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Your ref: Consultation Paper 380 regarding Sustainability Reporting
Our ref: Comments from GHD Group Limited

19 December 2024

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Comments to Consultation Paper 380 regarding Sustainability Reporting

Thank you for the opportunity to provide comments to Consultation Paper 380 regarding proposed regulatory guidance for the new statutory "sustainability report" per the Corporations Act.

As a provider of technical and commercial sustainability advice, as well sustainability assurance services in Australia, GHD Group Limited (GHD) follows the new sustainability and climate-disclosure requirements closely. GHD will also be preparing the statutory sustainability report (aka mandatory climate-related financial disclosures) as a Group 1 entity.

Summary of our letter and comments

Our comments are provided as a firm offering professional services to companies preparing the statutory sustainability report. Here is the structure of our letter:

- **Section 1 – Our relevant credentials, including as climate assurance providers**

  Before providing our comments, we provide a short summary of our credentials or relevance to the comments provided.

- **Section 2 – Item F2: ASIC to clarify ability to choose RCA**

  The Corporations Act subsection 324AA(1) allows companies to appoint more than one Registered Company Auditor (RCA) - and the sustainability audit is defined separately to the financial audit. Therefore, it appears possible for companies to appoint one RCA for the financial audit and another RCA for the sustainability audit – which would also benefit the climate disclosure framework, making it more internationally aligned and be in the public interest.

  We encourage ASIC to clarify that companies can appoint a different RCA to perform the sustainability audit.

- **Section 3 – Item F2: ASIC to clarify how it will enforce RCA sustainability competence**

  Whilst there are no legislated sustainability competence requirements for RCAs leading the statutory sustainability audit, we note that the assurance standard to be applied requires RCAs to have substantial relevant competence in the matters to be audited – in particular given the complexity and judgements required in preparing climate statements. This is important to ensure credible sustainability audits of sufficiently high quality. Whilst the Auditing and Assurance Standards Board (AUASB) may make further pronouncements relating to this, the AUASB has no enforcement powers.

We encourage ASIC to clarify how it will enforce that RCAs appropriately determines whether they have appropriate and sufficient climate competence to lead and perform the statutory sustainability audits.

– **Section 4 – Item C5: ASIC to provide less prescriptive labelling guidance to avoid confusion**

  We agree with the intention of the proposal but note the prescriptive nature of it may lead to increased confusion among report users. The statutory sustainability report only mandates reporting on the financially related aspects of one sustainability topic, namely climate-related financial disclosures. Reporting of other sustainability disclosures remain voluntary. True sustainability reporting, which has been around for decades and is widely applied in Australia and Worldwide, is broader and ideally reports on all material sustainability topics.

  We encourage ASIC to provide labelling guidance that is less prescriptive to avoid confusing report users, including international report users of true sustainability reporting that companies may prepare.

1. Our relevant credentials, including as climate assurance providers

GHD is an employee-owned global professional services company with over 11,000 employees in 160 offices on five continents – and with approximately 5,000 of our employees in Australia in 40 locations across the nation. Our professional services are primarily within engineering and environmental services focussing on making water, energy, and communities sustainable for generations to come.

We provide technical climate related services and advice

GHD provides a significant amount of climate related technical and design advice to clients, as well as related environmental services, such as:

– **Decarbonisation services –** we provide a suite of services relating to decarbonising our clients' operations or projects. These include providing technical feasibility studies and design services for decarbonisation solutions, including in hard to abate processes, as well as environmental impact assessments and technical design services for implementing low carbon energy related solutions.

– **Water resilience** – we provide a suite of services relating to making the water infrastructure we all depend on more resilient to the potential impacts of climate change. This includes considering the potential climate risks associated with water infrastructure to identify appropriate mitigating actions – which may include design adaptations for new water infrastructure we design.

– **Sustainability advice** – we provide sustainability related advice to clients relating to (among other) decarbonisation option identification and implementation, greenhouse gas reporting, climate change risks assessments as well as advice relating to preparing for the new statutory sustainability report.

We are a leading climate assurance practice in Australia

We are currently one of Australia's leading assurance providers in respect of climate aspects, with eight (8) Category 2 Registered Greenhouse and Energy Auditors (RGEA Cat 2s) practicing as lead auditors for National Greenhouse and Energy Reporting (NGER), projects under the Australian Carbon Credit Unit (ACCU) scheme and under the Safeguard Mechanism.

Our RGEA Cat 2s annually lead up to 80-100 or more assurance engagements. GHD is also on the Clean Energy Regulator's (CER) panel for auditors leading assurance engagements under its regulatory compliance programme – with the CER over the last five years having commissioning more such engagements to GHD than from any other firm.

We deliver climate assurance applying AUASB's standards

To deliver these assurance engagements GHD and its lead auditors (RGEA Cat 2s) must apply assurance approaches based on standards issued by the AUASB – including ASAE 3000 and ASAE 3410[1], as well as applying AUASB's quality management standards such as ASQM1[2] and meeting relevant professional, ethical and independence requirements set out in APES 110[3] – equivalent to the requirements of RCAs. It is mandated in a legislative requirement for performing audits and assurance engagements under the CER's schemes – and is subject to regulatory oversight and inspection by the CER, with GHD's RGEA Cat 2 auditors being subject to regulatory inspections by the CER's audit inspectors.

2. Item F2: ASIC to clarify ability to choose RCA

Our observation is that there is an assumption in the market that the RCA the company uses for the financial audit <u>must</u> perform the new statutory sustainability audit – whilst not being corporate law professionals, we note this assumption does not seem to be supported by the actual wording of the Corporations Act:

– Subsection 324AA(1) explicitly allows companies (and registered schemes) to appoint more than one RCA.
– The sustainability audit is defined as a separate audit to the financial audit:
  - Separate audit requirements (s301 and 301A)
  - Separate audit scopes (s307 and s307AA)
  - Separate audit reports (s308 and s309A).
– The statutory sustainability report is clearly defined as separate to the statutory financial report (even as there obviously are linkages between the two) – implying that the two separately defined audits are also auditing two different sets of disclosures.
– There is no explicit requirement stipulated in the Act that the RCA for the sustainability audit <u>must</u> be the same as the financial audit RCA.

Accordingly – whilst it obviously is allowed to appoint the same RCA for both audits, it seems allowable for companies to choose to appoint one RCA to perform the statutory financial audit and another RCA to perform the separate statutory sustainability audit.

Given ASIC's regulatory oversight role, including in respect of registering appointed RCAs, we believe ASIC should clarify that the Act allows for companies to appoint a different RCA than the financial audit RCA for its sustainability audit. We note that this is also in the public interest, for the following reasons:

– **Any requirement for the same RCA should be explicitly required in the Act** – it has been suggested that Treasury intended the Bill to require it be the same RCA – but that would have been easily achieved by drafting a bill that explicitly requires it. When it is not explicitly required, then an Act of Parliament should be interpreted as passed – i.e., in this case allowing different RCAs to be appointed for the two separate audits – noting further, allowing a choice is better aligned with other intentions stated by Treasury for the framework (refer below).
– **Avoiding an entrenched market for sustainability audit services** – as intended by Treasury. Without a choice, the financial audit RCA will automatically assume the sustainability audit role without having to compete for it based on capability, capacity and price – i.e., no effective market for the new sustainability audit role, and with limited incentives (if any) for the RCA to delegate part of the scope to other providers – which Treasury stated as important to address the capability and capacity gap.

[1] That is the Australian Standard on Assurance Engagements 3000 *Assurance Engagements other than Audits of or Reviews of Historical Financial Information* (ASAE 3000), and Australian Standard on Assurance Engagements 3410 *Greenhouse Gas Statements* (ASAE 3410)
[2] That is AUASB's Australian Standard for Quality Management 1 (ASQM1).
[3] That is the Code of Ethics for Professional Accountants (APES 110) by the Accounting Professional & Ethical Standards Board (APESB) referred to in AUASB's standards.

- **Ensuring the market benefits from synergies between the two audits** – acknowledging synergies between the two audits, most companies, even if given the choice, probably will choose the same RCA for both audits. However, without effective competition for the sustainability audit role, the financial audit RCA may feel comfortable to "bank" the synergies rather than it benefitting the market – they may even over-quote as companies will find it difficult to challenge their costings when they cannot invite proposals from other RCAs.
- **Internationally aligned assurance framework** – Treasury intended the Australian climate disclosure requirements to be internationally aligned – which would suggest there should be a choice of RCA, as similar audit requirements being implemented elsewhere allows for appointing a different auditor to perform mandatory sustainability related assurance– e.g., in the European Union (EU), the United States (US) and New Zealand.
- **Potential adverse impact on financial audit market** – to accept the statutory sustainability audit, the RCA must have sufficient and substantial relevant sustainability competence (refer section 3 below). By requiring the financial audit RCA to take on the sustainability audit, the financial audit RCA must invest in and focus on acquiring this competence – and may fall short for some clients. This would imply that otherwise competent financial audit RCAs may have to reject performing financial audits, perhaps even for existing clients, because they cannot lead and perform the sustainability audit – further entrenching the financial audit market among few providers.
- **Addressing the sustainability audit capability and capacity gap** – Treasury acknowledged that there is a significant capability and capacity gap for the new sustainability audit requirement – which is one of the reasons Treasury considered that delegation to other providers, such as RGEAs, was important. However, Treasury may have underestimated this gap significantly, as its impact assessment significantly under-estimated the likely costs (and therefore scale) of the new statutory sustainability audit – which may be 5 to 10 times as expensive than Treasury estimated, with sustainability audit fees of up to 50-100% of financial audit fees possible. This may imply that thousands of additional audit professionals will be required to deliver the financial and sustainability audits simultaneously – making it significantly harder to address the challenging capability and capacity gap if there is no choice of which RCA can perform the sustainability audit.

3. Item F2: ASIC to clarify how it will enforce RCA sustainability competence

To lead financial audits, RCAs must have appropriate, sufficient and proven financial reporting competence to ensure credible financial audits of appropriate high quality. The competence requirements are defined in legislation with requirements to prove such competence in order to be able to qualify to become and remain a RCA – and with it being monitored and enforced by ASIC.

Relevant sustainability reporting competence is also important for credible statutory sustainability audits of appropriate high quality. However, no relevant legislative or registration requirements have currently been defined.

Irrespective of this, sufficient and at times substantial relevant subject matter competence is required. The AUASB is working on issuing an Australian "ASSA 5000" standard aligned with the new *International Standard for Sustainability Assurance 5000 General Requirements for Sustainability Assurance Engagements* (ISSA 5000) – and intends to make it mandatory to apply ASSA 5000 for the statutory sustainability audit.

Under ISSA 5000 the determination of competence sufficiency is ultimately a judgement at the engagement leader's discretion, subject to the RCA firm's quality management procedures. However, it includes the following observations that the lead RCA needs to consider when making the judgement:

- **Lead RCA must personally be appropriately competent** – ISSA 5000 prohibits the engagement leader (i.e., the lead RCA) to accept the engagement unless personally appropriately competent in the matter to be audited (refer paragraphs A81 – A83 of ISSA 5000), as well as supported by an appropriately competent engagement team (refer paragraph A98 of ISSA 5000).

- **Using the work of an expert cannot bridge insufficient lead RCA competence** – it has been suggested that the RCA can rely on experts where they have insufficient subject matter competence. Whilst this may be appropriate, it cannot bridge insufficient competence – when using experts, paragraph A82 of ISSA 5000 clarifies that the lead RCA must have sufficient sustainability competence to be able to ask appropriate questions of the expert, be able to evaluate the audit implications of the answers, be able to evaluate the expert's work, and be able to integrate it into the audit as a whole – given the technical complexity of some climate disclosures this may require substantial sustainability competence by the lead RCA to enable the use of experts.
- **Lead RCA competence increases with complexity and judgements required** – paragraph A83 of ISSA 5000 clarifies that sufficient sustainability competence *depends on the engagement circumstances and differs from engagement to engagement*. It depends on factors such as the complexity and nature of the sustainability matters to be audited, the extent and complexity of judgements required in evaluating the reporting criteria and the sustainability matter, the extent to which the sustainability matters are capable of precise measurement or need significant knowledge and judgement, and the previous experience in relation to the audited matters.

Climate statements, as the most significant part of the statutory sustainability report, must be prepared per Australian Accounting Standards Board (AASB)'s new S2 standard *Climate-related disclosures* (AASB S2). Preparing climate statements per AASB S2 include complex disclosures requiring substantial judgements, and with uncertain measurements – all suggesting that substantially competent engagement leaders (i.e., lead RCAs) and engagement teams are required to be able to accept and perform the statutory sustainability audit in accordance with ASSA 5000.

Whilst the AUASB may make further pronouncements in respect of how these competence requirements are to be considered by RCAs, the AUASB does not have any enforcement powers. Given how important this is for the quality and credibility of the statutory sustainability audits, we encourage ASIC to provide regulatory guidance on how it intends to monitor and enforce these important competence requirements. Without a defined competency framework, as is the case for financial audit competence, this may be challenging for RCAs and ASIC – until a relevant competency framework is defined, we would encourage ASIC to clarify in regulatory guidance:

- the expectation that RCAs document the reasonable basis for making the determination of whether they and their engagement team meet the requirements for sufficient climate related competence to accept and perform the statutory sustainability audit, and
- an intention to monitor and enforce this documentation requirement, including the possibility of ASIC inspecting these records to evaluate whether the RCA has appropriately considered and documented sufficient competence to lead and perform the statutory sustainability audit.

4. Item C5: ASIC to provide less prescriptive labelling guidance to avoid confusion

We note and agree with ASIC's intention of avoiding confusion in respect of the statutory sustainability report with other sustainability reporting. However, the prescriptive nature of the proposal may lead to increased confusion – noting:

- ASIC's proposal appears to restrict the use of the label "sustainability report" for any other reporting than the statutory sustainability report – including sustainability reporting that may appropriately report on all material sustainability topics. This discourages the use of an appropriate label for such reporting and may discourage companies from preparing broader sustainability reporting altogether.
- Sustainability reporting has been around for decades – with the Global Reporting Initiative (GRI)'s Sustainability Reporting Standards (GRI Standards) remaining the global leading framework for it:

- A recent survey by KPMG International found that three-quarters of the World's largest 250 companies are using GRI Standards for their sustainability reporting[4].
- A related survey by KPMG Australia found that 72% of ASX100 companies preparing sustainability reporting use the GRI Standards[5].

Accordingly, the statutory "sustainability report" is far from being the definitive form of sustainability reporting – other than for the narrower purpose of the statutory report defined by the Act.

– ASIC states that it does *not intend to inhibit the provision of voluntary sustainability information nor disrupt existing practices in the market unnecessarily*. We agree with this intention – however, the prescriptive nature of the proposal does not align with the intent. Voluntary sustainability reporting is provided for many different reasons, and to many different audiences – for some Australian companies this includes international report users (including investors and analysts), who may consider it less that satisfactory to find a sustainability report prepared by Australian companies not covering relevant material sustainability topics.

– Some Australian companies may also be required by other jurisdictions to prepare sustainability reports according to other reporting frameworks that may comprise more complete sustainability reporting – for example companies with significant business in the EU, who may be required to prepare sustainability reporting under the EU Corporate Sustainability Reporting Directive. How are these companies going to navigate a restriction on calling such reporting a "sustainability report"?

The intention of making it clear when reporting is part of the statutory sustainability report under ASIC's oversight and subject to the statutory sustainability audit has merit. However, there is an opportunity to provide clearer labelling guidance whilst avoiding confusion – we encourage the following:

– ASIC to provide regulatory guidance that emphasises the importance of clearly distinguishing the statutory sustainability report from other sustainability reporting the company may provide.

– Instead of prescribing how this is to be achieved, ASIC should provide examples and guidance on how it may be achieved – e.g., by labelling the statutory report the "statutory sustainability report", or "the statutory sustainability report prepared per the Corporations Act" – or by labelling the other reporting in ways that clearly distinguishes it from the statutory sustainability report.

5. Thank you for considering our comments

Thank you again for the opportunity to comment. Should you have any further questions or inquiries relating to our comments, please feel free to contact the undersigned.

Regards

[redacted]

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Senior Technical Director, RGEA Cat 2

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[4] KPMG International (November 2024), *The move to mandatory reporting: Survey of Sustainability Reporting 2024* **– accessed in December 2024 at https://assets.kpmg.com/content/dam/kpmgsites/xx/pdf/2024/11/the-move-to-mandatory-reporting-executive-summary.pdf.coredownload.inline.pdf**

[5] KPMG Australia (November 2024): *Australian Sustainability Reporting Trends* – accessed in December 2024 at **https://assets.kpmg.com/content/dam/kpmg/au/pdf/2024/australian-sustainability-reporting-trends-november-2024.pdf**