

* Financial materiality is used here in the broad sense of affecting the value of the company, not just in the sense of affecting financial measures recognised in the financial statements.

Source: (European Union, 2019, p. 5)

Submission

**Oral Submission to Select Committee on
Climate Change Response (Zero Carbon) Amendment Bill
30 August 2019**

About the McGuinness Institute

The McGuinness Institute was founded in 2004 as a non-partisan think tank working towards a sustainable future for New Zealand. *Project 2058* is the Institute's flagship project focusing on New Zealand's long-term future. Because of our observation that foresight drives strategy, strategy requires reporting, and reporting shapes foresight, we developed three interlinking policy projects: *ForesightNZ*, *StrategyNZ* and *ReportingNZ*. Each of these tools must align if we want New Zealand to develop durable, robust and forward-looking public policy. The policy projects frame and feed into our research projects, which address a range of significant issues facing New Zealand. The six research projects are: *CivicsNZ*, *ClimateChangeNZ*, *OneOceanNZ*, *PublicScienceNZ*, *TacklingPovertyNZ* and *TalentNZ*.

About the author

Wendy McGuinness, Chief Executive

Wendy McGuinness wrote the report *Implementation of Accrual Accounting in Government Departments* for the New Zealand Treasury in 1988. She founded McGuinness & Associates, a consultancy firm providing services to the public sector during the transition from cash to accrual accounting from 1988 to 1990. Between 1990 and 2003, she continued consulting part-time while raising children. Over that time she undertook risk management work. In 2002, she was a member of the New Zealand Institute of Chartered Accountants (NZICA) Taskforce, which published the *Report of the Taskforce on Sustainable Development Reporting*. From 2003–2004 she was Chair of the NZICA Sustainable Development Reporting Committee. In 2004 Wendy established the McGuinness Institute in order to contribute to a more integrated discussion on New Zealand's long-term future. In 2009 she became a Fellow Chartered Accountant (FCA).

Contact details:

Wendy McGuinness
Chief Executive

McGuinness Institute
Level 2, 5 Cable Street
PO Box 24-222, Wellington 6142
+64 4 499 8888
wmcg@mcguinnessinstitute.org
www.mcguinnessinstitute.org

1. Key observations

1. We fully support the purpose of the Bill, which is to ‘provide a framework by which New Zealand can develop and implement clear and stable climate change policies that contribute to the global effort under the *Paris Agreement* to limit the global average temperature increase to 1.5° Celsius above pre-industrial levels’ (Explanatory note).
2. The Bill contains three essential components: institutions (i.e. Climate Change Commission), instruments (i.e. emission budgets, risk assessment and adaptation plan) and information (i.e. provision of information).
3. The Bill contains three essential processes: risk identification (i.e. the risk assessment), measurement (i.e. emissions and emission budgets) and management (i.e. the adaptation plan).

2. Key observations regarding information

Table 1: High level analysis of information requirements mentioned in the Bill

Key characteristics	Bill	Outstanding issues
1. Who	Public sector entities (see Figure 1 below)	Private sector and industry organisations should also be included. Note: s 5ZW(1)(a) refers to ‘different sectors’ (which implies primary/secondary sectors). See 3.1 and 3.2 below.
2. What	Listed in s 5ZV(1)	‘Provision of information’ to be separated in a new Part 1D and emissions to be included in list (as necessary for preparing and tracking budgets). See 3.3 and 3.4 below.
3. When	At discretion of Minister (via regulations)	No issues.
4. Where (where information is made available to the public)	Delivered from Minister to the Commission	Clarity required that information provided to the Commission will be publicly available and the Commission will be responsible for creating a repository over time. Note: s 5B does not discuss role of being a repository or providing public access to information. See 3.5 below.
5. How (how information is prepared, sought and delivered)	To be outlined in regulations	Suggest alignment with existing reporting frameworks added to list in s 5ZW(2) – a new (d). See 3.6 below.

3. Areas of concern and suggested solutions

3.1 Private sector and industry organisations should be included under new ss 5ZV(4)(j)–(m).

Our area of interest is the reporting of entities and how this contributes to the risk assessment and the adaptation plan. We suggest that the reporting of entities is regularly reviewed for alignment with national reporting in regard to emissions, risks, and plans.

Since the Bill has been drafted, new information on international initiatives has become available. We discuss these developments in more detail in our *Discussion Paper 2019/01 – The Climate Reporting Emergency: A New Zealand case study*. In this submission we briefly discuss some of these developments to illustrate how New Zealand is falling behind international best practice. Given the responsiveness of the government to climate change, and our emerging economic challenges (particularly in regard to international tourism and agriculture), we believe New Zealand should be a fast follower.

We note the following from the Bill’s *General policy statement* regarding adaptation information-gathering power:

Requiring all organisations, companies, and firms to report on adaptation risks and efforts under the Bill was considered to be cumbersome at this time. Proposals for climate-related financial disclosures have also been ruled out at this time, as those sorts of reporting requirements for the private sector are being progressed outside of the Bill.

This enables future governments to consider extending reporting requirements if they choose to do so.

Although not all organisations should report, those that have a material impact on the climate (e.g. heavy emitters) or those that will be significantly impacted (e.g. infrastructure providers) should report. Reporting requirements should not be determined by the type of organisation but by the extent to which the climate will impact on the entity (what the EU calls ‘financial materiality’ where the audience is the primary investor) and the extent to which the entity will impact on the climate (what the EU calls ‘environmental and social materiality’ where the audience is the consumer, civil society, etc.) (European Union, 2019, p. 5).

We consider it imperative that selected companies be required to report on climate-related information and that those reports should be easy to understand and access.

Although we can see the advantages of legislating requirements for public sector organisations first, we believe this staged approach will disadvantage New Zealand businesses in several ways:

- Overseas investors may see New Zealand as behind in best reporting practices and, may not invest because we do not provide the necessary information to meet their investment portfolio requirements.
- Overseas suppliers may decide not to sell raw products to New Zealand enterprises as they do not meet their supply chain requirements.
- Overseas consumers may decide not to buy/consume New Zealand products and services as they do not act responsibly (even if a New Zealand company does act responsibly, the fact that they do not report it, means competing companies will gain an advantage).
- New Zealand investors/suppliers/consumers will be less informed about the impacts the climate may have on an entity and may lead to investment in an entity with stranded or risky assets. This will create unnecessary uncertainty and volatility in New Zealand financial markets and banking systems.
- New Zealand will transition to a low-emissions economy slower than other nations and therefore lose any competitive advantage from being a market leader. Those that transition early will gain access to markets that are slow to transition (e.g. by adopting low-emission technologies and innovations).
- New Zealand’s reputation and brand will be disadvantaged.

Our concern is that if the Bill is enacted in its current form, it will take many years before the legislation can be revisited and further amendments made to enable selected companies to report climate-related information. We are unable to see the reasoning for this delay, especially given the action already being undertaken in the UK:

- Nearly 12,000 companies are now required to report GHG emissions within the directors' report, which is then required to be filed at the Company House (the equivalent to New Zealand's Companies Register) (Carbon Trust, 2019).²
- The UK's *Green Finance Strategy* outlines the expectation that all listed companies (referred to in the UK as quoted companies) and large asset owners will be required to disclose in line with the TCFD recommendations by 2022 (BEIS & HM Treasury, 2019, p. 23).

By expanding the list of reporting entities in the Bill, future governments will be able to require a wider range of entities to report as and when needed. This will enable New Zealand to follow best practice internationally. We see this as an area of emerging issues that the New Zealand government should position itself to be flexible and responsive to.

Suggestion:

- Add the following entities to the list in s 5ZV(4):
 - (j) listed companies,
 - (k) large companies (as defined in s 45 of the Financial Reporting Act 2013),
 - (l) FMC reporting entities, and
 - (m) other selected entities as considered appropriate.

3.2 More clarity is required over the existing list of reporting organisations under s 5ZV(4).

This will make it more immediately apparent that the reporting provisions apply only to the public sector, not broader companies and organisations.

Suggestions:

- Amend s 5ZV(4)(e) to read 'non-listed companies in which the Crown is a majority or sole shareholder listed in Schedule 4A of the Public Finance Act 1989'.
- Amend s 5ZV(4)(f) to read 'state enterprises listed in Schedule 4A of the Public Finance Act 1989'.

3.3 Sections under 'Power to request provision of information' should include emissions and be treated as a separate, new Part 1D.

Given that (i) ss 5ZV and 5ZW are the only sections in the Bill that relate to entities (all other sections relate to national reporting), (ii) users of climate-related information will require both 'emissions reduction' data and 'adaptation' data to understand the broader narrative and to achieve the targets, and (iii) information is needed in terms of how the climate impacts the entity and how the entity impacts the climate (e.g. along the lines of the EU Guidance mentioned above), we believe ss 5ZV and 5ZW (the 'Power to request provision of information') should relate to both Part 1B 'Emission reduction' and Part 1C 'Adaptation'.

² The Companies (Directors' Report) and Limited Liability Partnerships (Energy and Carbon Report) Regulations 2018 come into force on 1 April 2019 and apply to financial years starting on or after 1 April 2019. The 2018 Regulations impose new obligations for what must be included in the Directors' Report for quoted and large unquoted companies as well as imposing an obligation on large LLPs to prepare a new kind of report ("the Energy and Carbon Report") (DEFRA & BEIS, 2019, p. 7).

"The definition of "large" is the same as applies in the existing framework for annual accounts and reports, based on sections 465 and 466 of the Companies Act 2006. The qualifying conditions are met by a company or LLP in a year in which it satisfies two or more of the following requirements: turnover £36 million or more, balance sheet total £18 million or more number of employees 250 or more' (DEFRA & BEIS, 2019, p. 29).

Suggestions:

- Make the sections in Part 1C under ‘Power to request provision of information’ into a separate, new Part 1D.
- Rename s 5ZV ‘Minister may require certain organisations to provide information on climate change adaptation’ to s 5ZV ‘Minister may require certain organisations to provide information on how the organisation impacts the climate and how the climate impacts the organisation.’

3.4 Include carbon accounting and assurance information under s 5ZV(1)(a).

Although there is room for carbon accounting and assurance information to be required by regulations under s 5ZV(1)(d), we believe retrospective carbon emissions should be reported alongside future-focused prospective emissions, and should therefore be included in the list in s 5ZV(1)(a).

Suggestion:

- Amend s 5ZV(1)(a) to include carbon emissions accounting and, where appropriate, assurance as part of the ‘metrics and costs used to understand and benchmark the effects of climate change’.

3.5 Consider providing more clarity over the role of the Commission as a repository of climate-related information over time under s 5B.

The Commission is a Crown entity acting in the public interest. It will have an extremely important role to play in New Zealand’s future and will need to contend with high levels of uncertainty over data, information, impacts and risks in making its assessments. To this end, it will be in everyone’s interests if the information upon which the assessments are undertaken is made available in the public arena, allowing all stakeholders to discuss and stress-test the thinking of the Commission, and build consensus and support for the resulting adaptation plan.

Suggestion:


- Add a new s 5B(c) to include a purpose of the Commission ‘to be a repository of climate-related information collected by or provided to the Commission and to ensure that public information is made publicly available in a timely manner’.

3.6 Consider accounting for alignment with existing reporting frameworks as part of s 5ZW(2).

To produce consistent and durable public policy, it is important to ensure that those designing and setting out regulations consider the needs of both preparers and users, particularly in terms of the benefits of aligning new reporting requirements with existing reporting frameworks. For example, if the XRB is not responsible for prescribing the recurring reporting requirements, the reporting tiers already established by the XRB’s Accounting Standards Framework for public benefit entities and for-profit entities should still be taken into account. Those designing the information requirements will need to be aware of the wide range of standards and guidance that exist such as the XRB’s *ISAE (NZ) 3410: Assurance Engagements on Greenhouse Gas Statements*. Having an overall strategy on reporting would ensure that we do not create silos. A consistent reporting framework will make reporting clearer and easier for preparers and users of reports.

Figure 1: Reporting entities under the Bill and existing accounting standards

Entity Type	Public Policy Perspective		Accounting Perspective	
	Public	Private	Public benefit entities	For-profit entities
Public sector entities (e.g. Crown entities)	✓		✓	
Public sector for-profit entities (e.g. SOEs)	✓			✓
Private sector not-for-profit entities (e.g. registered charities)		✓	✓	
Private sector for-profit entities (e.g. listed companies and FMC reporting entities)		✓		✓

 Covered under the Climate Change Response (Zero Carbon) Amendment Bill

Suggestion:

- Add a new s 5ZW(2)(d) ‘the alignment of new reporting frameworks with existing reporting frameworks’.

References

Business, Energy and Industrial Strategy UK (BEIS) and HM Treasury. (2019). *Green Finance Strategy: Transforming Finance for a Greener Future*. NL: HM Government. Retrieved 8 August 2019 from https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/820284/190716_BEIS_Green_Finance_Strategy_Accessible_Final.pdf.

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