THE STATE OF ESG REPORTING IN AUSTRALIA

Date: 15 December 2022

By: Clive Cachia, Adam Levine

Whilst there has been a marked improvement in the aspirations of Australia's leading companies with respect to environmental, social and governance (ESG) reporting over the last few years, we expect the requirements for more comprehensive and standardised reporting will only continue to grow.

There are a number of "push" and "pull" factors which will spur this trend.

PUSH FACTORS – THE RISE OF REGULATION

There are number of current Australian mandatory reporting requirements in ESG such as:

- For environmental – under the *National Greenhouse and Energy Reporting Act 2007*, under conditions to Commonwealth and State environmental and planning approvals and under the recently introduced *Climate Change Act 2022*.
- For social – workers' rights under Commonwealth and State industrial relations and work health and safety legislation; various discrimination and equal opportunity laws and modern slavery reporting under the *Modern Slavery Act 2018* (Cth) and the NSW equivalent for state-owned corporations.
- For governance – under the ASX Listing Rules, pursuant to the ASX Corporate Governance Principles and Recommendations, and disclosure obligations of directors and financial reporting obligations under legislation and common law.

There are also various *voluntary* ESG disclosures commonly made by Australian companies such as:

- Particular social risk disclosures – e.g., the Global Reporting Initiative, the UN Guiding Principles on Human Rights and the Organisation for Economic Co-operation and Development Guidelines for Multinational Enterprises.
- Particular climate risk disclosures – e.g., in accordance with the Sustainability Accounting Standards Board and the Taskforce on Climate-Related Financial Disclosures.
- Industry based reporting frameworks – e.g., Principles for Responsible Investment requiring asset owners and investment managers to meet minimum annual reporting requirements.
- Reconciliation Actions Plans.
- Net zero commitments and aspirational targets.

However, these requirements have been developed on a sporadic and fragmented basis. This has led to companies developing ESG compliance policies and practices which differ markedly and focus on short-term effects rather than on long-term risk and opportunities. This fragmentation enables "greenwashing" in which corporates can disclose compliance with certain standards to give a misleading impression of compliance with other, more rigourous, standards. Interested stakeholders (investors, employees, customers, suppliers and local communities) are demanding increased oversight and transparency on the effects of ESG matters on companies' financials and regulators are being compelled to act. These demands have belatedly been supported by current proposed comprehensive and standardised regulatory developments.

Such regulatory developments include:

- The International Sustainability Standards Board is preparing a definitive suite of global disclosure standards by merging various national voluntary ESG frameworks including those referred to above.

  Such globalised standards are expected to be formalised by the end of 2022 and are proposed to require all entities (regardless of industry and geographic location) to disclose significant ESG-related risks and opportunity that can reasonably be expected to affect that entity's enterprise value.

- The European Financial Reporting Advisory Group and the Securities and Exchange Commission in the United States have also proposed new sustainability and climate reporting principles and standards.

- Concurrent bespoke sector developments such as:

  - The Australian Sustainable Finance Initiative (to align Australia's financial systems with the Paris Agreement's commitments on climate change, the UN Development Goals and conventions on human rights).

  - The Responsible Investment Association of Australasia providing certification of responsible and ethical investment products and services.

  - Fair Farms Initiative providing horticultural and agricultural organisations with information and training to promote ethical supply chains.

PULL FACTORS – COMPARATIVE COMPETITION

Operating alongside regulatory compliance, forward-thinking companies are seeing the comparative advantages in disclosing not only the impact they have on the economy, environment and people, but also the effect such ESG matters have on their enterprise value and various financial metrics. This 360 degree view of ESG serves to better demonstrate how an organisation is responding to these pressures. The focus on financial data necessarily overcomes the tendency to report motherhood-statements and requires a level of detail promoting authenticity in disclosures and accountability against targets.

The investment community has clearly articulated the need for such accountability when deciding where to invest.

With close to AU$1 trillion in assets under management, Australia's institutional investors (particularly superannuation funds) have the financial firepower to compel rigorous responses to ESG issues by investee companies. They do this by deciding whether to invest, making investment conditional on ESG-related remediation and reporting, active stewardship of an investee's operations with respect to ESG matters and making specific impact investments. With competition for investment only increasing, companies will need to demonstrate they have the systems in place to minimise risks affecting investors' capital.

NEXT STEPS

These push and pull factors are driving a virtuous circle of ESG plans and reporting both locally and internationally and particularly with respect to any remediating any actual or perceived shortfall.

The upcoming round of international standardisation of reporting standards offers a convenient opportunity for those corporates whose reporting may be lacking in detail, consistency or ambition to regain momentum in the drive for competitive advantage.

KEY CONTACTS

CLIVE CACHIA
PARTNER

SYDNEY
+61.2.9513.2515
CLIVE.CACHIA@KLGATES.COM

ADAM LEVINE
PARTNER

PERTH
+61.8.9216.0965
ADAM.LEVINE@KLGATES.COM

