NOVEMBER 2024 ESG POLICY UPDATE—AUSTRALIA

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Australia Environmental Social Governance (ESG) Alert

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AUSTRALIAN UPDATE

Appointment of the Inaugural Australian Anti-Slavery Commissioner

On 11 November 2023, the Attorney-General announced the appointment of Chris Evans as the inaugural Australian Anti-Slavery Commissioner (Commissioner).

Chris Evans will commence his five-year term as Commissioner on 2 December 2024. He has previously served as CEO of Walk Free's Global Freedom Network and played a significant role in campaigning for the introduction of the *Modern Slavery Act 2018* (Cth) (Modern Slavery Act). Prior to his time at Walk Free, Mr Evans was a Senator for Western Australia, serving for two decades. The appointment comes after the Governor-General assented to the *Modern Slavery Amendment (Australian Anti-Slavery Commissioner) Act 2024* (Cth) on 11 June 2024 (Amendment Act).

The Amendment Act establishes the position and functions of the Commissioner which include:

- Supporting Australian entities and entities carrying on business in Australia to address risks of modern slavery practices in their operations and supply chains;
- Promoting business compliance with the Modern Slavery Act;
- Engagement with victims of modern slavery to inform measures for addressing modern slavery; and
- Supporting, encouraging and conducting education and community awareness initiatives relating to modern slavery.

The Australian Government committed AU$8 million over four years in the 2023-24 Budget to support the establishment and operations of the Commissioner.

For more information on the role of the Commissioner, you can read our June 2024 ESG Policy Update – Australia.

Feedback Sought on Proposed Guidance on Sustainability Reporting Regime

On 7 November 2024, the Australian Securities and Investments Commission (ASIC) released a draft regulatory guide on the new sustainability reporting regime for consultation with stakeholders.

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As reported by K&L Gates on 11 September 2024, certain organisations will be required to make mandatory climate-related financial disclosures in their annual reports for financial years commencing after 1 January 2025.

The draft Regulatory Guide 000 Sustainability Reporting (Draft RG) includes draft guidance on:

- ASIC proposed enforcement approach;
- The scope of directors' ability to rely on third parties;
- The scope of directors' obligations to establish operational systems to assess climate related risks and opportunities;
- The scope of directors' obligations to keep records;
- The bases upon which a reporting entity may make statement of no climate risks;
- The bases upon which a reporting entity may make forward looking climate statements;
- Exceptions to directors' obligations including under proportionality mechanisms and transitional arrangements; and
- The scope of ASIC's enforcement tools including the power to compel corrective statements.

ASIC is seeking feedback on:

- The Draft RG;
- Whether any existing ASIC financial reporting-related instruments should be extended to sustainability reporting; and
- Any other areas of uncertainty on sustainability reporting where ASIC should provide support.

ASIC Commissioner Kate O'Rourke said the focus of the Draft RG is to assist preparers of sustainability reports to comply with their obligations so that users are provided with high-quality, decision-useful, climate-related financial disclosures that comply with the law and relevant accounting standards.

Comments are due by 19 December 2024, including feedback on any other areas where guidance should be provided.

Standby for a separate ESG Alert on this Draft RG.

Concern Over Governance Gap With Use of AI by Licensees

In October, ASIC published its first report on 'Governance arrangements in the face of artificial intelligence (AI) innovation'. The report examines the ways Australian financial services (AFS) licensees and credit licensees are implementing AI that directly or indirectly impacts consumers, identifying a governance gap.

ASIC reviewed 624 cases of AI use by 23 licensees in the banking, credit, insurance and financial advice sectors. Whilst overall, ASIC's findings indicate that the way licensees use AI is cautious in terms of decision making and interactions with consumers, acceleration is rapid and 61% of licensees in the review are planning to increase AI usage in the next 12 months.

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ASIC is concerned that not all licensees are well positioned to manage the challenges that are likely to accompany their increasing use of AI.

The report made the following key observations on the use of AI by licensees:

- The use of AI by licensees varied significantly. While some licensees had incorporated AI use for several years, others had only just adopted AI;
- While the majority of current cases involving AI relied on well-known and established machine-learning techniques that produced explainable results, it was observed that there is an increase in the use of more complex techniques (such as the use of generative AI); and
- Existing AI deployment strategies were mostly cautious, observing that AI was generally used to aid human decisions or increase efficiency and was not used to make autonomous decisions.

ASIC outlined its key findings in respect of risk management and governance, noting that:

- There was a lack of adequate arrangements in place for managing the risks that come with using AI;
- There were significant gaps in how licensees assessed risks, finding that risks were often assessed through the lens of the business rather than the consumer;
- There was wide variation in terms of the maturity of AI governance and risk management frameworks and there needs to be greater attention given to developing a strategic and centralised approach to AI governance; and
- There was a heavy reliance by many licensees on third parties for their AI models, but not all had appropriate governance arrangements in place to manage the associated risks.

ASIC Chair Joe Longo has emphasised the importance of updating governance frameworks to manage the risks associated with AI, such as misinformation, algorithmic bias, and data security issues. He stressed that licensees must not wait for new AI laws but should ensure their governance and compliance measures are robust to handle AI's challenges and benefits responsibly.

Climate Goals Increasingly Forming Part of Executive Remuneration, but Challenges Remain

A study published by the Investor Group on Climate Change (IGCC) and Pollination Global Holdings Limited (Pollination) has found that whilst Australian companies are increasingly linking executive remuneration to climate goals, doubts remain in the effectiveness of this practice.

The study was completed by benchmarking 14 high-emitting companies listed on the Australian Securities Exchange (ASX) against a set of Guiding Principles developed by the IGCC and Pollination which purport to represent best practice in linking executive pay to climate performance.

The Guiding Principles aim to establish a base for effective climate incentives and also encourage a principled approach to ensure the development of unique climate-linked incentives which are simple, measurable and suited to the sector in which the company operates in, rather than a standardised approach across all industries.

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In 2024, 54% of ASX200 companies have integrated climate-related targets into executive remuneration, up from 10% in 2020. Increased regulatory obligations and reputational concerns are cited as common factors driving this growth.

The study contends the best examples of climate incentives were those clearly linked to the company's climate strategy and time horizons and were ambitious and measurable. However, in many other cases, selected metrics are failing to create strong climate transition outcomes, particularly due to difficulty aligning long-term commitments with meaningful short-term action.

The study recommends that companies develop a credible climate strategy before incentivising action to ensure proper strategic alignment and ensure that strategy is functionally integrated into its operations through effective governance, capital allocation and reporting frameworks. Further, it is suggested that providing an engagement framework for investors to evaluate company performance will also foster improved strategic alignment and encourage companies to pursue long-term sustainability over short-term gains.

VIEW FROM ABROAD

80% of Global Financial Regulators Aligned with ISSB, TCFD Recommendations: FSB Report

On 12 November 2024, the Financial Stability Board (FSB) released its 2024 progress report on Corporate Climate-related Disclosures (Report). The Report emphasises the strides made by global jurisdictions in implementing International Sustainability Standards Board (ISSB) disclosure standards.

The Report's key findings were as follows:

- In 2023, 82% of companies disclosed information in line with at least one of the 11 recommended disclosures of the Task Force on Climate-related Financial Disclosures (TCFD), but only a fraction (under 3%) satisfied all 11 recommendations. This suggests that information on climate-related governance, strategy, risk management, and metrics remain undisclosed, which hinders investors' ability to evaluate climate risks and opportunities;
- Between October 2023 and March 2024, more than 1,000 companies referenced the ISSB in their reports;
- In the past 12 months, jurisdictions representing approximately 57% of global gross domestic product have made progress towards the adoption or use of ISSB disclosure standards; and
- 19 out of 24 FSB member jurisdictions have regulations, guidelines or strategic roadmaps in place for climate-related disclosures. Further, 17 FSB jurisdictions have introduced voluntary or mandatory disclosure requirements based on ISSB standards and TCFD recommendations.

ISO Announces new ESG Implementation Principles at COP29

At the 2024 United Nations Climate Change Conference (COP29), the International Organisation for Standardisation (ISO) announced new Environmental, Social and Governance (ESG) Implementation Principles (Principles). Global ESG regulations have increased by 155% in the past decade, which has created a

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challenging environment for consistent reporting across different jurisdictions and sectors. The Principles aim to assist organisations to navigate this increasingly complex ESG landscape.

The Principles were developed in consultation with national bodies, including the British Standards Institution, the Standards Council of Canada and the Brazilian Association of Technical Standards, and incorporate input from over 1,900 industry experts across 128 countries. By providing a standardised structure for sustainability practices designed for use by organisations of all sizes and sectors worldwide, the Principles:

- Support management of ESG performance;
- Bolster measurement and reporting under existing disclosure frameworks to enable consistency, comparability, and reliability of ESG reporting and practices globally;
- Facilitate interoperability by aligning with existing reporting standards, creating a harmonized approach to ESG compliance across borders;
- Promote global consistency, enabling clear communication of sustainability efforts worldwide; and
- Focus on facilitating the integration of ESG principles into organisational culture and addressing environmental impacts, social considerations, and governance practices for a holistic approach to sustainability.

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