LAW
COMPLIANCE

Upcoming Changes to Environmental, Social and Governance Reporting Requirements and the risks of 'greenwashing'

March 2023

Upcoming Changes to Environmental, Social and Governance Reporting Requirements and the risks of 'greenwashing'

PRIVATE SECTOR

What is environmental, social and governance reporting?

For some time now in Australia and across the world society's expectations of commercial entities have been shifting as the concept of corporate responsibility gains traction. There is increasing global recognition that it's not sustainable for private entities to operate in a vacuum with little regard to the impact they have on society, the environment, or the economy. Frameworks for environmental, social and governance (ESG) reporting, also referred to as sustainability reporting, are intended to provide greater transparency and accountability for these impacts.

Current context of ESG reporting in Australia

Currently, there is no national framework for ESG reporting in Australia. Various state and national legislation contain some ESG reporting requirements, some national examples include:

- requirements to report greenhouse gas emissions under the *National Greenhouse and Energy Reporting Act 2007* (Cth);
- the preparation of financial reports and directors' reports required under Part 2M.3 of the *Corporations Act 2001* (Cth);
- reporting on the risks of modern slavery under the *Modern Slavery Act 2018* (Cth); and
- notifying incidents to Comcare under the *Work Health and Safety Act 2011* (Cth).

Several industry bodies and regulators, such as ASIC, APRA and the ASX, have developed recommendations and/or guidance relating to the ESG reporting requirements that they oversee.

The private sector itself is driving change with many entities already making voluntary ESG disclosures that are greater than what is currently required by statute by looking to international organisations for models and guidance: Some entities are applying the Global Reporting Initiative (GRI) standards, the first universal standards for sustainability reporting,[1] and/or implementing the recommendations from the Taskforce on Climate-related Financial Disclosures (TCFD), which have been endorsed by ASIC.[2] However, the lack of a holistic approach to ESG reporting in Australia has resulted in inconsistent and incomparable ESG reporting by private entities – a situation that is not unique to Australia.

Global standards for sustainability-related and climate-related disclosure

The International Sustainability Standards Board (ISSB) which forms part of the International Financial Reporting Standards Foundation (IFRS) is seeking to further the work of the TCFD by developing two global standards that are designed to ensure entities disclose 'consistent, complete, comparable and verifiable' sustainability-related and climate-related information to assist users of general purpose financial information, such as investors and lenders, to accurately assess an entity's enterprise value.[3] These new standards are intended to compliment the IFRS global accounting standards and have come about in direct response to requests from World Leaders and international organisations. The ISSB and GRI are working together to ensure each organisations' sustainability

---

[1] GRI, Our mission and history.

[2] ASIC, Climate risk disclosure by Australia's listed companies, September 2018, 12. See also, AASB Exposure Draft Request for Comment on ISSB [Draft] IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information and [Draft] IFRS S2 Climate-related Disclosures ED 321, April 2022, v-vi.

[3] ISSB, Exposure Draft IFRS Sustainability Disclosure Standard IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information (Draft IFRS S1), March 2022, 5; ISSB, Exposure Draft IFRS S2 Climate-related Disclosures (Draft IFRS S2), March 2022, 5.

standards align and will together form 'a comprehensive corporate reporting regime'.[4] The applicability of the ISSB global disclosure standards in Australia (as in other countries) will rely on the Australian government adopting or codifying these or similar national standards.

The ISSB published the exposure drafts for the standards in March 2022 with an invitation to interested parties to comment during a period of consultation which ended in July 2022. Currently in deliberation over the drafts with the comments they received, the ISSB is expected to publish these new standards as early as the second quarter of 2023.[5]

Draft IFRS S1: General Requirements for Disclosure of Sustainability-related Financial Information

The objective of ISSB's draft standard IFRS S1 is to ensure entities disclose 'material information' about 'sustainability-related risks and opportunities' to enable users of general purpose financial information to accurately assess the enterprise value of an entity. Entities will be required to provide 'a complete, neutral and accurate depiction of its sustainability-related financial information' within their general purpose financial reports.[6]

Importantly the ISSB have not defined 'sustainability-related risks and opportunities' and as such IFRS S1 is expected to encompass reporting on sustainability risks and opportunities across the broad categories of environmental, social and governance.[7] The ISSB has stated that:

> Sustainability-related financial information is broader than information reported in the financial statements and could include information about:
>
> - an entity's governance of sustainability-related risks and opportunities, and its strategy for addressing them;
> - decisions made by the entity that could result in future inflows and outflows that have not yet met the criteria for recognition in the related financial statements;
> - the entity's reputation, performance and prospects as a consequence of the actions it has undertaken, such as its relationships with people, the planet and the economy, and its impacts and dependencies on them; and
> - the entity's development of knowledge-based assets.[8]

Entities will be required to make sustainability-related financial disclosures in relation to matters of governance, strategy, risk management and metrics and targets. In relation to the information disclosed there will be obligations for entities to provide a 'fair presentation' of the entity's position and this may include reporting on the combined effects of related risks and opportunities and equally by not drawing connections between information or events that are not similar in nature.[9]

If you wish to read the Draft IFRS S1 standards in full, please click here.

Draft IFRS S2: Climate-related Disclosures

The objective of the draft standard IFRS S2 is to require entities to disclose information about their exposure to 'climate-related risks and opportunities' to enable users of general purpose financial information to:

- accurately assess an entity's enterprise value;
- understand how the entity manages resources in response to climate-related risks and opportunities; and
- evaluate the entity's adaptability to climate-related risks and opportunities.[10]

[4] IFRS, ISSB and GRI provide update on ongoing collaboration, 23 June 2022.
[5] IFRS, Foundation Work Plan.
[6] Draft IFRS S1, 22.
[7] This position has been taken by various commentators including PWC, Allens Linklaters and K&L Gates.
[8] Draft IFRS S1, 22-23
[9] Draft IFRS S1, 31-32.
[10] Draft IFRS S2, 32.

Similar to the Draft IFRS S1 entities will be required to make disclosures in relation to matters of governance, strategy, risk management and metrics and targets.

Entities will be expected to identify and describe climate-related risks that affect their business strategy and cash flow over the 'short, medium or long term'.[11] The ISSB has noted that 'climate-related risks' include 'physical risks' from extreme weather events or changing weather patterns due to climate change and 'transition risks' related to the transition to a lower-carbon economy, these categories reflect the TCFD findings and recommendations.[12] More specifically entities will be required to report data about greenhouse gas emissions and internal carbon prices and 'how climate-related considerations are factored into executive remuneration'.[13] It is likely there will be cross-industry disclosure requirements as well as industry specific disclosure requirements. Further, entities will be expected to use 'climate-related scenario analysis' to assess their 'climate resilience'.[14]

If you wish to read the Draft IFRS S2 standards in full please click here.

Australian sustainability-related and climate-related disclosure standards

In late 2021 a joint position statement from the Australian Accounting Standards Board (AASB), the Financial Reporting Council (FRC) and the Auditing and Assurance Standards Board (AUASB) revealed the government's intentions to develop a regime for extended reporting of financial and non-financial information which would include sustainability reporting.[15]

Last year, the AASB published the ISSB's Draft IFRS S1 and Draft IFRS S2 with a request for comment from interested parties by mid-July 2022. The responses received informed the AASB's own response to the ISSB's request for comments on their exposure drafts. The AASB also noted that the responses it received would inform the future development of national sustainability-related and climate-related reporting standards.

Preliminary decisions by the AASB

When the AASB published the Draft IFRS S1 and Draft IFRS S2 for comment, they set out several preliminary decisions in respect of the development of Australian standards which may be revisited. These preliminary decisions were:

- the sustainability-related reporting standard would be separate and 'operate alongside' the Australian Accounting Standards;
- to use the work of the ISSB as a foundation;
- to focus on for-profit entities (FP entities) before not-for-profit and public sector entities (together, NFP entities); and
- to apply its Due Process Framework for Setting Standards.[16]

The AASB has noted that national standards may go further than the global standards from the ISSB which are intended to be minimum requirements, however consultation has already revealed the importance of any national standards aligning with the ISSB's globally recognised standards.[17] The AASB's work program indicates that it will consider the draft sustainability reporting standard-setting framework and the draft project plan for climate-related financial disclosure (which will include discussion on alignment with the ISSB standards) in March 2023.[18] Given the preliminary decision of the AASB to utilise the work of the ISSB as a foundation the timeframe for the AASB to develop

---

[11] Ibid 34.

[12] Ibid 46-47.

[13] Ibid 41-42.

[14] Ibid 37.

[15] FRC/AASB/AUASB, Position Statement Extended External Reporting and Assurance, November 2021.

[16] AASB Exposure Draft Request for Comment on ISSB [Draft] IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information and [Draft] IFRS S2 Climate-related Disclosures ED 321, April 2022 (ED 321), iii-v.

[17] Ibid iv.

[18] AASB Workplan, 4.

national standards seems likely to follow the publication of ISSB's standards and form part of the general international uptake.

Legislative framework for Australian standards

In mid-December 2022 the period of consultation ended for an exposure draft bill published by the Treasury.[19] The draft bill would make legislative changes to the *Australian Securities and Investment Commission Act 2001* (Cth) to empower the AASB to make national sustainability standards with monitoring and oversight, both national and international, from the FRC. It appears the Australian government is preparing for the creation and implementation of national sustainability standards.

Timeline for compliance with new standards

The timeline for compliance with the ISSB's global standards is not clear as they are yet to be published. One of the questions that formed part of the ISSB's consultation was when the effective date for compliance with the disclosure standards should be. The AASB and the AUASB's joint submission to the ISSB proposed an effective date for compliance with global standards to be at least two to three years after the date of issue with early compliance permitted for entities that are in a position to do so, which aligned with the majority of global respondents who made submissions to the ISSB.[20] That said, ISSB staff have recommended an effective date of on or after 1 January 2024 citing an urgent need for sustainability-related and climate-related disclosure standards but acknowledging that this date is ambitious and indicating that some transitional relief, particularly in respect to the timing of initial reporting, will likely be provided.[21]

A warning against 'greenwashing'

Investors and consumers are increasingly choosing products and services based on their environmental impact and sustainability which is one of the drivers for businesses to make ESG or sustainability-related disclosures. However, with the current lack of standards for how these are to be made it remains difficult for investors and consumers to verify claims made by entities in relation to their environmental and sustainability practices. Greenwashing occurs when an entity misrepresents the extent to which their products or investment strategies are 'environmentally friendly, sustainable or ethical'.[22] Australian regulators are now tackling greenwashing as it is becoming a growing problem. Having issued over $140,000 worth of infringements in 2022 and 2023 for alleged greenwashing,[23] ASIC have stated that 'misleading conduct in relation to sustainable finance' is an enforcement priority for 2023.[24] Against that backdrop, in February 2023 ASIC commenced their first court proceedings against Mercer Superannuation (Australia) Limited (Mercer) for severe allegations of greenwashing.[25] When advertising or providing financial products or services entities must comply with the prohibitions against false and misleading statements and dishonest, misleading and deceptive conduct found in the *Corporations Act 2001* (Cth) and the *Australian Securities and Investments Commission Act 2001* (Cth) which are regulated and enforced by ASIC.[26] Mercer claimed on its website that their 'sustainable' investment options excluded investments in 'carbon intensive fossil fuels', alcohol production and gambling.[27] ASIC alleges these statements were misleading as the relevant investment options invested in various companies involved in these industries such as mining giant

[19] Treasury, Empowering the AASB to deliver sustainability standards.

[20] AASB and AUASB joint submission on ISSB Exposure Drafts on [Draft] IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information and [Draft] IFRS S2 Climate-related Disclosures, 28 July 2022, 4; ISSB Staff Paper General Sustainability-related Disclosures, September 2022, 25.

[21] ISSB Staff Paper General Sustainability-related Disclosures and Climate-related Disclosures, February 2023.

[22] ASIC, INFO271 How to avoid greenwashing when offering or promoting sustainability-related products, June 2022 (INFO271).

[23] ASIC, 23-043MR ASIC launches first Court proceedings alleging greenwashing, 28 February 2023 (23-043MR).

[24] ASIC, Enforcement priorities.

[25] ASIC, 23-043MR.

[26] ASIC, INFO271.

[27] ASIC, 23-043MR.

BHP Group Ltd, alcohol producer Heineken Holding N.V. and gambling and entertainment complex owner Crown Resorts Ltd.[28]

ASIC are not the only regulator actively pursuing greenwashing, on 3 March 2022 the Australian Competition & Consumer Commission (ACCC) announced their compliance and enforcement priorities for 2022/23 which included deceptive environmental and sustainability claims made by businesses.[29] The ACCC are empowered to enforce the *Competition and Consumer Act 2010* (Cth), which includes the Australian Consumer Law, and have stated they have several investigations underway following an internet sweep in late 2022 which revealed 57 percent of 247 business whose websites they reviewed made 'concerning claims about their environmental credentials'.[30]

The ACCC published their findings from the internet sweep revealing several concerns, being:

- the use of vague and unqualified claims, such as 'green', 'eco-friendly' or 'sustainable', which are not verifiable;
- a lack of substantiating information, meaning a failure to provide sufficient evidence to support claims;
- the incorrect use of absolute terms, such as '100% plastic free', '100% recyclable' or 'zero emissions';
- the use of unhelpful comparisons, such as saying a product uses 'fewer resources' or 'less plastic', or by drawing comparisons with a generalisation such as 'conventional alternatives';
- an exaggeration of the benefits or an omission of relevant information, such as claiming a product is recyclable when there is no system to recycle it or promoting renewable energy projects while omitting the fact that most of the business' projects are fossil-fuel based;
- the use of aspirational claims without a clear or practical plan to achieve them;
- improper use of third-party certifications such as failing to describe the nature of the certification scheme; and
- the use of logos and symbols which appear to be trustmarks but are not actually associated with certification schemes.[31]

Entities should be careful to avoid engaging in greenwashing practices and ensure any ESG or sustainability-related disclosures they make provide an accurate and fair representation. Until international and national standards exist, as noted above ASIC are encouraging voluntary disclosures under the framework produced by the TCFD[32] and have released an information sheet to provide guidance on how to avoid greenwashing.

If you wish to read the information sheet from ASIC, please click here, or if you wish to read the findings on greenwashing published by the ACCC please click here.

[28] Ibid.

[29] ACCC, Compliance and enforcement priorities for 2022/23, 3 March 2022.

[30] ACCC, ACCC 'greenwashing' internet sweep unearths widespread concerning claims, 2 March 2023.

[31] ACCC, Greenwashing by businesses in Australia, March 2023.

[32] ASIC, INFO271.

PUBLIC AND NOT-FOR-PROFIT SECTORS

Will public entities and not-for-profit entities be required to undertake ESG reporting?

The AASB’s preliminary decision to focus on FP entities was based on their understanding from consultation already undertaken that:

> …sustainability-related reporting for NFP entities is significantly different to sustainability-related reporting for FP entities and that further outreach and research was needed to determine the relevance of such reporting for NFP entities.[33]

Further, the scope of the ISSB’s Draft IFRS S1 acknowledges that the terminology used was intended to suit the private sector and may require adaptation if it were to be applied to the public and not-for profit sectors and the Draft IFRS S2 is to be applied in accordance with Draft IFRS S1.[34]

Accordingly, it seems unlikely that any ESG standards which are being developed or soon to be developed would be applicable to NFP entities in the short term. In the long term it seems likely that ESG reporting requirements for public entities will expand and this may be via adaptation of any relevant standards.

For now, the relevant ESG reporting requirements for NFP entities are that which are included in their current reporting obligations.

Contact

For further information on the contents of this report please contact:

Natalie Franks
CEO and Legal Counsel
Direct: 1300 862 667
Email: natalie.franks@lawcompliance.com.au

Jillian Britton
Compliance Solicitor
Direct: 1300 862 667
Email: jillian.britton@lawcompliance.com.au

LAW COMPLIANCE

[33] ED321, v.

[34] Draft IFRS S1, 23 and see Draft IFRS S2, 32, 33, 2 and 43.

LAW COMPLIANCE

Law Compliance provides legislative compliance services to organisations throughout Australia. We make legal compliance easy.

48-48 Boundary Street
South Melbourne Vic 3205
Phone: 1300 862 667
info@lawcompliance.com.au
www.lawcompliance.com.au