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Via email: mavis.tan@asx.com.au
Att: Mavis Tan

27 July 2018

Dear Ms Tan

Response to the consultation on the proposed fourth edition of the ASX Corporate Governance Principles and Recommendations

We welcome the opportunity to respond to your consultation on the proposed fourth edition of the ASX Corporate Governance Principles and Recommendations.

By way of background, the Commonwealth Climate and Law Initiative (CCLI) is a research, education, and outreach project focused on four Commonwealth countries: Australia, Canada, South Africa, and the United Kingdom. The CCLI examines the legal basis for directors and trustees to take account of physical climate change risk and societal responses to climate change, under prevailing statutory and common laws. In addition to the legal theory, we also undertake a practical assessment of the materiality of these considerations, in terms of the scale, timing, and probability of liability and the potential implications for company and investor decision-making.

Our recent publications include:

- *Director's Liability and Climate Risk: Australia – Country Paper*,[1] which provides a comprehensive assessment of the discharge of directors' duties in the climate context under Australian law; and
- *The Climate Risk Reporting Journey: A Corporate Governance Primer*,[2] which is an 'Actionable Framework' for directors on how to integrate climate change issues into governance practice, published in partnership with Minter Ellison and the Centre for Policy Development.

We are strongly supportive of recommendations of the Task Force on Climate-related Financial Disclosures (TCFD Recommendations), which are rapidly emerging as the industry standard. While the TCFD Recommendations provide a framework for reporting rather than board governance per se, as we demonstrate through the Actionable Framework, the reporting

[1] Sarah Barker, Commonwealth Climate and Law Initiative, *Directors' Liability and Climate Risk: Australia – Country Paper* (April 2018) https://ccli.ouce.ox.ac.uk/wp-content/uploads/2018/04/CCLI-Australia-Paper-Final.pdf ('CCLI Country Paper - Australia').

[2] Centre for Policy Development, Commonwealth Climate and Law Initiative and Minter Ellison, *The Climate risk reporting journey: A corporate governance primer* (June 2018) published as Annexure B to Centre for Policy Development, *Climate Horizons Report: Scenarios and Strategies for Managing Climate Risk* (June 2018) https://cpd.org.au/wp-content/uploads/2018/06/Climate-Horizons-report-2018.pdf ('Actionable Framework').

framework of the TCFD Recommendations also informs the robust processes of governance and oversight on which those disclosures must be based.

The CCLI strongly supports the acknowledgement that boards are increasingly being called upon to address issues surrounding sustainability and climate change and supports the reference to the TCFD Recommendations. Yet climate change poses a fundamental challenge to the governance, strategy and risk management of listed entities and requires response across all facets of corporate governance practice. We are concerned that the management and reporting of climate risk is not reflected as a pervasive theme throughout the proposed fourth edition.

In particular, our key concerns about the proposed fourth edition are that it:

- has the potential to cause confusion about existing mandatory legal duties under the *Corporations Act 2001* to report climate risks which are material financial risks;
- lacks clarity in relation to the reporting of climate risk under recommendation 7.4, as recommended by the Senate inquiry into carbon risk disclosure and encouraged by the Federal Government;[3] and
- should provide more detailed guidance on the fundamental role and responsibilities of directors in managing and reporting on the impacts of climate change.

We set out our comments in relation to specific text in the proposed fourth edition below. First, we deal with Principle 7 and recommendation 7.4 in relation to the management and reporting of the impacts of climate change in line with the TCFD Recommendations. Second, we deal with other areas of the proposed fourth edition which we think could better reflect the management of climate risk as a pervasive theme permeating corporate governance practice. Where applicable, we have included in boxes our proposals as to how the text could be amended to address our concerns.

We hope that our suggestions will assist with the progress of your work.

Revised commentary to principle 7 (Recognise and manage risk)

We are pleased to see proposed amendments which go some way to reflect the step change that has occurred in the approach to the management and reporting of the impacts of climate change. In particular, we support the acknowledgement in the commentary to principle 7 that a sound risk management framework should address 'risks with a short, medium or longer term horizon'.

However, we do not support the reference to 'non-financial risks'. The persistence of this terminology perpetuates the misconception that environmental, social and governance issues have no direct impact on corporate value and hence are 'optional extras' from a strategy and oversight perspective. Historically, these have been understood through an ethical lens as issues which a company might address as a moral imperative, but which do not impact on a company's financial prospects or performance. In recent years there has been a fundamental shift in perspective, with an increasing recognition by key stakeholders across the corporate and financial sector that environmental, social and governance issues, and in particular, climate change, present (material) financial risks to companies.

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[3] Senate Economic References Committee, *Final Report - Carbon Risk: A Burning Issue* (April 2017) [4.30] recommendation 2 https://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Economics/Carbonriskdisclosure45/Report ('Senate Inquiry'); Australian Government, *Australian Government response to the Senate Economics Reference Committee report: Carbon risk: A Burning Issue* (March 2018) https://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Economics/Carbonriskdisclosure45/Government_Response.

We suggest the commentary to principle 7 reflect the increasing recognition of the breadth of financial risks as follows:

A sound risk management framework is based on an informed understanding of the key drivers of an entity's long term success and a thorough assessment of the material risks inherent in its business model and strategy. It should address financial risks (established and emerging), including risks that may have historically been perceived as 'non-financial' but which have an impact on corporate performance and value via, at a minimum, impacts on reputation or social licence to operate ~~and non-financial risks~~, as well as risks with a short, medium or longer term horizon.

Revised commentary to recommendation 7.4 (Sustainability disclosures)

Disclosure of climate risks which are material financial risks

We have concerns that the revised commentary to recommendation 7.4 creates unintended confusion in its interaction with disclosure obligations under law, which undermines its ability to provide guidance on climate risk.

Climate change presents material financial risks to many, if not all, listed entities. The types of risks defined in the commentary as 'carbon risk' may materially impact on the profitability and long-term viability of listed entities. The *Global Risk Report 2018* identified extreme weather events, natural disasters and failure of climate change mitigation and adaptation in the top five global risks in terms of both likelihood and impact.[4] Australia's economy is heavily skewed towards those industries and sectors the TCFD considered to be particularly vulnerable to the financial impacts of climate change: financial services, energy, transportation, materials and buildings, and agriculture.[5]

The final report of the Senate inquiry into carbon risk disclosure concludes that 'the committee considers that firms are already required to disclose [climate-change and carbon] risks under the general provisions in ss299(1) and 299A, and that it now falls to regulators to issue appropriate guidance'.[6] Accordingly, the Senate Report recommends that ASIC 'review its guidance to directors to ensure that it provides a proper understanding of the manifestations of carbon risk, and reflects evolving asset measurement implications of carbon risk'.[7]

Formal ASIC guidance, as well as informal guidance such as the recent speech by ASIC Commissioner Price and ASIC Report 567, is of central importance for mandatory disclosure requirements.[8] The ASX Guidance should make clear that it is '*further* guidance to listed entities'[9] about when disclosure is required under recommendation 7.4, which sits alongside any ASIC guidance of when disclosure of climate risk (or other environmental risk) is required to be disclosed under the *Corporations Act 2001*.

Without this clarification, we are concerned that the commentary in the proposed fourth edition

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[4] World Economic Forum, *Global Risks Report 2018* (13th edn, January 2018) http://www3.weforum.org/docs/WEF_GRR18_Report.pdf.
[5] Task Force on Climate-Related Financial Disclosures, Final Report: Recommendations of the Task Force on Climate-related Financial Disclosures (June 2017) ('TCFD Recommendations'). CCLI Country Report - Australia, 7.
[6] Senate Inquiry, [4.34].
[7] Senate Inquiry, [4.30] recommendation 1.
[8] See comments in ASIC Report 567, *ASIC regulation of corporate finance: July to December 2017* (26 February 2018) [152]-[155]; John Price, Commissioner, Australian Securities and Investments Commission, K*eynote address: Centre for Policy Development: Financing a Sustainable Economy, Sydney, Australia, 18 June 2018* https://asic.gov.au/about-asic/media-centre/speeches/climate-change/ ('ASIC Commissioner Price - Keynote Address'.
[9] Senate Inquiry, [4.32].

implies that climate risks are not, or may not be, material financial risks required to be disclosed under the mandatory reporting regime of the *Corporations Act 2001*. Although the definition of 'material exposure' to risk in the commentary to recommendation 7.4 is not identical to the 'materiality' requirement for mandatory disclosure of financial risks,[10] there is likely to be considerable overlap. Yet the proposed commentary states that a listed entity that may make the disclosures under recommendation 7.4 by publishing an integrated report or a sustainability report and is silent as to how this interacts with any mandatory disclosures. A sustainability report is not part of the mandatory reporting regime and while integrated reporting may be used to fulfil the requirements of the mandatory regime,[11] it is not itself a legal requirement.

To avoid undermining listed entities' compliance with their existing legal obligations, the commentary to recommendation 7.4 should acknowledge the primacy of the mandatory disclosure obligations under the *Corporations Act 2001* and to the extent that a climate risk presents a material financial risk to a listed entity, it must be disclosed in mainstream corporate reports and in accordance with any guidance published by ASIC.

<u>Process of benchmarking and analysis for entities that believe they do not have material exposure</u>

We commend the additional commentary that '[e]ntities that believe they do not have any material exposure to environmental and social risks should consider carefully their basis for that belief and benchmark their disclosures in this regard against those made by their peers'.

No company escapes climate risk entirely.[12] It is also widely acknowledged that climate change poses potentially systemic risks to the finance sector which would have implications for the real economy. The final report of the Senate inquiry noted that climate risks 'have potential system wide implications'[13] citing testimony before the committee where Executive Board Member of APRA, Mr Geoff Summerhayes explained that APRA's risk management framework refers to 'six specific risks: credit risks, market investment risks, liquidity risks, insurance risks, operational risks, and strategic investments and business plans. Climate risks potentially impact every one of those…'.[14]

Given the systemic nature of climate risk and number of listed entities which operate in high-risk industries, the starting presumption should be that listed entities do have material exposure to climate risks, but the nature, extent and type of climate risk will depend on the circumstances. Investors increasingly expect to see such disclosures.[15]

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[10] See, for example, 'material business risks' in the operating and financial review: *ASIC Regulatory Guide 247*, [247.61], and 'materiality' in the continuous disclosure context: ASX Listing Rule 3.1; Guidance Note 8.
[11] Proposed amendments to the commentary to recommendation 4.4 recognise that 'some entities use the principles of "integrated reporting" as a useful framework for preparing the mandatory operating and financial reviews' included in the annual directors' report under s299A.
[12] Elisa de Wit and Victoria Vilagosh, 'Climate Change Risks: What Do You Need to Know?', *Governance Directions* (March 2017) 78.
[13] Senate Inquiry, [3.14].
[14] Senate Inquiry, [3.15] citing Mr Geoff Summerhayes, Member, APRA, Committee Hansard 8 March 2017, 40. See also Mr Geoff Summerhayes, Executive Board Member, Australian Prudential Regulatory Authority, Australia's New Horizon: Climate Change Challenges and Prudential Risk, Speech to the Insurance Council of Australia Annual Forum (17 February 2017) http://www.apra.gov.au/Speeches/Documents/ICA%20Speech%20Geoff%20Summerhayes%2017%20February%202017.pdf.
[15] See n31 below and accompanying text.

We suggest that the commentary to recommendation 7.4 cross-refer to proposed new recommendation 4.4 to make clear that this process of analysis and benchmarking should be done as part of the formal process to validate that the listed entity's corporate reports are accurate and provide investors with appropriate information to make informed investment decisions.

Trichotomy of 'carbon risks'

We strongly support the explicit reference to the trichotomy of climate risks – physical, transition and liability risks – first outlined by Prudential Regulation Authority (PRA) of the Bank of England in its seminal 2015 report on the impacts of climate change on the insurance sector and adopted by the Senate inquiry under the terminology 'carbon risks'.[16]

The term 'carbon risks' is unhelpful. It perpetuates the misconception that climate change impacts begin and end with carbon emissions, rather than a broader suite of risks (and opportunities) that arise from the physical, economic transition and liability channels. The ASX Guidelines should resist the narrow term used by the Senate Inquiry and should instead refer to 'climate risk' or 'climate-related risk', which are widely adopted by key stakeholders in Australia and internationally and used in the TCFD Recommendations.

The term 'carbon risk' should be replaced by 'climate risk' or 'climate-related risk'.

Further, the descriptions of transition risks and liability risks are incomplete and miss some key elements of the PRA definition. Transition risks include indirect risks such reputational harm from consumers' or the community's changing perceptions of an entity's response to the transition to a lower carbon economy.[17] Liability risks are not limited to liability for causing, contributing to or failing to mitigate climate change, but also include the risk of liability to the entity or its directors from the failure to manage or disclose climate risk.[18] Indeed this is the type of liability risk which is most likely to materialise.

We suggest the following amendment to the description of 'carbon risk' ('climate risk' or 'climate-related risk') to provide more complete guidance for entities:

transition risks, such as the risks arising from changes in legislation or government policy, or the need to adopt new technologies, seeking to mitigate the effects of climate change or facilitating the shift to a lower carbon economy<u>, and indirect risks including reputational harm</u>; and
liability risks, <u>such as</u> where people who suffer damage caused by climate change, or a failure to respond to climate change, seek redress from those they believe are responsible<u>, or the risk of legal liability for failure to manage or disclose climate-related risks</u>.

[16] Prudential Regulation Authority, *The impact of climate change on the UK insurance sector* (September 2015) 4 http://www.bankofengland.co.uk/pra/Documents/ supervision/activities/pradefra0915.pdf; Senate Inquiry [2.22]-[2.28].
[17] Senate Inquiry, [2.33]. TCFD Recommendations, 5-6.
[18] Senate Inquiry, [2.35]; Noel Hutley SC and Sebastian Hartford-Davis, 'Climate Change and Directors Duties: Memorandum of Opinion for the Centre for Policy Development and the Future Business Council' (7 October 2016) https://cpd.org.au/wp-content/uploads/2016/10/Legal-Opinion-on-Climate-Change-and-Directors-Duties.pdf ('Hutley SC opinion').

Reporting under the framework of the TCFD Recommendations

A theme running throughout our submission is that the TCFD Recommendations are fast becoming the baseline expectation by investors and regulators alike for identifying, assessing and disclosing climate risks. The London Stock Exchange Group also supports a 'comply or explain' approach to the implementation of the TCFD Recommendations. In its submission to the UK's Environmental Audit Committee inquiry into green finance, it stated:

> We recognise the effectiveness and market leadership of the "comply or explain" approach adopted in the UK with regard to disclosure and governance standards, and recommend that the same approach be followed in the implementation of the TCFD recommendations both for financial institutions and listed companies.[19]

Our concern with the wording of the proposed fourth edition is that it creates a 'chicken and egg' problem: how do entities know if they have material exposure to climate risk if they do not have regard to the TCFD Recommendations to adequately identify and assess that climate risk?

To clarify this, and to make a clear statement of the ASX Council's expectations of what is 'high quality reporting' of climate risk, we suggest the following amendment to the commentary to recommendation 7.4:

The Council would encourage all entities ~~that have a material exposure to climate change risk to consider implementing~~ to have regard to the recommendations of the Financial Stability Board's Task Force on Climate-related Financial Disclosures (TCFD) and expects entities that have a material exposure to [carbon / climate risk] to implement the recommendations in the disclosure of that risk.

Glossary definition of 'environmental risks'

We believe the definition of 'environmental risks' is inadequate. We agree that the impacts of a listed entity on the environment are important for investors to assess the prospects and performance of the listed entity. But it is only one aspect of environmental risk. Many of the environmental risks which could have a material impact on the listed entity's prospects or performance arise from the impact of the natural environment on the business, assets and operations of the listed entity. The joint publication of the Australian Council of Superannuation Investors and the Financial Services Council, cited in the proposed fourth edition at footnote 69, identify climate change, water scarcity, material resource scarcity and ecosystem decline as megatrends which may present material risks (and opportunities) to companies and shareholders. Reporting on the impact and perceived impact of the listed entity on the natural environment is not the same as reporting on the impact of the natural environment on the listed entity. The definition of 'environmental risks' should capture both.

Further, the commentary to recommendation 7.4 refers to 'carbon risks' as a 'source of environmental risks'. However, carbon risks do not fall within the definition of environmental risks in the proposed fourth edition.

[19] UK House of Commons, Environment Audit Committee, Greening Finance: Embedding Sustainability in Financial Decision Making (Seventh Report of Session 2017-19, 4 June 2018) [76] https://publications.parliament.uk/pa/cm201719/cmselect/cmenvaud/1063/1063.pdf.

We suggest the following amendments to the definition of 'environmental risks' in the Glossary:

environmental risks: the potential negative consequences to a listed entity arising from the impact of the natural environment on its business, assets or operations or its impact or perceived impact on the natural environment. It includes "[carbon / climate risks]" mentioned in the commentary to recommendation 7.4 above, the risks associated with pollution, environmental degradation, adding to the carbon levels in the atmosphere, and threats to a region's biodiversity or cultural heritage.

Revised commentary to recommendation 1.1 (Role of board and management)

We support the amendment that the board charter should (rather than could) set out the entity's policy on when and how directors may seek independent professional advice at the expense of entity – generally when necessary to discharge their responsibilities.

Developing board understanding of climate risk is key to the discharge of directors' legal duties.[20] A legal opinion by Noel Hutley SC concludes:

> It is likely to be only a matter of time before we see litigation against a director who has failed to perceive, disclose or take steps in relation to a foreseeable climate-related risk that can be demonstrated to have caused harm to the company (including, perhaps, reputational harm).[21]

This opinion was quoted in the final report of the Senate inquiry into carbon risk disclosure, and it is ASIC's view that it appears 'legally sound and reflective of our understanding of the position under prevailing case law in Australia in so far as directors' duties are concerned'.[22]

The CCLI country paper for Australia concluded that:

> It is likely that a director who is uninformed as to the risks associated with climate change, or who makes no conscious decision or judgment on this issue in their consideration of corporate strategy, planning and risk management, or in their consideration of transactions coming before them for approval, would fail to discharge their duty of due care and diligence under section 180 of the *Corporations Act*. The board is required to inquire where information is not presented to them, *and to seek advice on specialist and complicated issues*.
> It is also likely that inadequate consideration of climate-related risks will breach the duty. Australian courts tend to hold directors to particularly high standards of proactivity, professionalism and robust process. When considered in concert with the magnitude of climate-related risks for companies in the predominant sectors of the Australian economy (including energy and resources, financial services, agriculture, real estate, infrastructure and tourism), the courts are likely to hold directors to higher standards of proactive inquiry, *expert advice (from management or independent specialists*) and board evaluation of relevant issues. Moreover, Australian courts have shown a specific propensity to hold directors liable for deficiencies in the parameters or assumptions on which the advice or reports of delegates are based.[23]

The identification, assessment, management and reporting of the impacts of climate change involves a confluence of scientific, economic, financial and technological matters which often

[20] Actionable Framework, 2.
[21] Hutley SC opinion, [51].
[22] Senate Inquiry, [2.36]; ASIC Commissioner Price - Keynote Address.
[23] CCLI Country Paper – Australia, 23-24.

necessitates input from professionals. We find that:

> in informing themselves of (and critically evaluating) the risks and opportunities associated with climate change, *directors would be likely to require the input of independent, expert advice on this dynamic and specialised area* – including in relation to issues such as relevant technological trends and costs of substitute lower-emissions production, carbon pricing regimes, emissions reductions scenarios, the likelihood of each scenario crystallising and the impacts of each on price and demand, asset valuation, strategy and financial planning.[24]

Many directors are ill prepared to navigate this step-change in governance and disclosure expectations.

To provide useful guidance for listed entities, we suggest that the commentary to recommendation 1.1 expressly refer to climate risk:

The board charter should state the entity's policy on when and how directors may seek independent professional advice at the expense of the entity. This generally should be whenever directors, especially non-executive directors, judge such advice necessary for them to discharge their responsibilities as directors. <u>Independent professional advice at the expense of the entity may be appropriate for certain complex risks which affect the long term viability of entities, such as "[carbon / climate risk]" described in the commentary to recommendation 7.4 below</u>.

Revised commentary to recommendation 2.2 (Board skills matrix)

We commend the reference to sustainability and climate change as issues which boards are increasingly being called upon to address.

In the CCLI country paper for Australia, we find that:

> Whilst a board must be reasonably informed, it is not required to be informed of every fact. Whether the board has *sufficient* understanding of the relevant [issue] is a question that depends on the nature of the issue, the quality of the information and advice considered. However, the significance of the potential financial impacts of climate change risks on corporate performance and prospects suggest that the courts will require a proportionally broad and deep understanding of this issue by directors to obtain assurance that a robust interrogation of climate change has been undertaken for their corporation…
> The proliferation of 'soft law' instruments that provide guidance to corporations about their disclosure of climate-related risk are likely to be increasingly persuasive indicators of those kinds of information that directors must inform themselves of, and then critically evaluate, in order to discharge their duty of care.[25]

Such soft law instruments include guidance from APRA, respected bodies such as the Climate Standards Disclosure Board and the Sustainability Accounting Standards Board, and notably, the TCFD Recommendations.

We also draw your attention to our Actionable Framework for directors on how to integrate climate change issues into governance practice. As part of developing board understanding of climate-related risks and opportunities, directors should ask themselves if they understand the

[24] CCLI Country Paper – Australia, 20.
[25] CCLI Country Paper – Australia, 19.

different drivers and consequences of physical risks and economic transition-related risks, the difference between climate change mitigation and adaptation, the role of stress testing and scenario analysis, and relevant exposures to stranded asset risk.[26]

Recommendation 2.6 (Director induction and professional development)

We strongly support the amendment to recommendation 2.6 that listed entities should 'periodically review whether there is a need for existing directors to undertake professional development'. As above, we commend the reference in the commentary to sustainability and climate change as issues which boards are increasingly being called upon to address.

Directors' duties are broadly framed and designed to respond to evolving business norms and market dynamics. While directors' duties are owed by each director individually (generally to the company) and it is each director's responsibility that he or she fulfils those duties, it is in the interests of the listed entity and its security holders that directors do so. As discussed above, climate change is a complex and challenging issue and many directors are ill equipped to understand how climate change risks and opportunities affect the company's performance and prospects, and to then navigate what that means for corporate governance and disclosure.

While we support the addition to the commentary that an entity's induction program should include training on their legal duties and responsibilities as a director, this should not be limited to where the director is not familiar with the legal framework, nor to new directors.

The commentary to recommendation 2.6 should be amended as follows:

The board or the nomination committee of a listed entity should regularly assess whether the directors as a group have the skills, knowledge and experience to deal with new and emerging business and governance issues. Professional development for directors should be considered where gaps are identified and they are not expected to be addressed in the short term by new appointments<u>, and so that each director has an appropriate base level of understanding</u>.

…

The board or the nomination committee should also ensure that directors receive briefings on material developments in laws, regulations and accounting standards relevant to the entity<u>, including the legal duties and responsibilities of its directors</u>.

Revised principle 3 (Instil the desired culture)

We support the substantial change to principle 3 to address matters to do with values, culture and the social licence to operate. The management and reporting of issues relating to climate change has direct ramifications for an entity's social licence to operate. This theme was touched on by ASIC Commissioner John Price in a speech on 18 June 2018, where he noted that:

> For some company stakeholders, the social and environmental impact of corporate activity is an increasingly acute criterion considered in deciding which company to invest in or transact with. A salient question for boards and directors to ask now is therefore:
>
> > *'how do we identify the risks and opportunities presented by this new environment and respond in a manner that is both consistent with the social contract under which we operate and nurturing of long-term business success?'*
>
> For our part, we will continue to encourage boards and directors to ask these

[26] Actionable Framework, 2. Stranded assets risk refers to the risk that an asset cannot viably be exploited at a value, or for the life, for which it was expected to be utilised, which negatively impacts on its current value: CCLI Country Paper – Australia, 7.

> questions of themselves and shine the light on their own culture and corporate governance practices, two drivers which we believe are critical in answering them.[27]

Revised principle 4 (Produce corporate reports of high quality and integrity)

We support the change to principle 4 and additional commentary acknowledging the need for high quality reporting by corporates, in particular in relation to risk, to enable investors to make informed investment decisions.

High quality reporting of climate-related risks (and opportunities) will be crucial to enable investors to make an informed assessment of an entity's prospects for future financial years, as required by the operating and financial review.[28] As the final report of the TCFD states:

> One of the essential functions of financial markets is to price risk to support informed, efficient capital-allocation decisions. … One of the most significant, and perhaps most misunderstood, risks that organizations face today relates to climate change.[29]

Accordingly, the TCFD Recommendations provide a framework for disclosures on climate-related risks and opportunities that are 'consistent, comparable, reliable, and clear'.[30]

Investors are increasingly sophisticated in their approach to climate-related risks and are demanding the same from the entities in which they invest. In September 2017, the CCLI published a briefing to refute misplaced fears in industry about the legal risks of climate disclosure. On the contrary:

> Many major investors are making a strong push for robust climate risk disclosure and see the TCFD recommendations as the strongest framework for this. For example, Aviva Investors has warned more than 1,000 companies globally that it will vote against their annual reports and accounts if they fail to comply with the recommendations. Similarly, in March 2017, BlackRock published its 2017-18 Engagement Priorities, which includes climate risk disclosure and a warning that BlackRock will vote against management – and the re-election of directors – if they do not constructively engage with the issue of climate risk. European institutional investors have also urged companies to adopt the recommendations, as have sovereign wealth funds. For example, Yngve Slyngstad, chief executive of Norway's SWF, the world's largest sovereign investor, has stated: '[w]e want to have more transparency on investment plans and how they are affected [by climate risk]'.[31]

As our analysis shows, saying nothing at all about climate issues in corporate reporting puts directors at far greater risk of being sued than disclosure would. Rather, complying with the TCFD Recommendations will actually protect companies from the kind of liability claims they fear.

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[27] ASIC Commissioner Price - Keynote Address.
[28] *Corporations Act 2001* (Cth) s299A; ASIC Regulatory Guide 247.
[29] TCFD Recommendations, i-ii.
[30] TCFD Recommendations, 1.
[31] Alexia Staker, Alice Garton and Sarah Barker, CCLI, *Concerns misplaced: Will compliance with the TCFD recommendations really expose companies and directors to liability risk?* (September 2017) <https://ccli.ouce.ox.ac.uk/wp-content/uploads/2017/10/CCLI-TCFD-Concerns-Misplaced-Report-Final-Briefing.pdf> 15 citing FT, Aviva Investors demands greater climate change disclosure (20 July 2017) <https://www.ft.com/content/69daf7c6-67e3-11e7-9a66-93fb352ba1fe>, BlackRock, *2017-18 Engagement Priorities* < https://www.blackrock.com/corporate/about-us/investment-stewardship/voting-guidelines-reports-position-papers#2018-priorities>, IPE, *Investors urge widespread adoption of the TCFD climate reporting framework* (29 June 2017) < https://www.ipe.com/news/esg/investors-urge-widespread-adoption-of-tcfd-climate-reporting-framework/10019644.article>; Claire Milhench, Reuters, *Sovereign investors tweak portfolios for environmental risk* (19 June 2017) <https://uk.reuters.com/article/us-global-swf-environment-idUKKBN19A0HP>.

We urge the ASX Council to take the opportunity to make a clear statement of its expectations of what is high quality reporting of climate-related risk. The commentary to Principle 4 should cross-refer to Principle 7 or the commentary to recommendation 7.4 on the application of the TCFD Recommendations (see above).

New recommendation 4.4 (Process to validate directors' and other corporate reports)

We support the addition of new recommendation 4.4. The validation process is crucial for ensuring that the directors' report and other corporate reports are 'accurate, balanced and understandable and provide investors with appropriate information to make informed investment decisions'.

We understand that some stakeholders may be concerned that this new recommendation could create an onerous burden on listed entities and be a potential source of liability for directors. Disclosures to the market must be accurate, although forward-looking disclosures are subject to special rules, where the representation will not be misleading if there are 'reasonable grounds' for making it.[32] Directors already face various avenues for liability for misleading disclosures, either by being primarily engaged in the misleading conduct (for example, making statements in the directors' report) or accessorily involved in the listed entity's misrepresentation under section 79 of the *Corporations Act* (for example, aiding or abetting the listed entity's misleading or deceptive conduct). Misleading corporate disclosures can be a 'stepping stone' to establishing liability for breach of the duty of care and diligence under s180(1) of the *Corporations Act 2001*. Only material misstatements will be actionable.[33]

Accordingly, having a process to validate that corporate reports are accurate, balanced and understandable is a key way to ensure that the listed entity does not make misleading disclosures. As noted in the commentary, disclosure of the validation process assists the market in assessing the quality of information in corporate reports. The validation process is arguably part of the directors' duty of care and diligence so disclosing that process is evidence that directors are discharging their duties. It is likely that complying with the recommendation would protect directors from liability rather than expose them to it.

In relation to climate risk, we draw your attention to the Actionable Framework, which provides detailed guidance on how companies can communicate their path on the climate risk reporting journey so as to ensure that disclosures in corporate reports are complete, accurate and reliable.[34]

The CCLI congratulates the ASX Council on the proposed fourth edition. We hope that our suggestions will assist the ASX Council to provide listed entities with useful guidance on how to navigate the step change in corporate governance practice for the management and reporting of climate-related risks. If we can be of any assistance or you require additional information, please do not hesitate to contact us.

Yours sincerely

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[32] *Corporations Act 2001* (Cth) s 769C; *Australian Securities and Investments Commission Act 2001* (Cth) s12BB.
[33] Conduct in breach of sections 1041E or 1041H of the *Corporations Act 2001* (Cth) or section 12DA of the *Australian Securities and Investments Commission Act 2001* (Cth); CCLI Country Paper - Australia, 26-27, 30, 37.
[34] Actionable Framework, 5.