Governance Institute of Australia

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The Committee Secretary
Senate Economics Legislation Committee
Parliament House
CANBERRA ACT 2600

**RE: Treasury Laws Amendment (Financial Market Infrastructure and Other Measures) Bill 2024 (Bill)**

**Who we are**

Governance Institute of Australia (GIA) is a national membership association that advocates for a community of governance and risk management professionals, equipping over 8,000 members with the tools to drive better governance within their organisation. Our members have primary responsibility for developing and implementing governance frameworks in public listed, unlisted, and private companies, as well as the public sector and not-for-profit organisations. They have a thorough working knowledge of the operations of the markets and the needs of investors.

We regularly contribute to the formation of public policy through our interactions with Treasury, ASIC, APRA, ACCC, ASX, ACNC and the ATO. We are a founding member of the ASX Corporate Governance Council. We are also a member of ASIC's Business Advisory Committee and Registry Business Advisory Group , the ASX Business Committee and the ACNC Sector Users Group.

**Introductory comments**

Our members support a global approach to the development of sustainability reporting, particularly climate-related financial disclosure standards. They have also been active participants in the implementation of sustainability reporting standards in Australia.[1] Our members support the Bill in principle and are pleased to note that it has addressed many of the issues of concern noted in our Submission on the Exposure Draft and in previous Submissions.[2] However, our members remain concerned about the following aspects of the Bill:

**Summary of issues**

Our members key concerns with the Bill are:

- As currently drafted, the regulatory burden of the proposals on Group 3 entities is disproportionate to the benefits of requiring these entities to make climate-related financial disclosures, given many of them currently have no external reporting obligations. The reporting threshold should be

[1] See *Peak Australian Bodies Submission* to the International Sustainability Standards Board, 15 July 2022.
[2] See Submission Climate-related financial disclosure: exposure draft legislation, Governance Institute of Australia, 8 February 2024.

adjusted to $100M consolidated revenue with a corresponding adjustment to the consolidated gross assets threshold. Not-for-profits should also be excluded from the reporting requirements. There should also be a reduced disclosure regime for these entities given they are currently eligible to produce simplified financial disclosures. Assurance requirements should be appropriate for the size of these entities.

- While the proposed requirement for entities which have no material risks or opportunities to produce a climate statement to that effect is acceptable, to require an audit of that statement to be conducted imposes a significant and unjustified regulatory and cost burden on these entities as the auditor will need to form the view that the statement is correct for the reasons stated by the entity.
- There are continuing concerns about the use of the term 'sustainability report' in the Bill. This is likely to create confusion given many entities currently produce 'sustainability' reports which cover a broader range of issues than climate. While broader sustainability reporting is expected to be introduced over time, the first order issue is climate-related financial disclosure and the term used should make this clear. The term for the new report should be revised to 'climate report'. Alternatively, climate-related financial disclosures should be located within existing reports and cross referencing enabled, noting that the current ASIC instrument only permits cross-referencing in financial reports.[3]
- Our members remain concerned at the breadth of the Ministerial discretion in the proposed section 296A(5) giving the Minister power to require a sustainability report to include statements relating to 'financial matters concerning environmental sustainability' by legislative instrument. The Minister's ability to expand the regime should require industry consultation more expressly.
- Our members acknowledge that the Bill has addressed some of their concerns around the liability attached to the proposed regime. However, they consider there should be protection for climate disclosures extracted from the climate statement reproduced elsewhere, absent gross negligence or willful misconduct by an entity or its directors. They also recommend extending the limited immunity to entities in all Groups for the first three years of their reporting under the regime and clarifying that the dual lodgment relief provisions should also include climate reports.
- Our members remain concerned that there has been no adjustment to the continuous disclosure regime because of the interaction between periodic climate-related financial disclosures and the continuous-disclosure regime for ASX-listed companies. They continue to advocate that the most appropriate option for addressing these concerns would be to adapt the changes introduced during COVID-19 to the continuous disclosure regime.

Further details are set out below.

## 1. Scope of legislation and liability – Group 3 entities, not-for-profits

As we have consistently maintained in previous submissions, our members consider that the consolidated revenue threshold for Group 3 is too low.[4] They consider $100M consolidated revenue is a more appropriate threshold which would align the climate-related financial disclosure regime with other regimes with which entities are familiar including: the Payment Times Reporting Scheme, the Modern Slavery Act reporting requirements and the Corporate Tax Transparency Code. The consolidated gross assets threshold should also be appropriately adjusted.

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[3] See ASIC Instrument ASIC Corporations (Directors' Report Relief) Instrument 2016/188.

[4] See Submissions Climate-related financial disclosure: exposure draft legislation, Governance Institute of Australia, 8 February 2024, *Consultation paper - Climate-related financial disclosure June 2023*, Governance Institute of Australia, 28 July 2023 and *Climate-related financial disclosure – consultation paper*, Governance Institute of Australia, 24 February 2023.

One of the aims of aligning the legislative regime with International Standards is to 'support Australia's reputation as an attractive destination for international capital and help draw the investment required for the transition to net zero'.[5] If one of the chief aims of the regime is to provide information to investors to attract capital investment, our members question capturing entities of this size given their level of outside investment is likely to be low. They also question whether requiring these entities to make public disclosure of climate information or of the fact they have no 'material' climate risks is useful. Investors in these entities are generally 'close' to the entity and likely to have better access to information than investors in large listed entities or superannuation funds investing in listed companies.

We also note that some entities required to report under Chapter 2M which are impacted by the legislation are eligible to use the 'Simplified Disclosures' Tier 2 financial reporting framework which came into effect on 1 July 2022. Given the desire to leverage existing reporting frameworks our members maintain there should be a corresponding simplified climate-related financial disclosure regime for these entities to mirror the financial reporting regime with assurance requirements appropriate to their size.

**Statement - no material climate-related risks and opportunities and audit requirements**

Under proposed section 296B(1) the 'climate statement' for smaller in-scope entities which do not have material climate risks or opportunities is only a statement to that effect, as well as an explanation of how it reached this conclusion. The Explanatory Memorandum notes: 'To avoid doubt, where an entity's climate statement for the year is only a statement that the entity has no material climate risks or opportunities, this statement must also be audited' (paragraph 4.131). Our members consider this imposes a significant and unjustified regulatory and cost burden on these companies. It effectively imposes a requirement for an additional audit on a sector which is already under resource and cost constraints, noting that limited assurance will initially be required. An audit of this type of statement is not a 'tick and flick' exercise. Auditors will still need to enter an engagement with a client entity to 'audit' a statement which is governed by the auditing and assurance standards. The costs for an audit of the financial statements of a smaller entity are likely to be somewhere between $20,000 to $40,000. The requirement for an additional audit, even if only on a limited assurance basis initially increases the size of their annual audit fees. Given that many of these companies are likely to have few, if any outside investors, this is an unjustified expense.

**Governance Institute recommends**:
- The consolidated revenue threshold for Group 3 entities should be $100M to align with other reporting requirements applicable to these entities with a corresponding adjustment to the consolidated gross assets threshold.
- Excluding not-for-profits from the requirements
- A simplified climate-related financial disclosure regime for entities eligible to use the Simplified Disclosures Tier 2 financial reporting framework to align with that Framework, particularly for Group 3 unlisted entities and assurance requirements appropriate to the size of these entities, and
- Removing the requirement for audits of statements of no material risks and opportunities.

**2. 'Sustainability reports'**

**Terminology – 'sustainability' reports**

Our members have continuing concerns about the use of the term 'sustainability report' in the legislation because it is likely to cause significant confusion. While many entities currently produce sustainability reports they are not currently mandatory. These reports typically cover a range of issues in addition to climate change and other environmental matters and many of our members report that their investors engage closely with these 'sustainability reports'.

[5] Explanatory Memorandum para 4.10.

Using the term 'sustainability report' in the legislation is problematic because while on the face of it the term used in the draft legislation relates to climate matters, as a practical matter entities and their investors generally consider a sustainability report as covering a broader range of issues. Using a term which generally has a broader meaning in a narrow context in the legislation also potentially implies that 'sustainability reports' are mandatory. This seems contrary to the stated intention of a 'climate first approach' and the consistent references in the Explanatory Memorandum 'to climate-related financial disclosures'. Entities also approach reporting on climate issues in a variety of ways and the legislation needs to be sufficiently flexible to accommodate a range of practices. While our members acknowledge that there will be broader sustainability reporting in the future, the first order issue is climate-related financial disclosure and the terminology used should make this clear.

A preferable solution would be to adopt the term 'climate report' which clearly indicates that the report relates to climate-related financial disclosures. An alternative would be to locate these disclosures in existing reports and enable cross-referencing, noting that the current ASIC instrument only permits cross-referencing in financial reports.[6]

## 3. Ministerial discretion

Our members remain concerned at the breadth of the Ministerial discretion in the proposed section 296A(5) giving the Minister power to require a sustainability report to include statements relating to 'financial matters concerning environmental sustainability' by legislative instrument. This power is extremely broad. While our members acknowledge that there will be future standards relating to sustainability disclosure, they do not consider the fact that legislative instruments are subject to disallowance and sunsetting after 10 years to be a sufficient safeguard. Expansion of the regime should require consultation and legislative oversight. Our members consider the Minister's ability to expand the regime should require industry consultation more expressly.

The latest report by the Australian Law Reform Commission (ALRC), *Confronting Complexity: Reforming Corporations and Financial Services Legislation*, found the *Corporations Act* is no longer fit for purpose, unnecessarily complex, shrouded in obfuscation, obscure, convoluted, and like a maze – 'anything could be anywhere'. The proliferation of powers, including Ministerial instruments, was identified as a particular problem. Enshrining a broad Ministerial discretion of this type into the Corporations Act only proceeds further down the path of obfuscation and obscurity. Our members consider that any discretion should be limited to matters relating to climate-related financial disclosure, clearly linked to the Sustainable Finance Strategy.

**Governance Institute recommends** the Minister's ability to expand the regime should require industry consultation more expressly.

## 4. Liability

While our members acknowledge that the Bill has addressed some of our members' concerns around the liability provisions attached to the reporting regime they continue to have the following concerns:

- As noted in our previous submissions, there is no protection for climate disclosures extracted from the 'sustainability report' reproduced on websites, in investor presentations or disclosures such as Recommendation 7.4 of the ASX Corporate Governance Principles and Recommendations. Our members still consider this is likely to have the effect of limiting disclosure and may contribute to 'green hushing' due to concerns around liability. Absent gross negligence or wilful misconduct by an entity or its directors, identical content reproduced elsewhere should have protection.

[6] See ASIC Instrument ASIC Corporations (Directors' Report Relief) Instrument 2016/188.

- The limited immunity should apply to entities in all Groups for the first three years of their reports. Extending the protection period for forward-looking statements on climate to run for the first three years of the regime would align with the immunity period for 'protected statements'.
- Extending the dual lodgement relief provisions to include sustainability reports. Currently only financial reports that are lodged with the ASX are deemed to also have been lodged with ASIC.

**Governance Institute recommends:**

- Extending the protection for climate disclosures extracted from the climate statement reproduced elsewhere absent gross negligence or willful misconduct by an entity or its directors.
- Extending the limited immunity to entities in all Groups for the first three years of their reporting under the regime.
- Extending the dual lodgment relief provisions from financial reports only to include sustainability reports.

## 5. Continuous disclosure

Our members remain concerned that there has been no adjustment to the continuous disclosure regime because of the interaction between periodic climate-related financial disclosures and the continuous disclosure regime for ASX-listed companies. As noted in our earlier submissions, some entities currently issue periodic sustainability reports or disclosures which include information they do not consider will have a 'material effect' on the price or the value of their securities from the perspective of continuous disclosure. These entities may, at a later point, change a pathway towards achieving net zero because the pathway becomes blocked or if it fails to reach an interim target and it has disclosed the pathway or target in a periodic report. Given the difficulty of assessing the point at which a path becomes blocked and, while this information may be important to some stakeholders, it may not necessarily be market sensitive.

There are inherent uncertainties in relation to, for example, some of the data and the technologies underpinning emissions reductions which involve significant complexity and the application of judgement.

Our members continue to advocate that the most appropriate option for addressing these concerns would be to adapt the changes introduced during COVID-19 to the continuous disclosure regime. This would mean that reporting entities and their directors only attract civil liability if there is evidence that they knew or were reckless or grossly negligent with respect to reporting. An alternative option may be to adopt a modified business judgement rule where directors and/or entities are taken to have made a business judgement with sufficient care and diligence if there is evidence that they:

- made the judgement in good faith and for a proper purpose
- informed themselves about the subject matter to the extent they reasonably believed was appropriate
- rationally believed that the judgement was in the best interests of the entity, and
- rationally believed that the judgement was reasonable in the circumstances.

**Governance Institute recommends**:

- Adapting the changes introduced during COVID-19 to the continuous disclosure regime which would mean that reporting entities only attract civil liability if there is evidence that they knew or were reckless or grossly negligent with respect to reporting, or
- Alternatively, adopting a modified business judgement rule where directors and/or entities are taken to have made a business judgement with sufficient care and diligence if there is evidence that they:
    - made the judgement in good faith and for a proper purpose
    - informed themselves about the subject matter to the extent they reasonably believed was appropriate

- rationally believed that the judgement was in the best interests of the entity, and
- rationally believed that the judgement was reasonable in the circumstances.

If you have any questions in connection with this Submission, please contact me or Catherine Maxwell, General Manger, Policy and Advocacy.

Yours faithfully,

[redacted]

Megan Motto
CEO