depending on the service, from assurance to implementing new ICT systems and scope 3 modelling and scenario analysis.

Given the long-term nature of climate-related reporting, we assume companies will invest in the long-term internal capability of their businesses. As such, our analysis internalises the costs of for developing models, automation and capability uplift (data collection, modelling and scenario analysis) within companies. We also expect that models, scenario analysis and transition plans are updated routinely, with major changes to assumptions in these models occurring once every 3 years as entities review their plans and strategies. We introduce a discount rate of 33 per cent that is slightly higher than seen in the UK Impact Analysis as a result.

Internal labour rates for activities are expected to be performed by employees based on an annual blended salary of \$140,000. In accordance with the Regulatory Burden Measurement Framework, this salary amount is adjusted using a default multiplier of 1.75 to account for overhead and non-wage costs. As a result, internal labour is costed at \$245,000 or \$136 per hour (assuming 4 weeks annual leave and a work week of 37.5 hours). Table 6 below outlines the detailed breakdown of assumptions used to calculate ongoing costs at an entity level.

39 Casey, R. J., & Grenier, J. H. (2015). Understanding and contributing to the enigma of corporate social responsibility (CSR) assurance in the United States. *Auditing: A Journal of Practice & Theory*, 34(1), 97-130.

40 <https://download.asic.gov.au/media/5900581/rep678-published-22-december-2020.pdf>

41 De George, E. T., Ferguson, C. B., & Spear, N. A. (2013). How much does IFRS cost? IFRS adoption and audit fees. *The accounting review*, 88(2), 429-462.

42 <https://www.sec.gov/comments/climate-disclosure/c112-8914283-244663.pdf>

**Table 6: Assumptions for ongoing costs**

Recurring activity	Estimated efforts/costs (very broadly approximated)
<b>Legal review</b>	<p>We assume the same legal review is required each year following implementation, but discount by 33 per cent after the first year.</p> <p>Total hours = <math>77 \times 0.67 = 51.59</math></p>
<b>Data collection, Scenario analysis and Scope 3 modelling</b>	<p>Data collection: After the first year, we expect that more systems are in place that make data collection easier, decreasing the workload by half a year for a full-time analyst. This brings the total FTE to 1.5. Further improvements (automation and otherwise) in the future also bring down costs by 33 per cent after the first year.</p> <p>Scenario analysis: While the UK expects one analyst to develop and maintain climate scenarios, full time for 6 months. We expect it will be double this as we expect the greater requirement for eventual quantitative scenario analysis will require extra resources and investment. There is an expectation that the costs will decrease by 33 per cent after the first year.</p> <p>Scope 3 assessment: We expect that the mandatory inclusion of scope 3 will occupy one analyst full time for the first year, decreasing by 33 per cent in subsequent years as they become more familiar with boundaries and reporting.</p> <p>Total FTE = <math>3.5 \times 0.67 = 2.31</math></p>
<b>Preparation of climate report</b>	<p>Preparation of additional climate reports will require less time once capability has developed.</p> <p>We assume that 3 analysts, 2 managers and 1 executive will be involved in collating, proofing, drafting and signing-off the report. Each page is expected to take 3 hours to prepare.</p> <p>Total hours = 360 hours</p>
<b>Assurance</b>	<p>Over time we expect reasonable assurance to be phased in. There is a premium for performing reasonable assurance and we estimate reasonable assurance costs to be 1.66 times higher than limited assurance, similar to the SEC. This puts the cost of reasonable assurance between \$55,129 and \$110,257.</p> <p>It is likely that these estimates underestimate actual costs given they are based on assurance of financial statements, where is the assurance of emissions and other climate information is more novel.</p>

Source: Treasury analysis

Table 7 summarises our estimates of the initial and ongoing costs for an individual entity using assumptions in Tables 5 and 6.

**Table 7: Summary of initial and ongoing costs per firm in Option 1**

Activity	Transitional cost (\$)	Ongoing cost (\$)
Familiarisation and education costs	116,960	0
Legal review	10,472	7,854
Systems changes	245,000	0
Data collection	245,000	242,550
Scenario analysis	245,000	161,700
Scope 3 modelling	245,000	161,700
Preparation of climate report	149,600	48,960
Assurance	49,815	82,693
<b>Total</b>	<b>1,306,847</b>	<b>714,032</b>

Source: Treasury projections

International benchmarking reveals significant compliance burden when compared to the UK, mainly due to mandating a more prescriptive standard (aligned with the ISSB). When compared to the US, we note similar recurring costs. Due to the lack of granularity around the US cost estimate, it is difficult to explain the difference in initial costs. Our assumption that firms will internalise many of the costs associated with this reform means implementation costs are higher when compared to the US which assumes that external consultants with sufficient experienced are already used.

Feedback from consultation suggested the cost to implement a new climate disclosure system could be as low as a \$150,000 to more than \$1 million. One submission suggested costs of between 1 and 10 basis points of a company's financial assets. This suggests that for the median ASX300 company with \$1,858,000,000 in assets, this would amount to \$185,800 to \$1,858,000.

Overall, these costs acknowledge the ongoing burden that climate reporting places on companies, particularly as costs are still significant on a yearly basis due to the ongoing need to source data, model and perform scenario analysis.

**Table 8: Cost comparison from overseas (\$AUD), 1AUD = 0.527 GBP, 0.677 USD**

Country	Australia	UK	US
Initial cost	1,306,847	361,443	945,993
Recurring cost	714,032	263,622	783,250

Source: Treasury projections

### Cumulative compliance costs across groups

In preparing this estimate, Treasury considers it reasonable to amortise the transition costs over 10 years because climate-related financial disclosures would be an ongoing obligation for companies. Additionally, many new AASB standards and IFRS standards have been in effect for longer than a decade. Group 3 is not included in this table as the cost breakdown is more general in nature compared to the granular breakdown. This is in part due to proportionality as we expect costs to differ significantly. There are several assumptions made with these costs:

- Group 1 is the baseline and experiences the full cost with the exception of discounts for ongoing synergies and learnings from the first year of disclosing.
- We discount transition costs to Group 2 by 20 per cent as we expect implementation by Group 1 will lead to increased availability of methodology, data and frameworks across the market. The ongoing costs converge to the long-run recurring cost.

- We assume ongoing costs for both Group 1 and 2 entities to decrease and then stabilise over the horizon, notwithstanding any future changes to climate-risk disclosure reforms.
- We discount NGERs by 30 per cent for across all years of as they are already subject to NGER and other mechanisms of reporting such as the Safeguard Mechanism.

**Table 9: Transitional and ongoing costs for Groups 1,2 and NGER entities under Option 1**

Activity	Group 1 (729 entities)		Group 2 (755 entities)		NGER (362 entities)	
	Transitional cost (\$m)	Ongoing cost (\$m)	Transitional cost (\$m)	Ongoing cost (\$m)	Transitional cost (\$m)	Ongoing cost (\$m)
Familiarisation and education costs	85.26	0.00	70.64	0.00	29.64	0.00
Legal review	7.63	5.73	6.33	5.93	2.65	1.99
Systems changes	178.61	0.00	147.98	0	62.08	0.00
Data collection	178.61	179.50	147.98	185.90	62.08	62.39
Scenario analysis	178.61	119.67	147.98	123.93	62.08	41.60
Scope 3 modelling	178.61	119.67	147.98	123.93	62.08	41.60
Preparation of climate report	109.06	35.69	90.36	36.96	37.91	12.41
Assurance	36.32	60.28	30.09	62.43	12.62	20.95
<b>Total</b>	<b>952.70</b>	<b>520.53</b>	<b>789.34</b>	<b>539.09</b>	<b>331.14</b>	<b>180.93</b>

Source: Treasury projections

Group 3 has a separate calculation as we expect costs to be proportionate to size of the company, resulting in fewer costs. Many Group 3 entities are expected to have fewer material climate risks to disclose. Much like Group 2, Group 3 would benefit from delayed application of reporting obligations through increased availability of methodologies and data.

- We generalise the costs for Group 3, aligning with information received in submissions, reporting costs are between 1 to 10 basis points of net assets.
- For the median Group 3 company, Treasury analysis estimates net assets to be \$53,000,000 – placing fees between \$5,300 and \$53,000 with an average of \$29,150.
- In addition, we estimate assurance costs to be 3 basis points of net assets, costing \$15,900 for limited assurance. This brings the total cost per Group 3 entity to \$45,050.
- This would appear accurate given previous Treasury analysis that identifies the cost of financial reporting for large proprietary companies averages \$36,950 per year<sup>43</sup>. We assume the initial cost is higher but the cost falls to this long-term average as an ongoing cost.

**Table 10: Estimated total Group 3 compliance costs**

	Group 3
Transitional cost per entity (\$)	45,050
Ongoing cost per entity (\$)	36,950
Transitional cost (\$m)	205.20
Transitional cost by 10 (\$m)	20.52
Ongoing cost (\$m)	168.31
<b>Total compliance cost (\$m)</b>	<b>188.83</b>

43 Reducing the financi...~<https://treasury.gov.au/small-business/frt/factsheet>

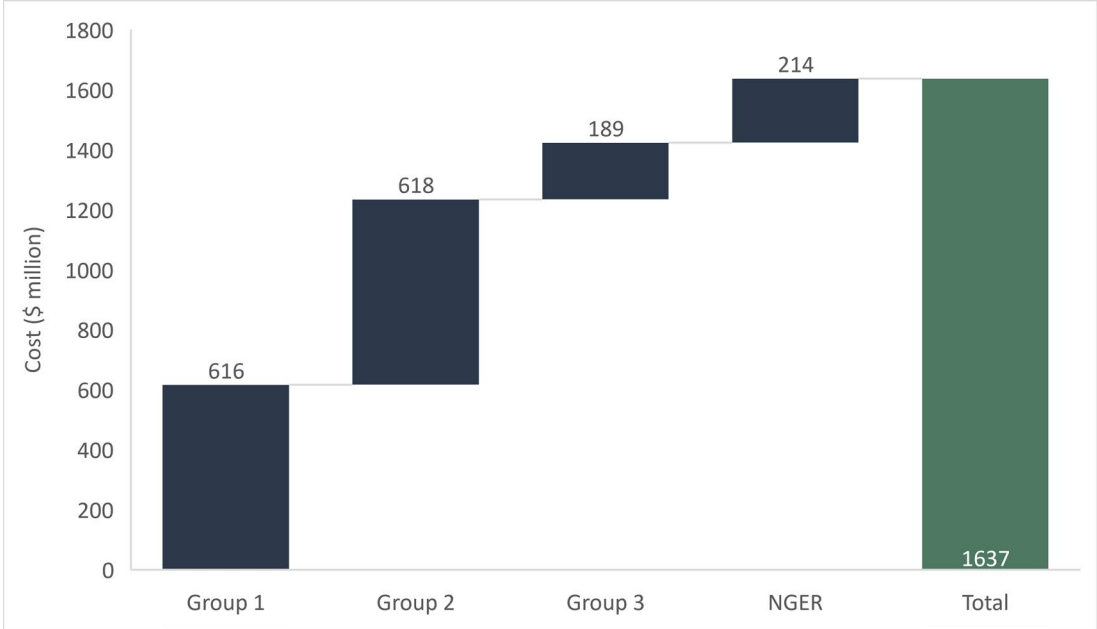
As seen below, there is an expected compliance burden of \$1,636.69 million per year for option 1 – largely driven by Groups 1 and 2 who are compelled to implement and maintain new systems to increase transparency in the market.

**Table 11: Total compliance costs across groups under Option 1**

	Group 1	Group 2	Group 3	NGER entities
Transitional cost	952.71	755.89	205.20	331.14
Transitional cost by 10	95.27	75.59	20.52	33.11
Ongoing costs	520.52	412.99	168.31	180.93
<b>Total compliance cost</b>	<b>615.79</b>	<b>618.03</b>	<b>188.83</b>	<b>214.04</b>

Source: Treasury projections

**Chart 3: Aggregate compliance burden for Option 1**



Source: Treasury analysis

**Option 1a: Narrower coverage with Group 3 only required to report if there are material climate risks and a specific threshold for asset owners**

In this option, we expect that the numbers of disclosing entities in Group 3 would be significantly lower compared with Option 1. Group 1 and Group 2 numbers will be consistent with Option 1 (i.e Group 1 will capture, at a minimum, 729 entities, Group 2 will capture, at a minimum, 755 entities). We assume 5 per cent of companies in this group have material climate risks that they would be compelled to disclose against in accordance with the Australian standards. This brings the number of Group 3 entities to 278.

Under Option 1a we expect the costs for Group 1, 2 and NGER entities to remain the same at \$615.8 million, \$618.0 million and \$214.1 million respectively.

We assume that only 5 per cent of Group 3 companies (278 entities) have material climate risk and would be required to report under Option 1a. Costs for Group 3 have been discounted by 30 per cent as voluntary disclosures are expected to be less detailed than the others.

At a median disclosing cost of \$45,050 and an expected long run reporting cost of \$36,950 we expect costs to be as outlined in Table 12.

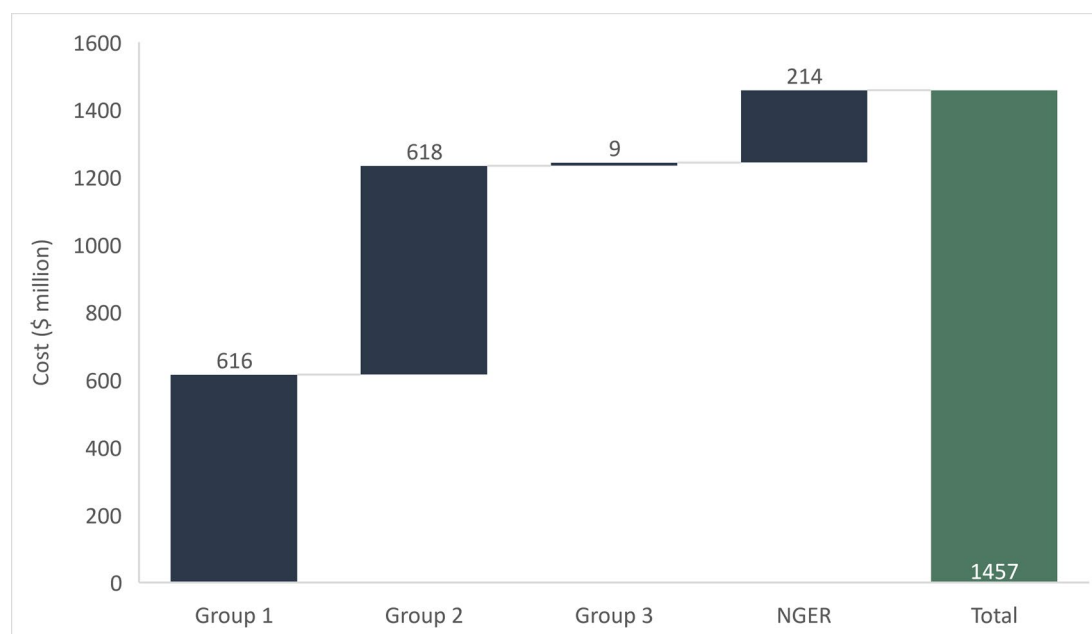
**Table 12: Adjusted compliance cost for Group 3**

Cost	Total (\$m) (228 entities)
Transitional costs	10.26
Transitional costs by 10	1.03
Ongoing cost	8.42
<b>Total compliance cost for Group 3</b>	<b>9.44</b>

Source: Treasury projections

As seen below in Chart 4, this option reduces costs for Group 3, with the total compliance burden of option 1a falling to \$1,457.3 million. Although this option reduces the regulatory burden for entities that are not captured in Groups 1 and 2, in some cases, Group 1 and Group 2 entities could ask such entities to provide their scope 1, 2 and 3 emissions to inform their disclosures.

**Chart 4: Aggregate compliance burden Option 1a**



Source: Treasury analysis

### Option 1b: Narrower coverage and changes to assurance framework

We have assumed the number of entities covered under Option 1b to be consistent with that of Option 1a, i.e. 729 entities in Group 1, 755 entities in Group 2 and 278 entities in Group 3.

We expect the same cost for Group 3 as they are already expected to have limited assurance. We make adjustments to the cost of assurance to the limited level for Groups 1, 2 and NGER reporters.

**Table 13: Total cost per entity under option 1b**

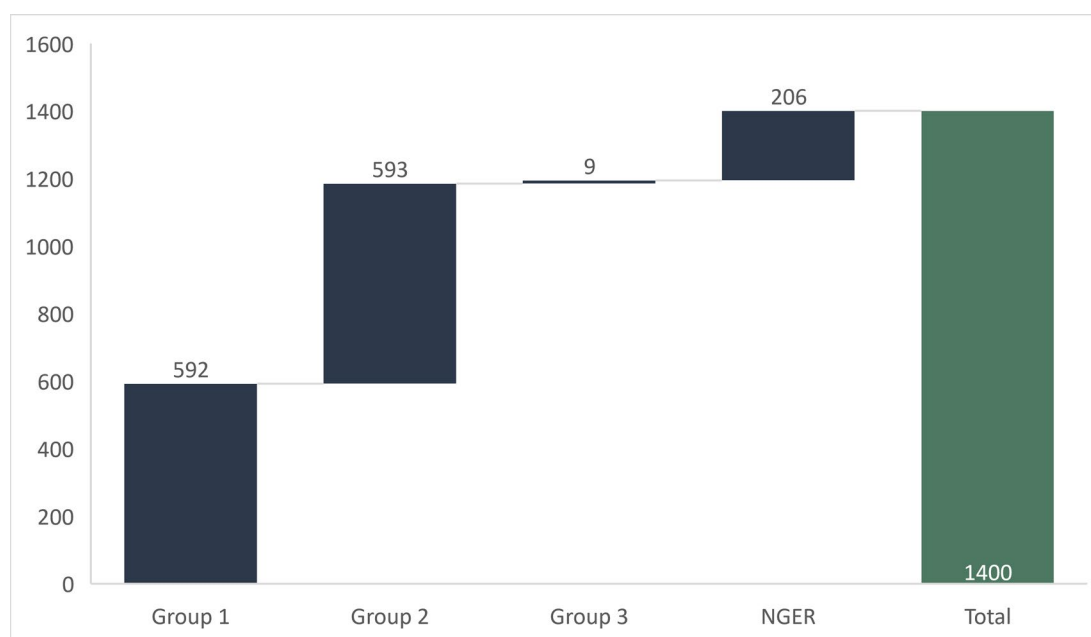
Activity	Transitional cost (\$)	Ongoing cost (\$)
Familiarisation and education costs	116,960	0
Legal review	10,472	7,854
Systems changes	245,000	0
Data collection	245,000	242,550
Scenario analysis	245,000	161,700

Activity	Transitional cost (\$)	Ongoing cost (\$)
Scope 3 modelling	245,000	161,700
Preparation of climate report	149,600	48,960
Assurance	49,815	49,815
<b>Total</b>	<b>1,306,847</b>	<b>681,154</b>

Source: Treasury projections

This leads to lower ongoing assurance costs as seen in the table, reducing the overall compliance costs in total for Groups 1, 2 and NGER reporters to \$591.83 million, \$593.20 million and \$205.72 million respectively. This would reduce the total compliance burden to \$1400.19 million (Chart 5).

**Chart 5: Aggregate compliance burden for Option 1b**



Source: Treasury analysis

## Mitigation efforts

Where possible, Treasury has made efforts to mitigate regulatory costs through leveraging existing structures, introducing other tools such as modified liability and phasing in differently sized groups in order to give time for the market.

### Leverage existing frameworks & legislative structures

Feedback from consultation suggested leveraging existing structures and building on existing frameworks to minimise implementation costs. As discussed earlier, the majority of the ASX200 are voluntarily disclosing climate risk in line with the TCFD. The proposal to implement a mandatory standard that is largely aligned with the ISSB means additional requirements will be based on existing frameworks since the ISSB builds off the TCFD foundations.

Legislative requirements will be designed to leverage existing definitions and obligations in the Corporations Act and NGER Act to increase clarity and simplify implementation as far as possible.

### Interoperability across jurisdictions

To reduce compliance costs for preparers operating in multiple jurisdictions, a mandatory disclosure regime that is internationally recognised is key. Alignment with the ISSB standards was almost universally supported by stakeholders during the discovery round of consultation. The ISSB has





worked to maximise interoperability with the European Sustainability Reporting Standards (ESRS) and the GRI standards.

### Modified liability framework

Concerns were expressed in consultation about liability settings. Stakeholders primarily raised issues around the applicability and operation of the current liability framework to forward looking statements. Reporters and some advisers noted forward-looking statements would require positions to be taken on inherently uncertain matters and thus leave company directors open to liability for misleading and deceptive conduct. Furthermore, concerns were expressed regarding Australia's class actions regime and the heightened scrutiny around climate and sustainability claims.

Other submissions commented that concerns about forward looking statements were overstated and that the reasonable grounds threshold was sufficiently flexible to account for the inherent uncertainty surrounding forward looking statements. As such, directors would be unlikely to be exposed to successful litigation and that modification of liability settings was unnecessary and undesirable.

To balance these competing views, Treasury proposes a modified liability framework for the first 3 years of reporting. 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. Relief provided in this way would encourage best-practice disclosures while assuaging concerns in areas of the disclosure regime that are more uncertain.

### Proportionality

This policy has considered circumstances for smaller companies that may not necessarily have the resources or in-house capability to confidently disclose climate risk. In the first instance, smaller companies will be phased in to ensure they can observe the market as disclosures develop. They will also be encouraged to voluntarily disclose earlier and take advantage of the modified liability framework. Similarly, smaller companies will be required to disclose only information that is available without undue cost or effort to reduce the regulatory burden. As a result of these considerations, Treasury has decided to implement an option that does not mandate climate-risk disclosures for all Group 3 entities but only for those with material climate-related risks and opportunities.

### Phasing

In response to the discovery consultation, 71% of 194 submissions agreed the Government should take a phased approach to coverage over time. A three-phased approach is proposed, starting with a relatively limited group of very large entities that expands after two years to apply to progressively smaller entities. Allowing smaller entities more lead time before they are subject to the mandatory requirements enables them to build the capability and skills required to meet their obligations.

The reform is also likely to increase the level of demand for professional services. Progressively expanding coverage over time should mitigate the risk of supply shortages and associated price increases in these service areas (particularly audit and assurance), by allowing sufficient time for the market to attract and grow the resourcing, capacity and expertise needed to meet this increased demand.

## Approximate regulatory burden estimate

Table 14: Annual regulatory costs (\$ million)

	Individuals	Business	Community organisations	Total change in cost
Status quo	\$0	\$249.99	\$0	\$0
Option 1	\$0	\$1,636.69	\$0	\$1,386.70
Option 1a	\$0	\$1,457.30	\$0	\$1,207.31
Option 1b	\$0	\$1,400.19	\$0	\$1,150.20

As there are compliance costs associated with abiding by the status quo, the approximate regulatory burden is calculated by deducting the compliance cost for status quo from each option. These costings are approximate only, and do not account for a number of unquantifiable costs of the status quo, such as a higher risk premium for investors, a higher cost of capital for companies and less efficient capital allocation across the economy. Estimated costs of the status quo also do not account for circumstances where companies would need to meaningfully increase climate risk reporting activities in order to remain compliant with existing obligations under the *Corporations Act 2001* to report on 'material' risks.


The proposal of a 'comply or explain' element for Group 3 in Options 1a and 1b acknowledges the undue regulatory burden that would have been imposed on a group that is least resourced to handle the burden. Similarly, we have heard during consultation of the lack of capability in the assurance markets and propose reducing the requirement for 'reasonable' to 'limited' assurance to ensure the needs of stakeholders have been balanced against the needs for greater decision-useful information. As such we recommend Government adopt Option 1b, with the lowest regulatory burden that aligns with improving transparency in the markets and the Government's election commitment to improve this through mandating climate-related financial disclosures.

### Flow on effects

We expect there to be a substantial flow on impact on the professional services and consulting industry as a result of these reforms. The increased compliance requirements for reporting entities will create benefits for service providers but also act as an impetus for developing this skills market and sustainability related jobs. Given this policy represents an innovation in financial reporting, we also expect there would be increased demand for sustainability assurance and auditing skills and capability in the market. In the short-term as supply of these skills catches up, prices for these services, from modelling, data collection, auditing and legal services are expected to rise. As seen in several surveys overseas and in submissions, these skills are generally outsourced in the short-term, causing higher profits for these service providers who have been purposefully recruiting professionals with these skills.<sup>44</sup>

Treasury received a number of submissions that noted the work underway by some academic institutions in meeting this shortfall in the supply of skills. The gap between demand and supply of these skills is expected to close slowly over the medium-term. In the long-term, we expect that the market for these skills will reach an equilibrium with many companies internalising these costs and developing models in-house as a way to reduce costs to external consultants and as more of these skills become available in the market. This is an assumption we have included in our analysis. In this manner, reporting entities will become more self-sufficient at managing their climate risk, reducing uncertainty for investors and potentially lowering their cost of capital. In the long-run, climate risk will

44 Big four accounting ...~<https://www.afr.com/companies/energy/big-four-accounting-firms-rush-to-join-sustainability-trend-20210901-p58nvm>



decrease across the Australian economy, entrenching Australia’s reputation as an attractive destination of capital.

# Consultation

The proposed mandatory climate disclosure regime is the result of extensive consultation with consumer groups, industry participants, peak bodies, academia and regulators. Treasury has undergone an extensive consultation process and consulted the public via:

## Discovery Consultation

Treasury released a consultation paper (Discovery CP) in December 2022 seeking initial views on key considerations for the design and implementation of standardised, internationally-aligned requirements for disclosure of climate-related financial risks and opportunities.

194 submissions were received. 181 of these were public submissions, with an additional 13 confidential submissions. Non-confidential submissions were published on Treasury's website<sup>45</sup>.

Treasury also hosted five industry roundtables with approximately 55 stakeholders, comprising superannuation funds, general insurers, banks, investor groups and industry associations from a wide range of sectors.

## What we heard

Stakeholders were almost universally supportive of the Government mandating climate risk disclosures. Feedback received from various sectors emphasised:

- The need for Australian and international standards to align, with appropriate adjustments to account for the Australian context.
- That the more challenging aspects of reporting content are disclosure of Scope 3 emissions and scenario analysis, with a need for supporting information and guidance to help companies to make quality disclosures.
- That requirements should apply to both large listed and unlisted entities and financial institutions, with coverage expanding over time.
- That reporting and assurance requirements should be phased in over a pre-determined and well-communicated timeframe, including allowing sufficient time following release of the final climate disclosure standards before the requirements come into force.
- That close consideration needs to be given to modifying existing liability settings related to forward-looking statements.

## Design Consultation

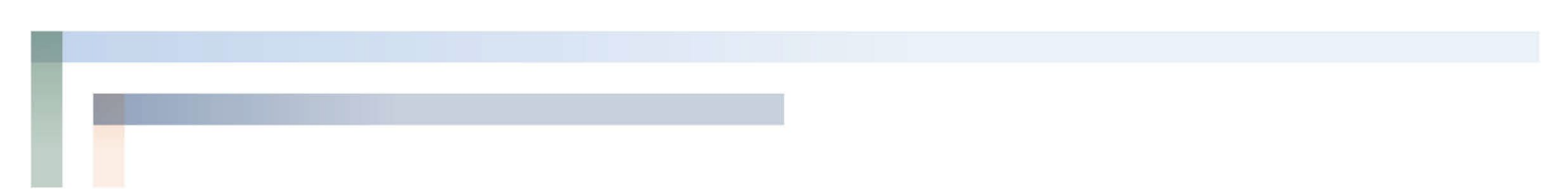
A second consultation paper (Design CP), informed by the views of the first consultation, was released in June 2023. That paper outlined proposals for the design of a mandatory climate disclosure regime, particularly seeking views on the proposed positions relating to coverage, content, framework and enforcement of the requirements.

146 submissions were received. 138 of these were public submissions, with an additional 8 confidential submissions. Non-confidential submissions will be published on Treasury's Consultation page.

During the second consultation period, three information sessions followed by a question and answer session were held. These invited interested parties to pose questions and express views on the

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<sup>45</sup> <https://treasury.gov.au/consultation/c2022-314397>



positions posed in the consultation paper. Each session had approximately 100 attendees from a range of interested stakeholders.

Outside consultation, Treasury has maintained contact with ASIC and other relevant government agencies such as DCCEE, Department of Finance, APRA and the CER. Treasury has also held numerous bilateral meetings with industry participants, peak bodies and law firms.

### What we heard

Stakeholders continued to express support for mandated climate risk disclosures, noting it struck a fine balance between ambition and coverage. Feedback received in the second round of consultation indicated:

- The regulatory burden on entities proposed to be included in Group 3 would be excessive compared to the benefit to be obtained from their inclusion, and as a result, requested an increased threshold or lighter touch reporting requirements.
- Size thresholds proposed would not be applicable to some financial institutions, for example in the superannuation industry, and specific thresholds may be needed for asset owners to give effect to the Government's policy intent to cover financial institutions.
- That entities are concerned around the availability of data to accurately report Scope 3 emissions, suggesting further guidance be provided if the requirement is not removed.
- That clarification and guidance should be provided regarding the specific location of reporting, the use of cross references and the timing of reporting.
- That there continues to be concern around the capacity and maturity of the Australian assurance sector and that requirements for reasonable assurance should only be introduced once consistent accounting standards are mandated and data quality standards are achieved.
- That close consideration needs to be given to the specific drafting of the requirements and any modifications to liability to ensure there are no unintended consequences.

### Early Outreach

A stakeholder engagement strategy was developed alongside the development of the first consultation paper, in line with the *Treasury Stakeholder Engagement Strategy*. This helped to categorise potential stakeholders, based on interest and influence, into groups used to create roundtables with balanced and meaningful dialogue.

An email was circulated to stakeholders identified as potentially interested in this consultation prior to consultation. Stakeholders ranged from potential reporting entities, regulators, assurance providers and investor/consumer representatives. Stakeholders were notified of the impending consultation and Treasury's intention to conduct roundtable discussions. In return, several groups reached out for informal consultation prior to the start of the consultation period to gain a better understanding of how to prepare for consultation and their submissions.

### Consultation Period

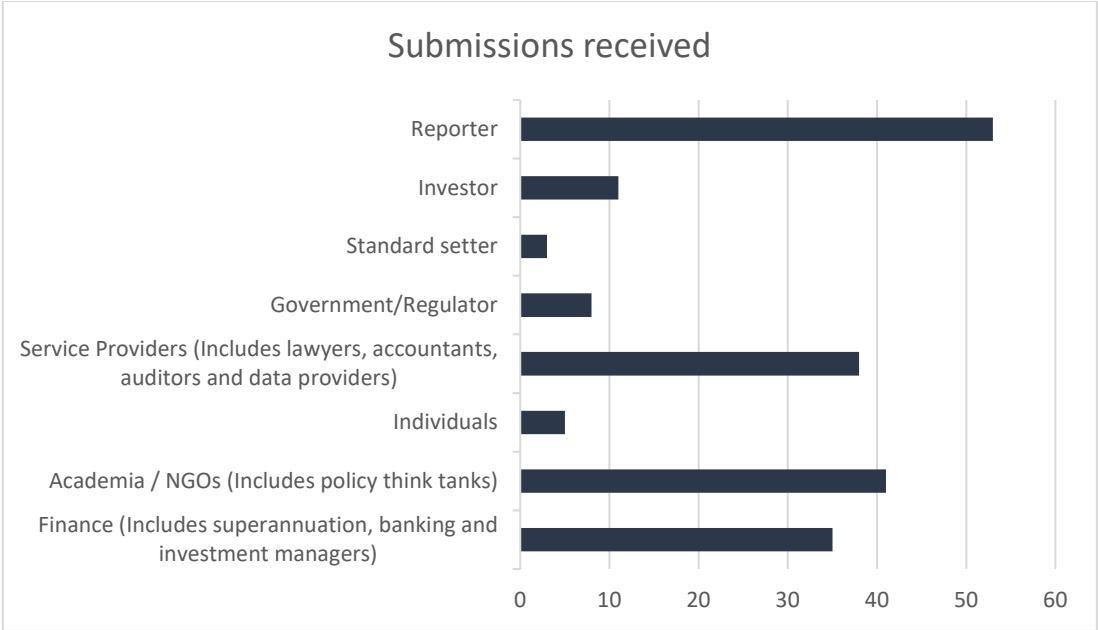
The Consultation Papers were published online via the Treasury website. The Discovery CP and Design CP were open for comment between 12 December 2022 – 17 February 2023 and 27 June 2023 – 21 July 2023, respectively. Extensions were provided to a number of stakeholders in both consultations, to allow additional time to make a written submission.

Treasury conducted digital promotion activities to inform stakeholders and the public about the consultation period, including:

- Media releases from the Treasurer to launch both public consultations
- Email updates to Stakeholders
- Social media posts on Treasury channels

The Discovery CP received a total of 194 written submissions including from the finance sector, academia, service providers, regulators, investors and reporters (Chart 6).

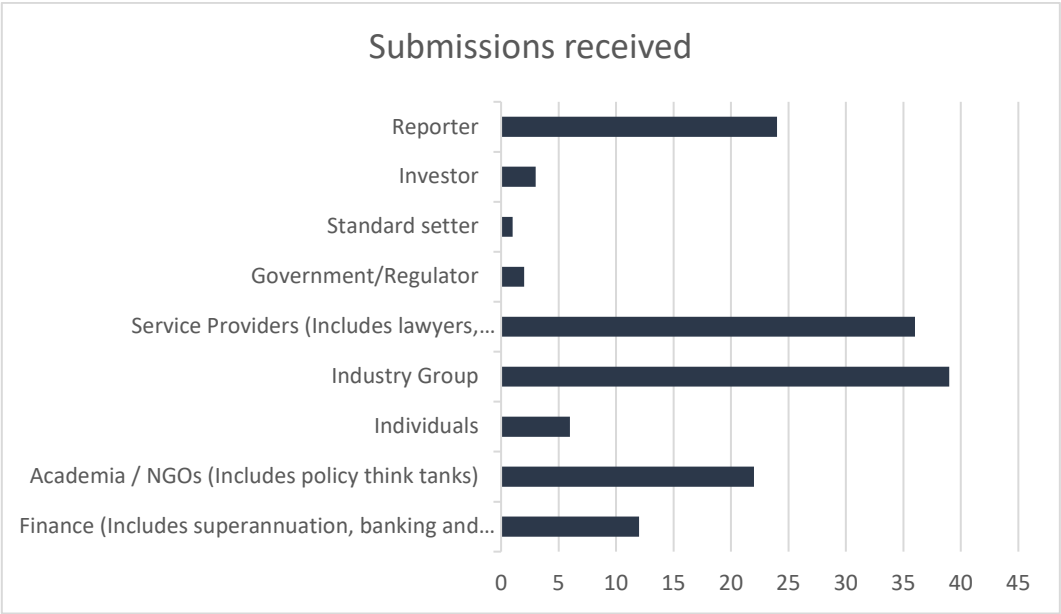
**Chart 6: Distribution of written submissions in Discovery CP by stakeholder group**



Source: Treasury analysis

The Design CP received a total of 145 written submissions from a similar range of stakeholders. 63 per cent of responses came from stakeholders who had made a submission to the Discovery CP (Chart 7).

**Chart 7: Distribution of written submissions in Design CP by stakeholder group**



Source: Treasury analysis

## Industry Roundtables

Treasury held a series of 5 Industry Roundtables during the Discovery consultation period. Approximately 55 stakeholders were invited to provide feedback on the proposal ask questions.

Invitees included:

- Superannuation funds
- General insurers
- Banks
- Australian financial services licensees
- Investor groups
- Industry associations

## Question and Answer Sessions

During the Design consultation period, Treasury held a series of 3 Question and Answer Sessions with approximately 100 attendees per session. This allowed stakeholders the opportunity to ask questions related to the specific proposed design positions for the regime. Attendees included:

- Australian financial services licensees
- Investor groups
- Reporters under the proposed regime
- Industry associations
- Regulators

## Status of the IA at each major decision point.

Table 15: Impact analysis at each major decision point

Decision point	Timeframe	Status of the IA
Government Announcement	May 2022	Undeveloped
Funding request	October 2022	Undeveloped
Authority to consult	November 2022	Discussed with OIA the need for an IA, ruling out the need for preliminary assessment.
Discovery consultation	February 2023	Begin collating data for cost-benefit analysis in IA. Discovery consultation included a question on broad cost-benefits of implementation. Quantification encouraged.
Design consultation	June 2023	Discussed drafting process with OIA and requirements for early assessment. Stakeholders asked for quantified cost-benefits in information sessions and bilateral meetings.
Cabinet submission drafting	July 2023	Early assessment process not pursued due to time constraints. Several drafts of IA sent to OIA for comments.
Cabinet submission Draft exposed	August 2023	1st pass assessment completed. Comments noted and addressed.
Cabinet submission	September 2023	2nd pass assessment presented to OIA.

# Option selection

## Options considered

Treasury considered the impact of allowing the status quo to continue. Under this option, the market would decide how Australian firms should disclose their climate-related financial risks. In the absence of mandatory disclosure, Australia would have to rely on further guidance by ASIC, supported by obligations imposed by the Corporations Act. Evidence to date suggests that this approach has been somewhat successful in increasing the number of firms disclosing climate-related financial risks,<sup>46</sup> however has not produced consistent and high-quality disclosures that are useful to investors. Additionally, shareholder activism could lead to voluntary disclosure of climate change risks. However, this strategy will not achieve the standardisation that many users of general-purpose financial reports demand, while being an avenue that unfairly favours larger corporates who have more resources to voluntarily disclose.

Treasury also considered three implementation options during the policy development process. As outlined in the sections above, these options balanced four key design criteria:

- The appropriate coverage of entities that would be captured by these requirements.
- The reporting content of these disclosures
- The assurance framework
- Appropriate timeframes for introducing mandatory disclosures.

Treasury considered Option 1 to deliver clear improvements in the quantity, quality and comparability of disclosures and consulted on stakeholder views for implementing this option between 27 June 2023 and 21 July 2023.

A number of stakeholders highlighted their main concern with proposed policy was the significant regulatory burden it would impose on smaller entities in Group 3 who are expected to have relatively minor climate-related risks. A significant proportion of audit and assurance industry stakeholders expressed concern regarding the proposed timeframes for phasing in and scaling up assurance requirements in Treasury's design consultation. Stakeholders noted that the industry was not sufficiently mature, and that service providers face substantial challenges in mobilising and upskilling the required workforce.

## Recommended option


**Treasury recommends Government implement Option 1b.** In our view, if implemented, Option 1b achieves the Government's objective of reducing information asymmetry between investors and firms and establishes a standardized framework for reporting. This will improve the comparability, quality, and timeliness of disclosures and enhances the proportionality of the reforms. Australian reporting entities will be able to capitalise on the opportunity to improve climate risk management to align with international best practice. In such an ecosystem, regulators will have the certainty to enforce compliance against misleading claims and greenwashing.

Compared with Option 1 and Option 1a, Option 1b strikes the appropriate balance between the costs and benefits of these reforms. Under Option 1b, Group 3 entity reporting would be limited to only those with material climate risks, substantially reduces the regulatory burden. Given entities are already required to report material climate risks under their Corporations Act obligations, the need to complete a materiality assessment from 2027-28 should also not impose additional regulatory burden. This consideration should already be a part of their financial reporting. Compared with status quo, this option also provides Australian companies with a framework for reporting, improving comparability of decision-useful information.

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<sup>46</sup> Page 6 -ACSI – Promises, Pathways, Performance – Climate Reporting in the ASX200 (2023).





For the assurance framework, Option 1b mandates reasonable assurance should be achieved by 2030, however does not mandate a pathway. We consider this approach to be appropriate as it provides the AUASB with the flexibility to develop a roadmap to full assurance, ensuring that consideration is given to the international standard on sustainability assurance and the development of market capability.

As illustrated in Table 12 above, Option 1b imposes the least regulatory burden compared with other options for implementation.

# Implementation and review

## Implementation

Primary legislation changes will be required to implement the preferred policy option. In particular, primary legislation will be needed to specify the groups of entities that these disclosures apply to, when entities need to commence disclosing their climate risks as well as reporting location. Legislation will be amended to apply a modified liability regime for climate-related financial disclosures. It is expected that ASIC will issue updated regulatory guidance to assist entities captured by these reforms.

Responsibility for setting the Australian-specific sustainability standard lies with the AASB and for setting the Australian specific auditing standard with the AUASB. Treasury will collaborate with both agencies to ensure the Australian Sustainability Standards capture in detail all requirements entities that will be subject to mandatory climate reporting. Further, we expect ASIC to play a crucial role in the enforcement of this policy. Ongoing responsibility for the operation and management of this policy will be jointly held by Treasury, ASIC and AASB/AUASB.

Subject to legislation being enacted by the Parliament and receiving Royal Assent by end of June 2024, we anticipate mandatory climate-related financial disclosures to come into force for financial years commencing on or after 1 July 2024.

## Risks to implementation

Some implementation challenges and actions planned to alleviate these are discussed below:

- **Poor compliance:** If entities consider the regulatory regime to be imposing too heavy a burden on their resources, it could lead to non-compliance and/or poor-quality disclosure. Similarly, if entities do not consider this information to be valuable to their investors, the effort put into disclosing could be low. This would result in the regime being treated the same as status quo, where although there is already a legal obligation to disclosing climate risks if material, compliance is low and seen as voluntary.
  - To support implementation, the AASB, ASIC and APRA will undertake stakeholder engagement to improve understanding and educate businesses on their obligations. The phased-in approach will also assist implementation, with smaller entities having time to develop capability and understanding. Further, this risk will also be mitigated somewhat by market forces that will bear on those entities who do poor quality disclosures or who do not disclose given increased focus within international capital markets on sustainability reporting.
- **Limited professional capability:** Capability and capacity in the professional services industry for sustainability reporting is limited. This type of reporting is a relatively new practice, and these reforms would place additional demands on the industry, for example in assuring various disclosure requirements (i.e. scope 3 emissions). The Government will monitor whether the professional services industry is sufficiently upskilling and developing in order to implement these reforms.
- **Limited understanding of various elements of climate reporting:** As noted above, sustainability reporting is relatively new, and most Australian businesses will need to invest resources in understanding the various elements of climate reporting and developing systems to collect and analyse data to make effective disclosures. Related to this is also the lack of available data that would make it easier for companies to make these disclosures.

- To mitigate this risk, the Government is resourcing AASB, ASIC as well as APRA to assist Australian businesses understand their obligations and work closely with them to develop the necessary guidance. The AASB, ASIC and APRA intend to undertake an extensive program of targeted education and communication to raise awareness and develop a resource base for stakeholders. The Government, through its sustainable finance strategy, is also considering how it can support businesses by exploring viable solutions to data challenge.
- **Timeframes:** A number of stakeholders have expressed their concern regarding the implementation timeframes associated with this reform. Stakeholders contend that if there is insufficient time between when the AASB releases the final standard and companies have to have processes and systems in place to analyse their climate risks and opportunities.
  - Treasury is sensitive to these concerns. In our view, given many Group 1 entities already report their climate risks and opportunities against an international framework, this is unlikely to need large scale changes to their systems. Further, the Australian specific standards will be closely aligned to ISSB standards so it could be argued that Australian businesses will have at least a preliminary understanding of their reporting obligations.

## Evaluation

The objective of this policy reform is to reduce information asymmetries between investors and Australian firms, improving the depth and breadth of decision-useful information on climate-related risks and opportunities to enable better and more efficient capital allocation. Evaluating success of this policy is therefore hard to truly measure.

One of the main ways of evaluating the success of these reforms is through ASIC's ongoing supervision of quality of climate-related financial disclosures. ASIC has responsibility for the supervision, investigation and enforcement of the financial reporting and auditing requirements of the Corporations Act. As part of this function, ASIC reviews the annual and interim financial reports of a selection of listed companies and other significant entities to monitor compliance with the Corporations Act and Australian Accounting Standards. For example, ASIC conducted a review of 60 ASX 300 listed companies, 25 Initial Public Offering (IPO) prospectuses and across 15,000 reports in 2018 to assess their quality of climate-related financial disclosures.

Given climate-related financial disclosures will be mandated in the Corporations Act, the Government will provide ASIC with additional resources to:

- Review and publicly report on the observed standard of climate disclosures to be made under Chapter 2M of the Corporations Act and the quality of assurance work.
- Review market announcements made by listed entities and assess the market impact of key announcements.
- Review selected corporate finance transactions for appropriate disclosures that would have informed investor decision making.

ASIC will also be provided resources to update their external-facing forms to collect relevant data related to climate-related financial disclosures.

Given the ongoing interest in these reforms from the investor community, third-party reviews could also assist in canvassing the compliance and quality of disclosures. For example, the Australian Council of Superannuation Investors (ACSI) has published research in 2022 and 2023 that provided an overview of the state of climate-related disclosures in ASX200 entities.



## Review

A number of stakeholders emphasised the need for a Review of the regime. Treasury considers a legislative obligation to review the regime to be appropriate. Treasury proposes a review to be done by Treasury in 2028-29 with input from the Council of Financial Regulators (CFR) Working Group on Climate given the responsibilities of ongoing maintenance and enforcement lies across Treasury, AASB and ASIC.

While the terms of reference of the review will be settled closer to the date, we envision this review to be broad. The proposed review process will start after full coverage is achieved in 2029. While the parameters for the review have not been settled, Treasury considers there are a number of fundamental metrics that will enable the Government to measure the success of these reforms. These metrics will likely relate to the coverage of the disclosures, including the number of companies disclosing, the investor level of satisfaction with the quality of climate disclosures (through consultation, surveys and/or bilateral meetings).

The review would also examine the capability in the assurance market, given stakeholder feedback suggested this was an area that may be difficult to implement. The review could also conduct a deeper analysis of the available skills (assurance, scenario analysis, scope 3 modelling) through consultation and surveys. Such analysis could also reveal unintended consequences, particularly on 'smaller' businesses as these businesses have fewer resources but are still part of the value chain. The review could also consider how effective these disclosures have been for regulators. This could include monitoring greenwashing cases and through ongoing regulator supervisory, enforcement and compliance activities.

# Appendix A

## Estimated costs in other jurisdictions

Several jurisdictions have estimated a range of costs for the preparation of climate disclosures and the subsequent analysis of these disclosures by users of general-purpose financial reports. The section below discusses costs approximated by various jurisdictions to reporters and investors.

### United States

As part of the US SEC's climate disclosure rules, the SEC estimated the cost for Smaller Reporting Companies (SRC) and non-SRC registrants<sup>47</sup>.

**Table 1: SEC estimated costs for SRC and non-SRC registrants (\$USD)**

	Non SRC registrants	SRC registrants
<b>First year of compliance costs</b>	640,000	490,000
<b>Internal costs</b>	180,000	140,000
<b>Outside professional costs</b>	460,000	350,000
<b>Ongoing costs</b>	530,000	420,000
<b>Internal costs</b>	150,000	120,000
<b>Outside professional costs</b>	380,000	300,000

Source: US SEC

Several examples are highlighted by the SEC, with costs varying depending on the type of industry that was reporting, whether they had disclosed before and which standard(s) or framework(s) they had disclosed against. One submission provided costs for seven large cape firms across six different industries, with staffing requirements ranging from two to twenty full time equivalent employees, while others estimated the employee hours required ranged from 7,500 to 10,000 hours annually.

### UK

The 2021 'UK Impact assessment' on the proposed implementation of TCFD based mandatory disclosure broke down the costs to include; familiarisation costs, legal review, costs of collecting information from subsidiaries, costs to disclose against TCFD parts (Governance, Strategy, Risk Management and Metrics & Targets) and the costs for quality assurance. The total costs are estimated to be £190,500 in the first year and £138,950 in subsequent years with additional costs for subsidiaries<sup>48</sup>.

### New Zealand

In New Zealand, costings were in a range, brought forward from a global accounting firm and several large corporates<sup>49</sup>:

- GHG inventory and measurements: \$10,000 - \$50,000
- GHG assurance: \$30,000 - \$100,000
- Scenario Analysis: \$70,000 - \$150,000

47 <https://www.sec.gov/comments/s7-10-22/s71022-20130924-299962.pdf>

48 [https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/1055931/tcf-d-final-stage-ia.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1055931/tcf-d-final-stage-ia.pdf)

49 <https://www.treasury.govt.nz/sites/default/files/2021-05/ria-mfe-crfd-jul20.pdf>

- Advisory services: \$10,000 - \$20,000
- Investment data: \$10,000 - \$40,000
- Carbon analytics: \$6,500 per portfolio

The NZ Regulatory Impact Analysis highlights the uncertain nature (hence the range of numbers) of these calculations as being dependent on size of company and starting points in the disclosure journey.

A more recent 2022 survey by Environmental Resource Management (ERM) echoes the costs seen in previous studies, the ERM finds that companies that are preparing climate disclosures are spending on average \$539,000 annually<sup>50</sup>.

**Greenhouse gas (GHG) analysis and/or disclosures:** \$237,000 average annual cost for those reporting spend in this category.

**Climate scenario analysis and/or disclosure:** \$154,000 average annual cost for those reporting spend in this category.

**Internal climate risk management controls** (the costs related to integrating climate risk into business processes: \$148,000 average annual cost for those reporting spend in this category.

The ISSB received submissions that the factors that influenced disclosure costs depended on starting point in disclosure journey, company size, value chain complexity and location. Preparers mentioned that start-up costs to create and development climate governance systems and processes were high, but ongoing costs would decrease. Many submissions from emerging markets, developing economies and from smaller companies maintained that costs would be high for both implementation and ongoing costs due to a lack of available public goods, data and expertise. This echoes the sentiment in previous studies, suggesting that costs will be significant for smaller companies when adopting new accounting standards.

Many issues uncovered in the ISSB consultation mirrored issues during Treasury's consultation, particularly concerns about the large initial investment cost. Stakeholders pushed for certainty in timelines, scope and alignment to ensure costly initial investment was implemented once and once only. Similarly, there were concerns that small and medium enterprises (SMEs) would bear significant burden, whether through having to prepare disclosures with less available resources and capability, or through pressure upstream from bigger companies requiring SMEs to support their more complex disclosures.

Submissions during the design consultation estimated the costs to be as low as \$40,000 a year by smaller firms to more than a million for larger firms. In the modelling areas such as Scope 3 and Scenario analysis, costs ranged in the low hundreds of thousands to develop and maintain models. Lastly, in the assurance market submissions estimated costs from \$20,000 to \$150,000, depending on the level (limited vs reasonable) of assurance and the size of the entity. Another submission generalised the cost of reporting to be between 1 and 10 basis points of an entity's net consolidated assets.

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<sup>50</sup> SustainAbility Institute by ERM, Costs and Benefits of Climate-Related Disclosure Activities by Corporate Issuers and Institutional Investors, <https://www.sustainability.com/thinking/costs-and-benefits-of-climate-relateddisclosure-activities-by-corporate-issuers-and-institutional-investors/>.

# Appendix B

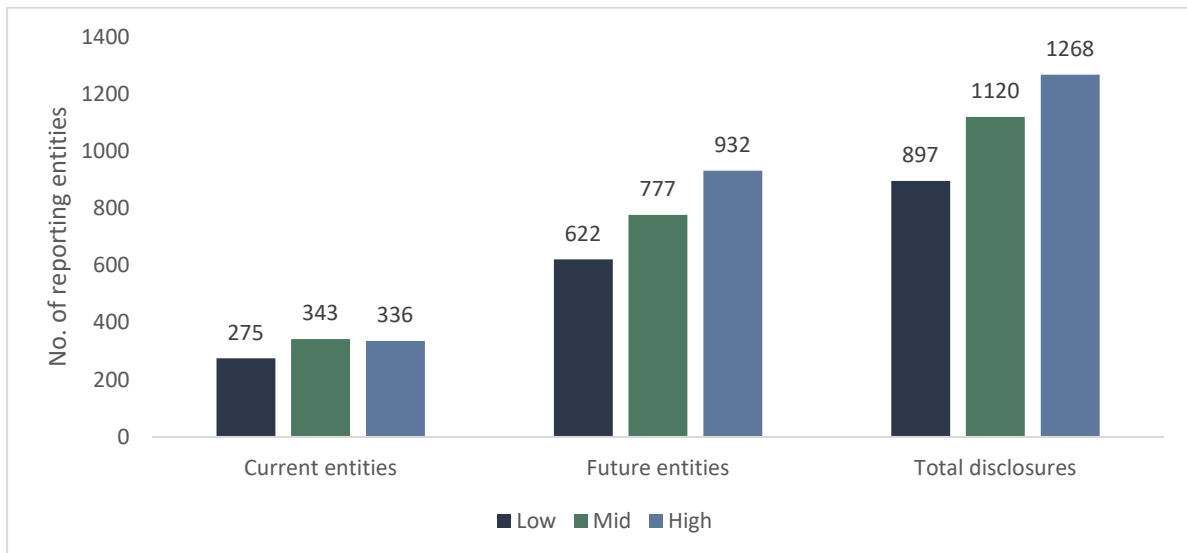
## Sensitivity analysis

Given the uncertainty in forecast cohorts that could be impacted by these reforms, it is appropriate to perform a sensitivity analysis for each option.

### Status quo

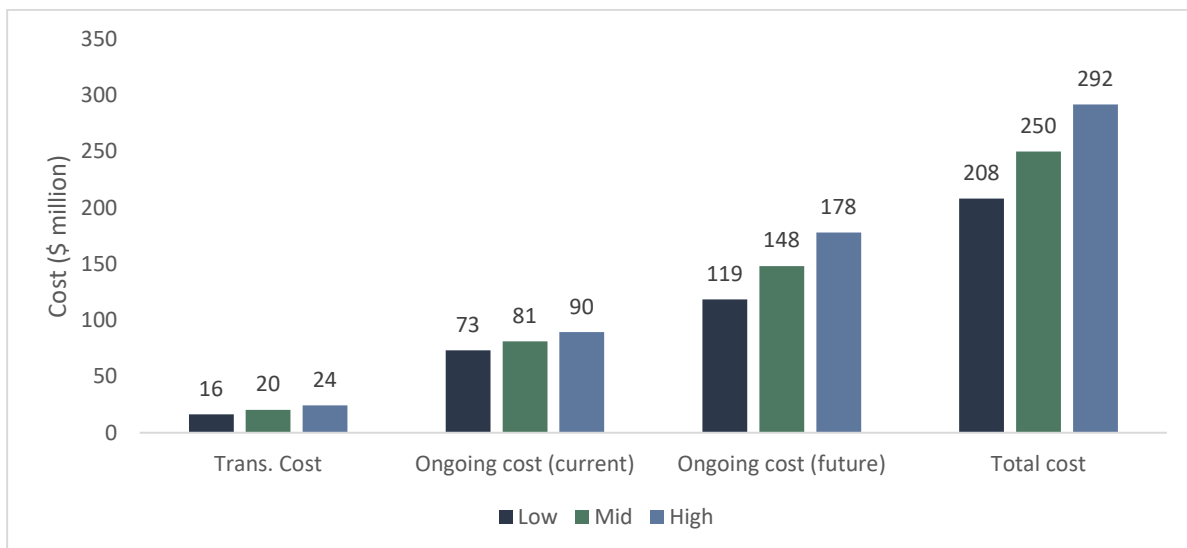
In the case of the status quo, there is uncertainty about both the current rate of voluntary disclosure and how many additional entities would disclose over the next decade without a regulatory imperative. We repeat the analysis above with an assumption that 10 per cent [fewer/more] entities are currently disclosing and 20 per cent [more/fewer] entities voluntarily disclose in the next 10 years. As seen below, there is a range of expected disclosing entities between 1,097 and 1,568 entities which results in costs incurred ranging from \$221 to \$314 million.

**Chart 1: Variance in forecast reporting entities for status quo**



Source: Treasury projections

**Chart 2: Variance in total compliance burden for status quo**

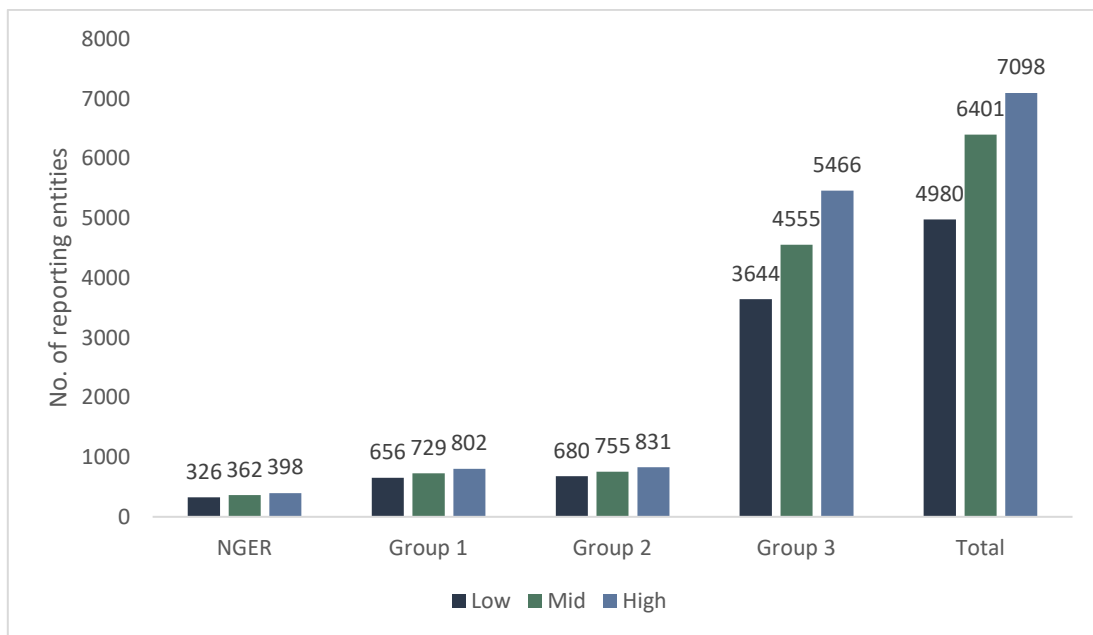


Source: Treasury projections

### Option 1: Design consultation policy

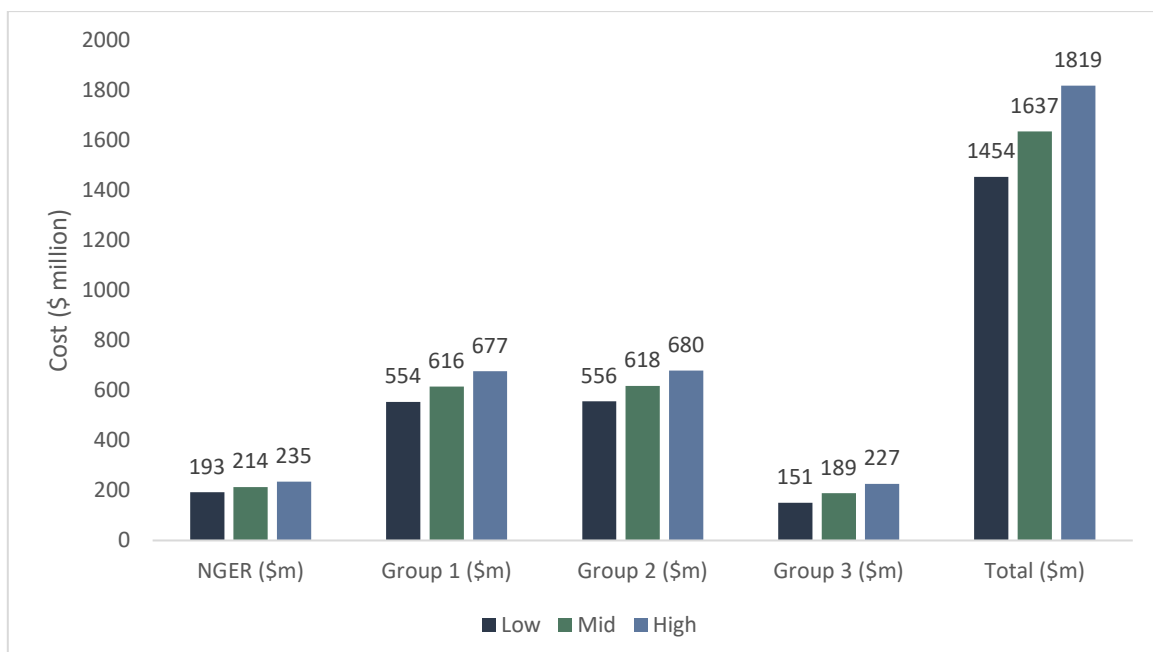
With option 1, we expect there to be some variance in forecasted numbers, particularly in Group 3 entities. With Group 1 and Group 2, we expect that publicly-listed companies will not vary as much as unlisted companies. Treasury expects 20% variance on either side for Group 3 entities and 10% on either side for Groups 1, 2 and NGER entities. There is increased uncertainty as an increase in Group 1 entities could decrease the number in Group 2, all other things being equal. However, a simultaneous decrease in Group 3 from increased revenue, assets and employee size could still increase Group 2. Therefore, we show a range for potential costs. In summary, we forecast a range of entities covered between 4980 to 7,098, accompanying compliance costs of between \$1,454 million and \$1,819 million.

**Chart 3: Variance in forecasted reporting entities for option 1**



Source: Treasury projections

**Chart 4: Variance in compliance burden for option 1**



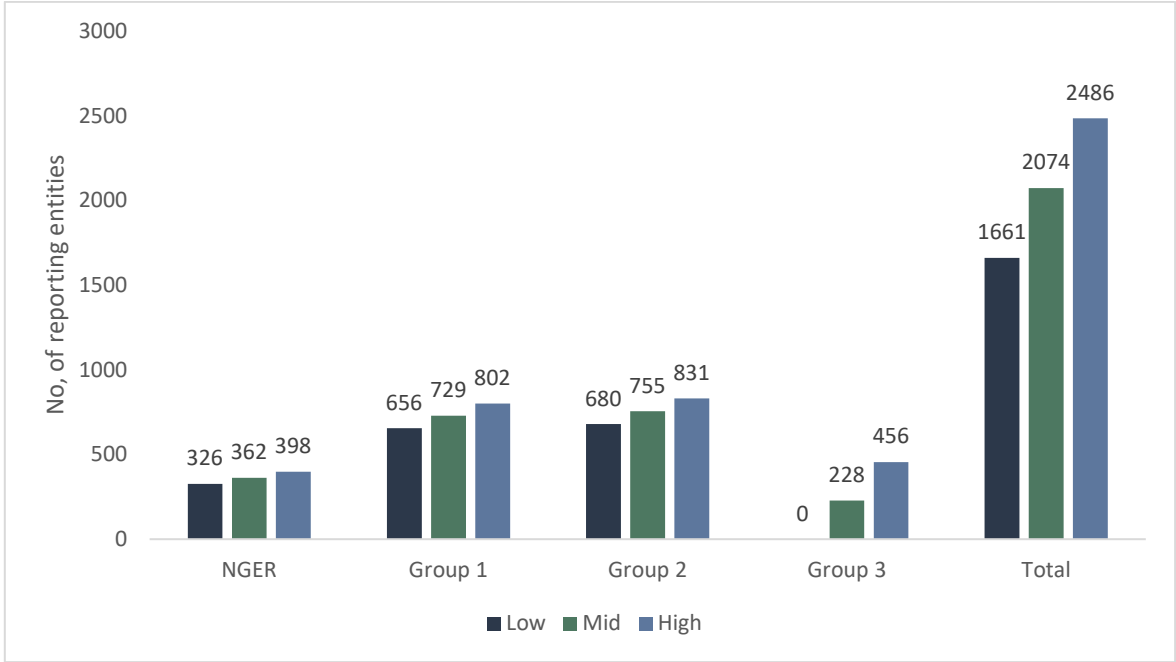
Source: Treasury projections



Option 1a: Narrower coverage with Group 3 only required to report if there are material climate risks

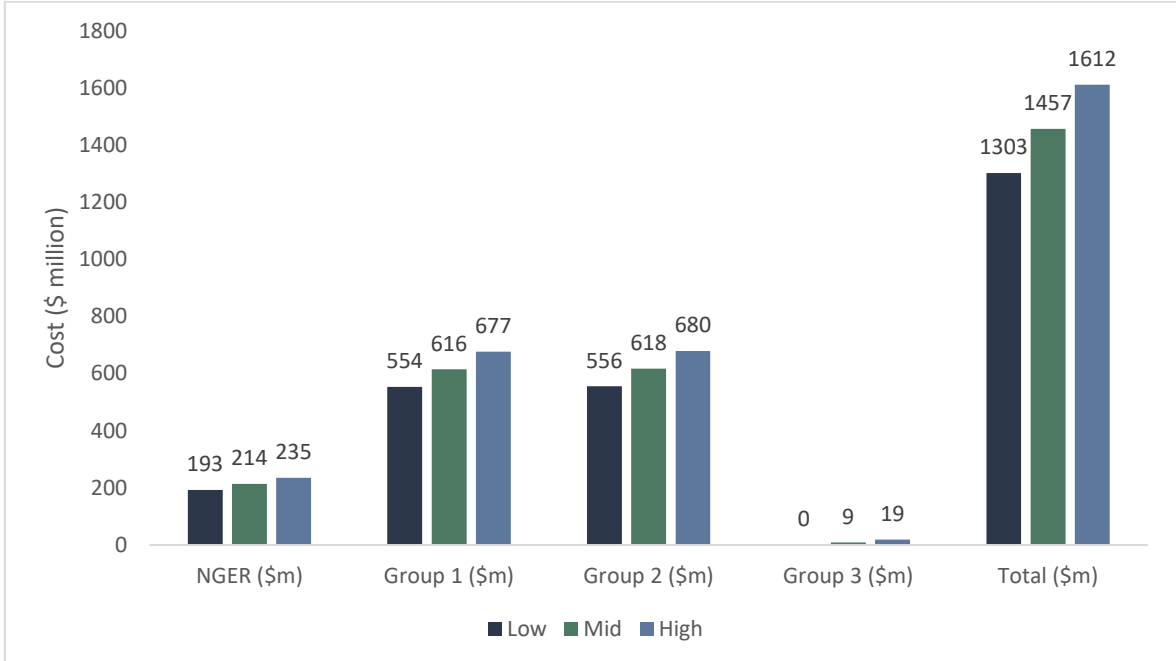
With option 1a, we expect there to be some variance in forecasted numbers, particularly in Group 3 entities. In this case, we show significant variance in Group 3 who may have material risk, while also accounting for those who may voluntarily taking up disclosure. This number could be as low as 0% and as high as double our initial assumption, given the increasingly fast uptake and demand of/for disclosures. In summary, we forecast a range of entities covered between 1,661 to 2486 accompanying compliance costs of between \$1,303 million and \$1,612 million.

Chart 5: Variance in forecast reporting entities for option 1a



Source: Treasury projections

Chart 6: Variance in compliance burden for option 1a

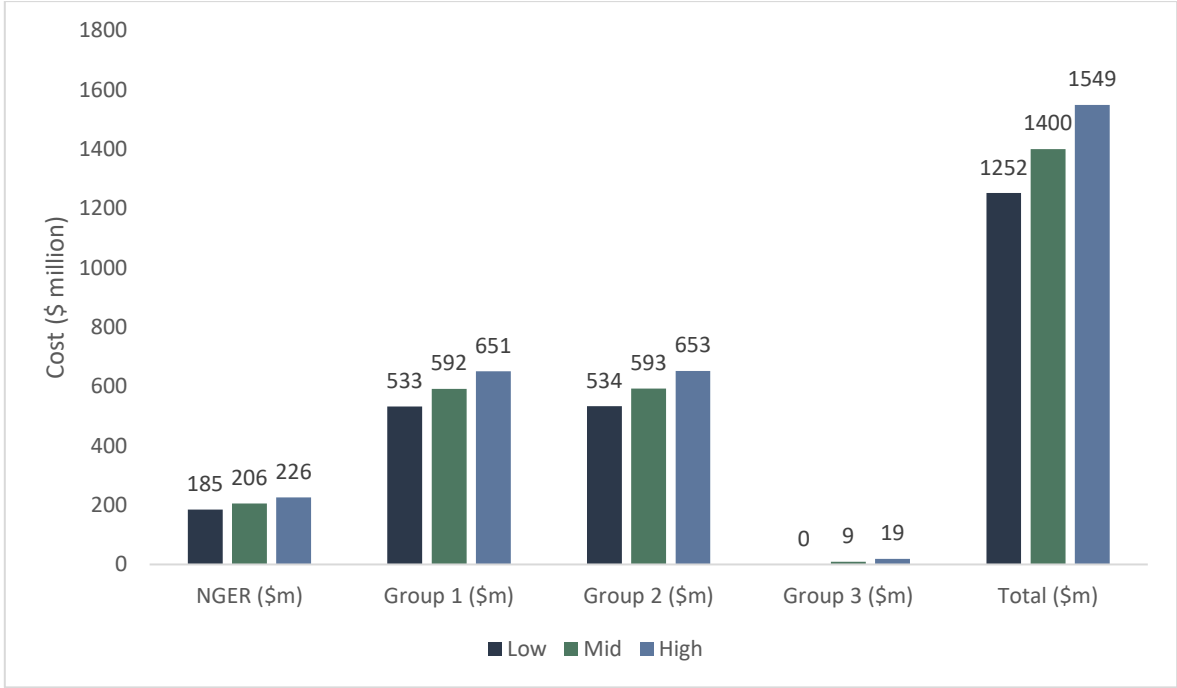


Source: Treasury projections

### Option 1b: Narrower coverage and changes to assurance frameworks

With option 1b, we match the assumptions for forecasted entities as in option 1a. There is still a variance in compliance burden due to the variance in forecasted entities. In summary, we forecast a range of entities covered between 1,661 to 2,486 (as in option 1a) accompanying compliance costs of between \$1,252 million and \$1,549 million.

**Chart 7: Variance in compliance burden for option 1b**



Source: Treasury projections