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External Reporting Board
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Submission on Aotearoa New Zealand Climate Standard 1: Climate-related Disclosures (relating to Strategy and Metrics and Targets)

The Institute of Directors (IoD) appreciates the opportunity to comment on the External Reporting Board's (XRB's) Strategy, and Metrics and Targets Consultation Document (Document) which will form part of the proposed standard, Aotearoa New Zealand Climate Standard 1: Climate-related Disclosures (NZ CS 1).

Key points:

The key points of our submission are:

- We continue to **support the XRB in their development of the climate-related disclosure standards**. It is important that the regime enables effective, meaningful reporting that helps drive strategic thinking and change. The Strategy and Metrics and Targets sections of the standard will provide climate reporting entities (CRE's) with a greater understanding of the implications of climate change on their organisations, and will also assist boards in the wider governance considerations relating to the strategy, purpose and risk management of their organisations.
- We **welcome XRB's acknowledgement that some entities may only be able to initially disclose a limited understanding of the impacts of climate change**. While many CRE's have already developed reporting frameworks, some are only just beginning. It is important that the focus is initially on supporting and encouraging CRE's to meet their reporting obligations and to provide guidance and education to help build capability and competence.
- **While challenging, there are benefits for organisations from the broader reporting of greenhouse gas (GHG) emissions proposed**. Requiring the disclosure of all scope 3 GHG emissions will be particularly challenging for some entities to start with and understanding will be required. A comprehensive approach to disclosing GHG emissions, however, will add value in the long run by contributing to a better understanding of an organisation's value and supply chains.

About the Institute of Directors

The IoD has over 10,000 members, is New Zealand's pre-eminent organisation for directors and is at the heart of the governance community. We believe in the power of governance to create a strong, fair and sustainable future for New Zealand. Our role is to drive excellence and high standards in governance. We support and equip our members who lead a range of organisations from listed companies, large private organisations, state and public sector entities, small and medium enterprises, not-for-profit organisations and charities. Given the size, diversity and spread of our membership many of our members and the organisations they govern will be directly affected by the introduction of climate-related disclosures and many more will be impacted in the future. Our Chartered Membership pathway aims to raise the bar for director professionalism in New Zealand, including through continuing professional development to support good governance.

The IoD is proud to be the host of [Chapter Zero New Zealand](#), the national chapter of the Climate Governance Initiative. The mission of Chapter Zero New Zealand is to "mobilise, connect, educate and equip directors and boards to make climate-smart governance decisions, thereby creating long term value for both shareholders and stakeholders".

Role of directors and boards on climate-related issues

The IoD has identified climate change as one of our Top Five Issues for Directors each year since 2018.¹ Directors clearly see climate action as a key leadership theme, which is evidenced by member feedback in a range of surveys, including our annual *Director Sentiment Survey*. With this focus, boards have a very real opportunity to be a powerful force in taking action on climate-related issues and reducing the environmental impact of their organisations. Climate-related disclosures support that direction.

General comments on XRB's proposals

Consistent with comments made in our first [submission](#) last November, we continue to support the approach the XRB is taking to developing the climate-related disclosure standards, including, in particular:

- staging the consultation process. This allows organisations to get started as soon as possible, which is necessary as the timing of the introduction of the regime is tight.
- enabling effective, meaningful reporting that helps drive strategic thinking and change and ensures that climate-related disclosures do not simply become a compliance exercise for organisations.
- keeping disclosures principles-based and focused on high disclosure levels, rather than being overly prescriptive. A shorter, more succinct standard, with accompanying guidance will allow organisations the flexibility to decide what information to provide, depending on the extent to which they are impacted by climate change. XRB's intention to have forward looking and ambitious disclosures will ensure a consistent clear path for entities to follow as the regime improves over time.
- XRB's intention to issue a climate-related disclosures first-time adoption standard (NZ CS 2) which will help support those entities still in the process of developing high quality disclosures.

To help ensure an effective and successful reporting regime, we encourage the XRB:

- to ensure the standards result in meaningful reporting that is:
 - relevant and of value to a wider group of stakeholders, as well as the intended primary users
 - appropriate to be applied to a wider group of reporting entities should the regime be expanded at a later date.
- to ensure the standards remain consistent and aligned with other national and international reporting frameworks, and in particular with the climate-related disclosure standard currently being developed by the newly formed International Sustainability Standards Board (ISSB). We acknowledge and support the significant amount of work undertaken by the XRB to stay closely connected to the work of the ISSB, as well as the many other international developments in this area. This will help the framework remain internationally relevant and ambitious.
- to follow through the intention to issue guidance as part of the exposure draft and to provide accompanying guidance in an ongoing manner. This will help entities develop capability and competence and ensure they are in a position to make meaningful disclosures. Guidance will also help CREs to understand this mandatory regime and put it into a New Zealand context.

¹ The Institute of Directors in New Zealand (Inc), *Boardroom* magazine, Dec/Jan 2019 issue; Dec/Jan 2020 issue; Dec/Jan 2021 issue; Dec/Jan 2022 issue.

Specific Comments

The proposed strategy section

The intention of the proposed strategy section is to provide primary users with an understanding of the strategic implications of climate change for the entity. Focusing on key strategic, social, governance and environmental risks, and long-term business sustainability, is fundamental to good governance². Complying with XRB's proposed strategy section will not just meet CREs' obligations under the new regime but will also add value to the wider strategic and risk management governance considerations of those organisations.

We support the XRB's attempt to balance the principles and rules-based disclosures in accordance with XRB's design principles. The XRB has used the Task Force on Climate-related Financial Disclosures (TCFD framework) as a base for this section, including some of its recent updates, and has also drawn from the prototypes developed by the International Financial Reporting Standards Foundation's Technical Readiness Working Group (TRWG).

While many entities already have well developed reporting frameworks, some are only at the beginning of their journey and, as such, they may find the strategy section a challenging one to report against. In our 2021 *Director Sentiment Survey* 48% of respondents reported their board is engaged and proactive on climate change risks and practices, while 20% (68% of publicly listed companies) said their latest annual reports included disclosures on climate related risks and/or the impact of climate change on their organisations. It is important to acknowledge that some entities' initial knowledge of the impacts of climate change on their organisations may be limited and it may take some time for them to implement new processes to capture the required data and understand the current risks, opportunities and financial implications. To that end we support the XRB's realistic acknowledgement that, in the first few years at least, some entities may only be able to disclose a limited understanding of the impacts of climate change. It is important that the focus is initially on supporting and encouraging CRE's to meet their reporting obligations and to create effective and meaningful reporting that helps drive strategic thinking and change.

We support the proposed first time adoption provisions for the strategy section. This will help provide clear guidelines on what is expected as plans develop year on year and allows time for entities to build their knowledge and understanding.

We note XRB is not providing climate-related scenarios and agree that industry sectors should be actively encouraged to work together to create sector-level scenario analysis before the standard comes into effect. Boards will need an appropriate level of oversight to ensure they understand how scenario analysis works and its strategic implications. We are aware that some entities have already started work in this area. This should help each industry reduce costs, and improve quality, comparability and consistency of their scenario analysis. It should also assist organisations with the issue of accessing enough climate-related data to support scenario analysis.

We support the XRB's intention to produce a significant amount of guidance in this area, including any guidance that is particularly important for the New Zealand context and environment. Scenario analysis has been excluded from the first time adoption provisions and we agree that this is something entities should

² The Institute of Directors in New Zealand (Inc), *The Four Pillars of Governance Best Practice*, 2021, Ch. 1.3.3

start as soon as possible as it plays a core role in the broader context of the reporting and precedes much of the other work that needs to be done.

We note that part of the disclosures in the strategy section include detailing the governance process used to oversee and manage the scenario analysis process, including the role of board and management. We suggest that this would be more appropriately included in the Governance section, which is intended to provide an understanding of both the board and management's role in overseeing, assessing and managing climate-related issues.

The proposed metrics and targets section

Well-designed and comprehensive reporting systems enable the board to hold management to account and to allocate resources and make strategic decisions with the best information available³. Metrics and targets form part of this.

As with the strategy section the metrics and targets section intends to balance a mix of principles based disclosures. This includes flexibility for entity-specific disclosures and more prescriptive disclosures that provide comparability, particularly around the disclosure of cross-industry metrics.

We support XRB's approach to this, including using the TCFD as a base and taking into account a range of other appropriate resources. We also consider it appropriate that entities should report those metrics that they actually use to manage climate-related risks and opportunities, whether industry specific or entity-specific.

The XRB has required disclosure of scope 3 GHG emissions, which is in alignment with the TCFD and the TRWG. These include all indirect emissions not covered in scope 2 that occur in the value chain of the entity, including all upstream and downstream emissions. We acknowledge that, for many entities, this is where their most significant emissions risks and opportunities lie, however there are significant data and methodological challenges associated with calculating scope 3 GHG emissions and many entities may find this particularly difficult. Despite the initial challenges, however, calculating an entity's scope 3 GHG emissions can add value to an organisation by requiring more robust systems and processes be introduced and can contribute to a more comprehensive understanding of an organisation's value chains.

Assurance

Boards need to be able to rely on the information they receive from management. The right information in board reports provides vital input to board decision-making.⁴ Assurance for financial and non-financial information plays a core part in this process.

Entities will be required to get their GHG emissions disclosures assured for any accounting period that ends on or after 27 October 2024. If the XRB issues NZ CS 1 as intended in December 2022 then all CRE's will publish at least one climate statement before assurance is required. We agree with the XRB's proposal that the minimum level of assurance be set initially at the lower standard of 'limited assurance' (as opposed to the higher standard of 'reasonable assurance') for the following reasons:

³ The Institute of Directors in New Zealand (Inc), *The Four Pillars of Governance Best Practice*, 2021, Ch. 3.9

⁴ The Institute of Directors in New Zealand (Inc), *The Four Pillars of Governance Best Practice*, 2021, Ch. 3.9

- given all scope 1, 2 and 3 emissions will be included there will be a higher degree of estimation involved and it may prove difficult for any assurance practitioner to find enough evidence to provide a reasonable level of assurance
- some entities will still be developing their information systems, processes and controls for an assurance provider to be able to rely on
- a higher standard of assurance would create a greater financial burden on entities.

We anticipate that over time boards will want increasing levels of assurance that their organisations are meeting their disclosure obligations in relation to their GHG emissions, in the same way as they might seek assurance on their financial reporting obligations. While we note that CRE's can choose a higher level of assurance if they wish, we agree with the XRB that the level of assurance should be revisited once the regime is well embedded.

Proposed NZ CS 3 and the definition of materiality

Boards need to operate at a different level from the management of their organisations. Materiality for financial and non-financial information, including climate-related disclosures assists them in doing this.

XRB are proposing that general requirements for climate-related disclosures are included in a third standard (NZ CS 3). This includes a definition of materiality as follows:

“Information is material if omitting, misstating, or obscuring it could reasonably be expected to influence decisions that primary users make on the basis of their assessments of an entity’s enterprise value across all time horizons, including the long term”.

The XRB has defined materiality using a lens of enterprise value, focusing on information about climate-related risks and opportunities that could reasonably be expected to influence decisions by primary users about assessments of an entity’s enterprise value across all time horizons. We support the XRB’s approach to materiality on the following basis:

- it aligns with the TCFD and the recommendations of the TRWG to the ISSB
- it is a pragmatic solution for a new regime that will include entities at all points of the reporting framework journey, with a tight timeframe for introduction
- XRB has left the door open to consider using double materiality (which considers not only the material impact of climate change on the entity itself, but also the entity’s material impact on climate change) in the future should it be considered a more appropriate definition further down the track.

Conclusion

Action is required urgently to address the effects of climate change and the IoD continues to support the approach the XRB is taking in developing climate standards and guidance. Capability to develop high-quality disclosures will take time to develop and the first time adoption standards, along with XRB’s guidance, support and education will help organisations build capability and competency to make meaningful disclosures under the regime. The true value of this reporting will be realised when it goes beyond compliance and is used to drive strategic thinking and decision making across organisations, and realises the goal of reducing emissions.

We appreciate the opportunity to comment on behalf of our members.

Yours sincerely,



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