



Investor Group on
Climate Change

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Submission on:

Corporate Emissions Reduction Transparency Report Consultation Paper

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ABOUT IGCC

The Investor Group on Climate Change (IGCC) is a collaboration of Australian and New Zealand investors focused on the impact that climate change has on investment. IGCC represents institutional investors with total funds under management of over \$2 trillion, and others in the investment community interested in the impact of climate change. IGCC members cover over 7.5 million people in Australia and New Zealand.

Overview

The Investor Group on Climate Change (IGCC) welcomes the opportunity to make a submission on the Corporate Emissions Reduction Transparency Report (CERT) consultation paper and draft guidelines.

IGCC broadly supports the intention and implementation of CERT because widespread adoption would boost the transparency of corporate climate risk disclosure practice and could better allow investors to assess the performance of companies as part of their portfolio and climate risk management decisions. However, implementation of CERT should not be considered a substitute for a comprehensive mandatory climate disclosure regime in Australia.

IGCC recognises that wide adoption of CERT would facilitate better information for those organisations engaging in carbon and renewable energy certificate markets, including more information about the surrender of different types of credits. IGCC is supportive of the role of carbon markets as a valuable policy tool. While improved voluntary carbon market efficiency is beneficial for IGCC members, the elements of CERT most relevant to institutional investors is where it can provide greater transparency on corporate climate commitments. Accordingly, our comments below are largely contained to these specific aspects.

Given the Clean Energy Regulator's (CER) functions in relation to measuring, managing, reducing and offsetting Australia's carbon emissions, beyond implementing CERT it would be prudent for the CER to coordinate with other Australian regulating entities, including relevant financial regulators, who are developing practice and guidance on climate risk disclosure.

Background

Institutional investors are broadly supportive of government efforts to increase the standard of climate-related reporting as it is central to the long-term sustainability of Australia's financial institutions and reduces the systemic risk climate change poses to the financial system.

There are several irreversible trends beyond existing legislation that are already establishing an onus on companies and financial institutions to report on their emissions reduction commitments and other climate-related risks and opportunities. These include regulatory and legal opinion; investor engagement; and the emergence of disclosure frameworks such as the Task Force for Climate-related Financial Disclosures (TCFD) recommendations.

There has been a live policy debate in Australia about strengthening climate risk disclosure for close to a decade. Notably, in 2017 the Senate Economics References Committee produced an inquiry report recommending among other things: Australian financial regulators issue clear guidance on climate risk reporting; the Federal Government give effect to the TCFD recommendations; and corporations law be reviewed to ensure ‘holistic’ financial disclosure.¹

Through subsequent regulator activity and legal opinion, it is now well established that climate change poses material financial risks and it is within directors’ fiduciary duties to consider these risks and respond. This position has been reinforced by the statements and recommendations of Australian and international central banks and financial regulators, and the ASX Corporate Governance Council. A summary of this legal advice, regulator guidance and other relevant market signals can be found in the November 2019 IGCC policy update – *Climate Risk and Fiduciary Duties*.²

Concurrently, and because of these trends, the TCFD framework has become widely accepted as a minimum standard for companies exposed to climate change risks. The number of ASX200 companies who adopted the TCFD framework grew six-fold to 60 from 2017 to 2019.³ More companies are also undertaking and disclosing scenario analysis and setting net zero emissions commitments and targets. Importantly, the TCFD recommendations put forward specific guidance for reporting on emissions and climate targets, summarised in Table 1.

Table 1. TCFD RECOMMENDED DISCLOSURES ON METRICS AND TARGETS⁴

a) Disclose the metrics used by the organisation to assess climate-related risks and opportunities in line with its strategy and risk management process.
b) Disclose Scope 1, Scope 2, and, if appropriate, Scope 3 greenhouse gas (GHG) emissions, and the related risks.
c) Describe the targets used by the organisation to manage climate-related risks and opportunities and performance against targets.

As part of managing their exposure to climate risk and identify opportunities in the net zero emissions transition, institutional investors are also routinely engaging directly with major emitting companies about their climate change disclosure and response through a range of practices, organisations and initiatives (alongside conducting their own organisational disclosure).

For example, Climate Action 100+ is a global investor-led initiative that is engaging with 167 companies to seek greenhouse gas emissions reductions and climate disclosure, among other asks (15 focus companies are Australian-listed). The initiative now encompasses 575 global investors, responsible for over \$US54 trillion in assets under management. In September 2020, Climate Action 100+ established a ‘Net Zero Company Benchmark’ to allow investors to track the publicly committed actions of major companies against the actions required for alignment with the Paris Agreement objective of limiting average global warming to 1.5°C above pre-industrial levels. As part of this benchmark, companies are being publicly assessed on their disclosure practices through a series of sub-indicators detailed in Table 2.

Table 2. Climate Action 100+ Net Zero Company Benchmark Disclosure Indicators

Disclosure Indicator 10 TCFD Disclosure ⁵			
Sub-indicator 10.1 The company has committed to implement the recommendations of the Taskforce on Climate-related Financial Disclosures (TCFD).		Sub-indicator 10.2 The company employs climate-scenario planning to test its strategic and operational resilience.	
Metric a): The company explicitly commits to align its disclosures with the TCFD recommendations OR it is listed as a supporter on the TCFD website.	Metric b): The company explicitly sign-posts TCFD aligned disclosures in its annual reporting or publishes them in a TCFD report.	Metric a): The company has conducted a climate-related scenario analysis including quantitative elements and disclosed its results.	Metric b): The quantitative scenario analysis explicitly includes a 1.5° Celsius scenario, covers the entire company, discloses key assumptions and variables used, and reports on the key risks and opportunities identified.

The impact of this investor engagement is becoming more apparent in major companies’ reporting and response. For example, Wesfarmers recently presented divisional break downs of emissions in its regular ASX presentation, with Managing Director Rob Scott telling media: “...shareholders increasingly wanted to see actual evidence, which in the case of environmental targets means actual proof the company is cutting emissions, and the inclusion of the numbers in the results presentation does that.”⁶

In this market and engagement landscape many of the data points proposed for CERT reporting are becoming standard elements of reporting under existing disclosure frameworks (like the TCFD) that are increasingly being considered a minimum standard of good corporate practice, or ‘voluntary’, in Australia and other markets.

There is a risk that introducing parallel, similar, but different voluntary reporting requirements may create market confusion when not aligned to emerging market practice and other regulator guidance.

Investor views on climate reporting

Despite the market convergence on climate risk disclosure practices via the trends outlined above, current climate-related reporting practices from companies are falling short of investor needs and expectations in many areas.

In 2020, IGCC held workshops and surveys to gather the in-depth views of over 50 Australian and New Zealand investors from 22 organisations with more than \$1.1 trillion in collective funds under management. These workshops found that while climate risk disclosure has become an increasing feature of corporate reporting, significant improvements are needed to make it more useful for decision-making, risk assessment, portfolio management and company engagement.⁷

As a result of these sessions, it was shown that Australian investors want the next generation of company reporting through the TCFD recommendations and other credible climate disclosure frameworks to:

- Demonstrate board, director and executive skills and expertise in climate change.
- Report links between climate-related performance and executive remuneration.
- Demonstrate links between risks and opportunities identified and the company’s strategic and organisational response.

- Extend reporting of emissions metrics and targets to scope 3 emissions, where scope 3 emissions are material.⁸
- Report on both transition and physical risks, costs and implications.
- Provide auditing and assurance of results as it becomes more important.

Importantly, investors, financial regulators and the market are all looking for climate reporting which addresses financially material aspects of company performance and promotes more informed investment decision-making.

Specific comments on the CERT

Given the investor desire for more transparency and consistency in TCFD and other corporate climate disclosure, CERT as proposed does have some attractive elements. IGCC supports the following elements of the draft CERT proposal:

- A standardisation of reporting on progress towards meeting emissions reduction targets that will assist with investors' ability to assess climate change performance and in turn portfolio risks and opportunities.
- Increased verification of emissions reduction claims.
- The increased transparency CERT reporting will provide on the use of offsetting versus operational emissions reductions, as well as the breakdown of international carbon units to Australian Carbon Credit Units (ACCUs).
- The potentially large numbers of companies that could be incorporated under CERT.

General issues to consider further are:

- In order to manage climate risk in their portfolios, investors are seeking to understand *all* emissions over which the company has responsibility, including those associated with joint ventures or minority share holdings in carbon intensive assets. The data reported through CERT could present a financially incomplete picture of the full scope of a company's total emissions and may lead to contradictory or inaccurate reporting in the public domain when company targets are based on the complete scope of emissions as reported through other market channels (e.g., TCFD reporting or other regulator recommendations).
- CERT does not address scope 3 emissions. Investors expect companies to understand and act on their scope 3 emissions. A number of companies, including BHP and Rio Tinto, are now setting goals to reduce their scope 3 emissions as a result. As scope 3 emissions reduction targets and reporting become more common it should be included as an option in voluntary CERT reporting.
- CERT is positioned alongside existing government certification schemes like Climate Active. However, it relies mostly on voluntary corporate disclosure. More information about the verification processes the Clean Energy Regulator (CER) would undertake (as reference in draft guidelines 8.1) would assist in understanding how CERT would provide additional certainty for investors over and above existing company disclosure frameworks.
- The prospects of wide company adoption of CERT are uncertain given its voluntary nature and the existing market convergence on other reporting frameworks like TCFD. CERT will provide the most value if there are large numbers of participants because this will allow institutional investors to making comparative climate performance assessments across a significant proportion of the Australian market. However, the voluntary nature of CERT means it may only capture the parts of the market that are already making similar climate disclosures. Mandatory reporting through an amendment to the National Greenhouse and Energy Reporting Act (2007) could be further considered if voluntary uptake proves limited.

Specific IGCC comments related to the consultation paper questions are as follows:

- Rather than requiring opt-in every year, continued participation should be assumed with an ‘opt out’ approach for companies who have registered to participate. This would assist in retention and consistency of reporting by improving process efficiency and reducing the decision burden and potential confusion for participants related to an annual opt-in approach.
- The guidelines should clarify the role of CERT in the context of national greenhouse gas emissions accounting and reporting through the scheme, and should also include notification of data as reported elsewhere to address the completeness issues flagged above including scope coverage.
- IGCC supports the CER’s proposed approach to double counting and addressing deemed surrendered ACCUs.
- IGCC supports year-by-year per centage change reporting as opposed to a projection approach. Ultimately, projections will be established by companies using scenario analysis constructed on assumptions such as technology costs. Until mandatory guidance from regulators on best practice scenario use and transparency is established it is unlikely the pathway approach would allow for ‘apples to apples’ comparisons via CERT as companies will take different approaches to scenario assumptions that could lead to a back ending of the breadth of emissions reductions to meet specific goals or unrealistic assumptions about technology and offsetting availability and costs.
- For transparency on emissions reduction claims and the primary driver of action, CERT should identify the percentage of offsets surrendered that are attributable to compliance requirements.

Conclusion

IGCC supports the implementation of CERT because widespread uptake could help with the transparency of corporate climate disclosure practice that would better allow investors to assess the performance of companies as part of their portfolio and risk management decisions. The proposed voluntary CERT has limited coverage and should not be seen as an alternative to establishing a comprehensive and mandatory climate disclosure regime in Australia like what is evolving in other markets including New Zealand, the United Kingdom, Canada and Hong Kong.

IGCC recognises the CER’s legislated role means it is not positioned to establish a comprehensive climate risk disclosure regime. However, beyond the recommendations stated above, it would be prudent for the CER to coordinate with other Australian regulating entities, including relevant financial regulators, who are developing practice and guidance on climate risk disclosure. The role and scope of CERT should also be periodically reviewed considering inevitable developments on climate risk disclosure in Australia, including movement towards a mandatory regime, to ensure it remains relevant and does not become duplicative or misaligned with emerging practice.

¹ https://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Economics/Carbonriskdisclosure45/Report

² https://igcc.org.au/wp-content/uploads/2020/06/IGCC_Policy-Briefing_Fiduciary-Duty_FINAL_1.pdf

³ <https://acsi.org.au/wp-content/uploads/2020/10/Climate-Change-disclosure-in-ASX200.-ACSI-REPORT-October-2020.pdf>

⁴ <https://assets.bbhub.io/company/sites/60/2020/10/FINAL-2017-TCFD-Report-11052018.pdf>

⁵ <https://www.climateaction100.org/wp-content/uploads/2020/12/Net-Zero-Benchmark-Indicators-12.15.20.pdf>

⁶ <https://www.theaustralian.com.au/business/retail/emissions-gap-widens-between-business-canberra/news-story/75d4beda92410400fe5986ec6e69e6f7>

⁷ https://igcc.org.au/wp-content/uploads/2020/09/IGCCReport_Full-Disclosure_FINAL.pdf

⁸ The Science-based Targets Initiative (SBTi) requires companies to report indirect emissions and to include Scope 3 targets where indirect emissions account for over 40% of total emissions: <https://sciencebasedtargets.org/resources/legacy/2019/03/SBTi-criteria.pdf>