KPMG

Climate-related financial disclosure: Second consultation

KPMG submission

KPMG Australia, July 2023

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Executive summary

As a leading professional services firm, KPMG Australia (KPMG) is committed to meeting the requirements of all our stakeholders – not only the organisations we audit and advise but also employees, governments, regulators – and the wider community. We strive to contribute in a positive way to the debate that is shaping the Australian economy and we welcome the opportunity to provide a submission to Treasury's consultation paper *Climate-related financial disclosure: Second consultation* (the Consultation Paper).

KPMG's response to Treasury's previous consultation paper *Climate-related financial disclosure* stressed the need for Australia to align our climate reporting requirements with the global baseline envisaged by the International Sustainability Standards Board (ISSB™). To this end, we welcome several proposals that align Australia to the International Financial Reporting Standards (IFRS®) Sustainability Disclosure Standards including aligning with the principles of financial materiality, the requirement to use qualitative scenario analysis to inform disclosures from commencement and the requirement to disclose information about any climate-related targets and progress towards these targets.

KPMG welcomes the phased adoption of mandatory climate financial disclosures as it will balance capacity building while ensuring that a sufficient level of emissions in Australia is covered. In KPMG's previous submission, we recommended that large, listed entities, significant financial institutions, entities with facilities covered by the Safeguard Mechanism and entities providing critical infrastructure that is exposed to physical climate risks should be subject to the disclosure regime. We were pleased to see this approach largely adopted in the Consultation Paper.

Additionally, KPMG was pleased to see the proposal around disclosures being included in primary reports and the phased approach to assurance outlined in the assurance roadmap and timeline. Assurance plays an important role in enhancing the credibility of climate disclosures and can help identify instances of 'greenwashing'.

Lastly, we welcome the proposal to leverage the *Greenhouse and energy reporting audit framework*[1] to ensure robust independence and quality management standards as outlined in our previous submission. There will need to be an industry wide campaign developed in consultation with government to ensure enough assurers are registered with the scheme to allow business to meet the proposed assurance roadmap and timeline outlined in Table 3 of the Consultation Paper.

Thank you for the opportunity to participate in the development of this important framework and we look forward to working with the government on the legislative and governance model and interaction with other reporting obligations. If you would like to discuss the contents of this submission further, please do not hesitate to reach out.

Yours sincerely,

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[1] Legislative framework for audits (cleanenergyregulator.gov.au)

Background

About KPMG

KPMG is a global network of professional firms providing a full range of services to organisations across a wide range of industries, governments and not-for-profit sectors. We operate in 147 countries and territories and have more than 219,000 people working in member firms around the world. In Australia, KPMG has a long tradition of professionalism and integrity combined with our dynamic approach to advising clients in the digital-driven world.

KPMG's commitment to climate action

KPMG supports the scientific consensus that human activity is the primary cause of climate change and acknowledges our responsibility in limiting warming to less than 1.5°C above pre-industrial levels.

Under our Climate Action Plan to 2022, we have committed to be a net zero emissions business, an enabler of the circular economy, and to transparently managing our climate risk and ongoing contribution to the UN Sustainable Development Goals.

KPMG is certified carbon neutral through Climate Active. On our journey to net zero, we are also committed to driving continuous operational improvement and minimising our impact on the planet through energy and waste efficiency, the sourcing of 100% renewable energy, reducing non-essential business travel and working with suppliers to minimise supply chain emissions.

Climate change & sustainability

KPMG's Climate Change & Sustainability (CC&S) team works with organisations to help them manage the risks and opportunities associated with climate change and GHG emissions, and to enhance all aspects of sustainability reporting and communication. Our Better Business Reporting team works closely with CC&S to assist organisations integrate sustainability information with financial disclosures to explain how they create sustainable long-term value for their investors and other key stakeholders, as well as ensuring that internal processes and systems are aligned and provide investment-grade information. We also provide assurance services over climate and other sustainability-related disclosures, as well as financials, to enhance the credibility of reported information.

We have been providing assurance over sustainability information, including climate change risks and greenhouse gas (GHG) emissions, for over two decades. During this time, we have been actively engaged with organisations in the largely voluntary landscape of sustainability standard setting, including with the Global Reporting Institute (GRI), CDP, Climate Active, the Climate Disclosure Standards Board and the Value Reporting Foundation (VRF) ahead of their consolidation into the IFRS® Foundation, as well as the Taskforce on Climate-related Financial Disclosures (TCFD).

Section 1:
KPMG recommendations

RECOMMENDATION 1:

KPMG understands that subsidiaries meeting prescribed size thresholds and that are required to lodge financial reports under Chapter 2M would not need to each report separately where their ultimate Australian parent makes climate-related financial disclosures in its annual report relating to the consolidated entity. We support this approach and recommend that this is made clear in the legislation when drafted.

RECOMMENDATION 2:

KPMG note there is some confusion in the application of the Group 1 and 2 definitions and recommends it is made clear in the drafting of the legislation that NGER reporters are considered separately from other entities meeting prescribed size thresholds. Treasury may also need to consider how excluded NGER reporters (without Chapter 2M reporting obligations) are captured in any climate related reporting on a go forward basis given some of these may be considered heavy emitters.

RECOMMENDATION 3:

KPMG note the high level of interest in climate-related information for all listed entities. Treasury may need to consider the inclusion of all listed entities, even those not meeting prescribed size thresholds, within the reporting regime from 2027-28 onwards.

RECOMMENDATION 4:

Given the significant number of entities expected to be covered by the regime, KPMG notes the importance of ensuring the Australian standard setters and regulators are sufficiently resourced to ensure the regime meets the needs of users and that preparers/reporters and assurance providers are sufficiently supported.

RECOMMENDATION 5:

KPMG note that the reporting timeframes are ambitious however, we support the urgency in attaining an end state by 2027-28. The proposed timeframes may require a coordinated government assistance package to ensure smaller entities meet the proposed timeframes.

RECOMMENDATION 6:

KPMG recommends consideration is given to the proposed Group 3 smaller entities being required to provide reduced levels of disclosures, such as only Scope 1 and 2 emissions reporting.

RECOMMENDATION 7:

KPMG suggests there be some flexibility in extending the transition period for aligning the publication of sustainability information with financial statements given the lack of maturity of reporting on climate related information and data.

RECOMMENDATION 8:

KPMG note that it is unclear under what circumstances it would be appropriate for an entity to reference climate related information contained in a separate report and still meet their annual report climate-related reporting obligations. We suggest Treasury consider clarifying this in the legislation when drafted.

RECOMMENDATION 9:

KPMG recommends that the CER register be used as the primary accreditation vehicle for auditors selected for delegation as third-party assurance providers and for specialist input into the assurance work to ensure a level of quality control over that third party assurance or specialist input. KPMG further recommends guidance is developed as to the circumstances (or expected scenarios) specialist input is to be applied in the assurance process, in advance of the planned detailed and specific consultation on professional audit and assurance requirements.

RECOMMENDATION 10:

KPMG recommends that the government may need to review the current pre-requisites for qualification on the CER register given that some practitioners may not have the full skillset required to assure or support the assurance of climate-related disclosures outside of the Scope 1 and 2 GHG emissions.

RECOMMENDATION 11:

KPMG considers that an industry campaign will be required to ensure enough assurers are registered on the CER register to allow business to meet their assurance requirements. The campaign should have registered assurer targets to ensure there is a sufficient level of capacity in the market to conduct limited assurance of Scope 1 and 2 emissions by 2024-25.

Section 2:
KPMG insights

KPMG insights

Introduction

KPMG welcomes the Australian Government's commitment to climate-related financial disclosures - globally consistent climate reporting standards is an imperative. The alignment of Australian climate reporting standards with those issued by the ISSB, in a timely manner and with due process, will strengthen the ability of Australian entities to participate on the international stage and engage in global capital markets.

Not aligning will result in both reduced competitiveness and higher costs of capital. Australian entities may also suffer reputational damage and be seen to be laggards in the increasing demand for high-quality, consistent and transparent climate related reporting. While KPMG is strongly supportive of the proposals outlined in the Consultation Paper, we have outlined a number of matters for consideration under the following themes:

1. Reporting entities

We note the proposal that all entities meeting prescribed size thresholds that are required to lodge financial reports under Chapter 2M of the *Corporations Act 2001* would be required to make climate-related financial disclosures. We understand that the intention is that the disclosures would be aggregated up to the ultimate controlling entity in Australia only, i.e. subsidiaries that meet prescribed size thresholds and that are required to lodge financial reports under Chapter 2M would not need to each report separately where their ultimate Australian parent makes climate-related financial disclosures in its annual report relating to the consolidated entity. We support this approach and recommend that this is made clear in the legislation when drafted.

Groups 1 and 2 include all entities meeting the size thresholds as well as entities reporting under the National Greenhouse Energy Reporting (NGER) framework who currently meet the NGER publication threshold (regardless of their size) (i.e. NGER reporters are considered separately). While this was confirmed on a stakeholder teleconference with Treasury, we are aware that there is some confusion in relation to this definition. We recommend that the inclusion of all NGER reporters, regardless of size, is clear in the legislation when drafted. We note that currently NGER reporters without Chapter 2M reporting obligations are exempt from the proposals in the Consultation Paper even though they may be considered high emitters. Treasury may need to consider how these excluded NGER reporters are captured in any climate-related reporting on a go forward basis.

The Consultation Paper proposes that listed and non-listed entities meet the same size threshold requirements. As listed entities are considered Public Interest Entities and face greater investor interest, Treasury may need to consider the inclusion of all listed entities within the climate related disclosure regime from 2027-28 onwards.

Lastly, given the large numbers of entities due to be covered by the regime, it is critical the Australian Accounting Standards Board (AASB) and associated standard setters/regulators are resourced appropriately. This will ensure Australian businesses are well supported and the regime best meets the Australian context. This will also ensure that resources will not be diverted away from other critical regulatory activities and standard setting projects.

RECOMMENDATION 1:

KPMG understands that subsidiaries meeting prescribed size thresholds and that are required to lodge financial reports under Chapter 2M would not need to each report separately where their ultimate Australian parent makes climate-related financial disclosures in its annual report relating to the consolidated entity. We support this approach and recommend that this is made clear in the legislation when drafted.

RECOMMENDATION 2:

KPMG note there is some confusion in the application of the Group 1 and 2 definitions and recommends it is made clear in the drafting of the legislation that NGER reporters are considered separately from other entities meeting prescribed size thresholds. Treasury may also need to consider how excluded NGER reporters (without Chapter 2M reporting obligations) are captured in any climate related reporting on a go forward basis given some of these may be considered heavy emitters.

RECOMMENDATION 3:

KPMG note the high level of interest in climate-related information for all listed entities. Treasury may need to consider the inclusion of all listed entities, even those not meeting prescribed size thresholds, within the reporting regime from 2027-28 onwards.

RECOMMENDATION 4:

Given the significant number of entities expected to be covered by the regime, KPMG notes the importance of ensuring the Australian standard setters and regulators are sufficiently resourced to ensure the regime meets the needs of users and that preparers/reporters and assurance providers are sufficiently supported.

2. Phased implementation approach

We support the three-phased approach to reporting climate-related financial disclosure standards. We acknowledge that the scale of entities reporting, and timeframes proposed are ambitious and may create challenges in the ability of corporate Australia to meet these timeframes, however, we support the urgency in attaining an end state by 2027-28.

RECOMMENDATION 5:

KPMG note that the reporting timeframes are ambitious however, we support the urgency in attaining an end state by 2027-28. The proposed timeframes may require a coordinated government assistance package to ensure smaller entities meet the proposed timeframes.

3. Phasing of reporting requirements

KPMG supports adopting a phased implementation of some disclosures consistent with IFRS S2 *Climate-related Disclosures*. For example, Scope 3 GHG emissions disclosures only being required from the second year of adoption. KPMG acknowledges that the determination of Scope 3 GHG emissions can be challenging for certain entities, especially initially.

To this point, consideration should be given to the proposed Group 3 smaller entities, for example, potentially only being required to provide reduced levels of disclosures, such as only Scope 1 and 2 emissions reporting. This differential reporting would align with the existing tiers of Australian Accounting Standards depending on whether an entity has public accountability[2].

RECOMMENDATION 6:

KPMG recommends consideration is given to the proposed Group 3 smaller entities being required to provide reduced levels of disclosures, such as only Scope 1 and 2 emissions reporting.

4. Reporting location, frequency and timing

KPMG acknowledges the pressure that these new disclosures will place on internal teams required to report during their annual reporting period. It is noted that material climate risk must be reported in the entity's financial report and the importance of greater connectivity between sustainability-related information and financial statements, supporting capital allocation decisions is essential.

The Consultation Paper notes that climate disclosures would be required to be published in an entity's annual report. In addition, the Consultation Paper provides the option for listed entities to report 'metrics and targets' in a separate report referenced in the directors' report. It is unclear, however, under what circumstances this external referencing would be considered appropriate, and we suggest Treasury consider clarifying this in the legislation when drafted. For example, metric and target information should be included in the annual report (and not referenced out) where it is material to the users' understanding of the effect climate-related risks and opportunities and the entity's response to them have on its financial performance, position, and future prospects.

KPMG supports the reporting of climate-related information at the same time as the financial statements, however, acknowledges the practical challenges for entities to achieve this – including the availability of data, using metrics and third-party data that is not yet final, and relying on estimates. In response to this KPMG recommends alignment with the temporary and optional transition relief provided by the IFRS Sustainability Disclosure Standards to allow

[2] *AASB 1053* Application of Tiers of Australian Accounting Standards

entities to report sustainability-related financial disclosures after their financial statements for the first year of application. The IFRS Sustainability Disclosure Standards allows for aligning the publication of sustainability information with interim reporting requirements, i.e. with Q2 earnings announcements for the first year of reporting only. After the transition period, entities would need to report sustainability information at the same time as the financial statements.

RECOMMENDATION 7:

KPMG suggests there be some flexibility in extending the transition period for aligning the publication of sustainability information with financial statements given the lack of maturity of reporting on climate related information and data.

RECOMMENDATION 8:

KPMG note that it is unclear under what circumstances it would be appropriate for an entity to reference climate related information contained in a separate report and still meet their annual report climate-related reporting obligations. We suggest Treasury consider clarifying this in the legislation when drafted.

5. Assurance

Overall KPMG supports the preferred policy parameters for climate disclosure assurance outlined in the consultation paper. We support requiring limited assurance and moving to reasonable assurance over time. However, we do have some specific concerns regarding the professional requirements of assurers.

Professional requirements

We support the policy parameter of the assurance being carried out by a qualified and experienced independent provider, however, through the next phase we would like clarification of how the financial statement auditor would "conduct or lead" the assurance of the climate disclosures and the role of auditors on the Clean Energy Regulator (CER) register.

The assurance standards issued by the Auditing and Assurance Standards Board (AUASB) are premised on the engagement leader having the competence and capability to perform the engagement. Whilst auditors will have competence and capabilities in assurance skills and techniques, it would be practical to provide flexibility for the auditor (especially for smaller audit firms) to have another assurance practitioner, who does have the required competence and skills in climate, to sign the opinion over the climate disclosures. This may be a suitability qualified in-house or external person. An example may be where the other assurance practitioner is already providing additional sustainability assurance services to the client and can leverage their existing knowledge (i.e. they are providing assurance over broader sustainability reports to the same entity). We support the use of the CER register but note that the number of the practitioners currently on the register may not be sufficient to support the quantity of engagements which will be required to be performed. In addition, current CER practitioners may not have the full skillset required to assure or support the assurance of climate-related disclosures outside GHG emissions, so the pre-requisites[3] for qualification may need to be reconsidered.

Clearer guidance needs to be developed for auditors that would require an external expert given they may not have in-house expertise. For example, due process would need to be conducted on external experts by the financial auditor, much like what happens when valuations and other service providers contribute to financial audits. Quality and independence controls like what exists with the CER register would also assist in due process.

Finally, we note that the Consultation Paper proposes that "*detailed and specific consultation on professional audit and assurance requirements is proposed to be conducted at a later stage, rather than prior to the commencement of the first phase reporting and assurance requirements*". To ensure the quality of audits, we suggest that this consultation is brought forward, or the CER register be used as an interim measure.

RECOMMENDATION 9:

KPMG recommends that the CER register be used as the primary accreditation vehicle for auditors selected for delegation as third-party assurance providers and for specialist input into the assurance work to ensure a level of quality control over that third party assurance or specialist input. KPMG further recommends guidance is developed as to the circumstances (or expected scenarios) specialist input is to be applied in the assurance process, in advance of the planned detailed and specific consultation

[3] How to register as an auditor (cleanenergyregulator.gov.au)

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KPMG considers that an industry campaign will be required to ensure enough assurers are registered on the CER register to allow business to meet their assurance requirements. The campaign should have registered assurer targets to ensure there is a sufficient level of capacity in the market to conduct limited assurance of Scope 1 and 2 emissions by 2024-25.

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