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11 April 2024

Committee Secretary
Standing Committees on Economics
Department of the Senate
PO Box 6100
Parliament House
CANBERRA ACT 2600

Dear Sir/Madam,

Treasury Laws Amendment (Financial Market Infrastructure and Other Measures) Bill 2024 – Schedule 4 - Sustainability reporting

Nexia Australia Pty Ltd represents the six independent chartered accounting firms comprising the Nexia Australia network with 80 partners providing audit, tax and advisory services to clients from small to medium enterprises, large private companies, not-for-profit entities, subsidiaries of international companies, and listed public companies. Nexia Australia is a member of Nexia International, a top 20 global network of independent accounting and consulting firms.

We are pleased to provide the Committee with the following comments and recommendations on Schedule 4 – Sustainability Reporting of the Bill.

Item 26, subsection 296B(1) and Item 98, section 307AA – Audit requirements where no material climate risks and opportunities

The directors may determine that a company has no material climate-related risks or opportunities and identifies no matters to be reported in a Sustainability Report [Item 26, subsection 296B(1)].

Item 98, Section 307AA sets out reporting obligations by the auditor of the Sustainability Report. That audit requirement applies even if the directors of the company determine that there are no material financial risks or opportunities relating to climate.

Treasury stated in their Policy Impact Statement on Climate-related Financial Disclosures that they believe that "only 5 per cent of Group 3 companies (278 entities) have material climate risk and would be required to report".

In relation to the expected 95% of Group 3 companies reporting no material climate risks, we are concerned that the auditor will be required to undertake their own analyses, scenario assessments, and business strategy and risk assessment procedures in order to form an opinion as to whether the auditor concurs with the directors' assessment.

In our opinion, there is a significant likelihood that the burden and responsibility for identifying material climate risks and opportunities will not reside with the directors but with the auditor.

We disagree with the proposal that could impose more onerous assessment obligations on the auditor than the directors of the auditee.

<u>We recommend that the audit and auditor's reports requirements in the Bill be amended so that an auditor is not required to form an opinion on the directors' assessment where subsection 296B(1) applies</u>.

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Appointment of separate Sustainability Auditor

Treasury stated at paragraph 1.72 of the Explanatory Memorandum to the *Treasury Laws Amendment Bill 2024: Climate-Related Financial Disclosure* that "The sustainability disclosure report would be audited by the auditor of the financial report supported by technical climate and sustainability experts where appropriate".

We understand that the operation of the *Corporations Act 2001* and the Bill will require the auditor of a company's Sustainability Report and the auditor of the company's Financial Report to be the same individual.

We are concerned that small and medium-sized audit practices that perform audits of Financial Reports may not have the capacity, capability, or expertise – or for risk management purposes may choose not to - perform an audit of a Sustainability Report.

Requiring the same individual or firm to be the auditor of the Financial Report and the Sustainability Report is likely to preclude some small and medium audit practices from the financial audit market which is expected to reduce overall competition in the sector and thereby further concentrating the audit market in the Big 4 and larger audit firms.

Furthermore, the proposed legislation potentially precludes an audit firm or audit company utilising in-house expertise to enable one individual auditor to perform the audit of an entity's Financial Report and another individual auditor to perform the audit of its Sustainability Report.

<u>We recommend that the Bill be amended to permit that the auditor of the Sustainability Report need not be the same individual auditor, audit firm, or audit company that performs the audit of the Financial Report</u>.

Group 3 reporting entities (large proprietary companies)

We acknowledge the proposal to address Group 3 entities that have no material climate-related risks and opportunities [Item 26, subsection 296B(1)].

As we previously advised Treasury, we remain concerned that many large proprietary companies (Group 3 entities) are closely-held by family groups and often have no or few external stakeholders or users of their financial information. In many cases, their financial reports are prepared solely to meet their reporting obligations under the Corporations Act and, where relevant, are provided to external lenders.

Furthermore, as noted above, Treasury expects that only 5 per cent of Group 3 companies (278 entities) have material climate risk and would be required to report.

Treasury has not indicated how Scope 1, Scope 2 and Scope 3 greenhouse gas data and other mandated climate-related information reported by Group 3 entities is intended to be collated and used by either governments or others.

Extending mandatory climate reporting to large proprietary companies would impose significant time, cost, and resource burden of preparing and auditing such information without explaining to this cohort the purpose, usefulness, or expected benefits of doing so.

Based on our preliminary discussions and analysis, and depending on the extent and number of locations of an entity's operations, we understand that the costs associated with the proposals for Group 3 entities could be in the ranges of:

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Requirement	Approximate cost range
First year implementation reporting	$30,000 - $70,000
Ongoing annual reporting	$20,000 - $40,000
Limited assurance of climate reporting	$15,000 - $30,000
Reasonable assurance of climate reporting	$25,000 - $50,000

We consider that these costs would represent an excessive regulatory burden on the majority of large proprietary companies and would outweigh any perceived benefits to the Australian economy.

Furthermore, we note that paragraph 4.12 of the Explanatory Memorandum to the Bill states "the Government is taking a 'climate first, but not only' approach to mandatory disclosure requirements and these amendments will establish an enduring framework for future sustainability-related financial disclosures". If the Bill requires all proprietary companies to comply with all future sustainability standards issued by the Australian Accounting Standards Board, then the above indicative costs would multiply and would impose a further substantial regulatory impost.

For the above reasons, we disagree with the proposed mandatory climate sustainability reporting being applied to Group 3 entities.

<u>We recommend that Group 3 entities be removed entirely from climate sustainability reporting obligations under the Bill.</u>

As an alternative to excluding Group 3 entities entirely, and to more appropriately balance the regulatory cost and the potential benefits on those entities, the Committee may consider a more appropriate threshold to be:

- <u>Disclosing entities [as defined in subsection 111AC of the Act]</u> required to report under Chapter 2M of the Corporations Act 2001 and that fulfill two of the three thresholds:
  - has over 100 employees;
  - The value of consolidated gross assets at the end of the financial year of the company and any entities it controls is $25 million or more;
  - The consolidated revenue for the financial year of the company and any entities it controls is $50 million or more.

Reporting location and timing

The Bill notes that climate-related disclosures will be included in a Sustainability Report which constitutes the fourth component of the annual financial reporting obligations and will be incorporated into an entity's annual report. Whilst the principal aim of integrating climate disclosures within the annual report is to foster consistency and mitigate redundant narratives across multiple reports, our previous concerns communicated to Treasury remain.

We maintain a preference for reporting climate-related information outside the company's annual report.

We remain concerned that requiring significant additional non-financial information to be prepared and lodged as part of an entity's annual report will:

i) Impose additional burden on financial report preparers by requiring them to provide climate-related information at the same time as resources are dedicated to the preparation of financial information;

ii) Impose additional burden on auditors who are required to perform additional procedures on potentially material climate-related information included as part of the annual report at the same time as resources are dedicated to the audit of the financial information;

iii) Delay an entity's planned finalisation and lodgment of its annual report due to the requirement to provide assurance over climate-related information before the entity can finalise and lodge its annual report; and

iv) Audit firms, currently under significant industry-wide resourcing constraints, will be subject to further resourcing pressure because of the requirement to have the technical knowledge to be able to provide assurance over climate-related information even if that information has been prepared by an external subject matter expert.

Should you wish to discuss any aspects of this submission, please contact Martin Olde at [redacted].

Yours faithfully

Nexia Australia Pty Ltd

[redacted]