Pollination
in collaboration with the
Commonwealth Climate and Law Initiative

"Nature-related risks and directors' duties"

Joint Memorandum of Opinion
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A. INTRODUCTION

1. We are asked to provide our opinion on the extent to which a director's duty of care and diligence under s 180 of the *Corporations Act 2001* (Cth) (**Act**) permits or requires company directors to consider, disclose and manage nature-related risks arising from dependencies and impacts on nature. While companies' nature-related dependencies and impacts may give rise to opportunities, we approach the topic for the purposes of this opinion from the perspective of risk and liability, which is more likely to be the focus of litigation against a director.

2. We adopt the definition of "nature-related risks" endorsed by the Taskforce on Nature-related Financial Disclosures (**TNFD**), namely: "potential threats (effects of uncertainty) posed to an organisation that arise from its and wider society's dependencies and impacts on nature."[1] This definition aligns with the International Organization for Standardization (ISO) 31000 Risk Management Standard and its definition of risk as the "effect of uncertainty on objectives".[2] When analysed from the perspective of directors' duties, that definition is almost self-fulfilling: the definition *assumes* that there are threats (i.e., risks) to an organisation from its dependencies and impacts on nature. The challenge for directors, of course, will be in identifying and giving content to the potential threats. In doing so, it is very important to note the dual aspect of the definition: it is not only threats to an organisation from its *dependencies* on nature, but also the threats to an organisation from its *impacts* on nature.

3. In summary, in our opinion, as a matter of Australian law:

   (a) "Nature-related risks" are, by definition, risks of harm to the interests of Australian companies.

   (b) At a general level, and subject to the circumstances of the company in question, there are risks arising from *dependencies* and *impacts* on nature that would be

[1] TNFD, *Recommendations of the Taskforce on Nature-related Financial Disclosures* (Report, September 2023) (**TNFD Recommendations**) page 131.
[2] International Organization for Standardization, *ISO 31000:2018 Risk Management – Guidelines* (February 2018), Section 3 'Terms and definitions'; TNFD Recommendations, page 33.

regarded by a court as being foreseeable at the present time. We give some examples below, to illustrate that "nature-related risk" is a label for a genus of risk to which directors should be alert.

(c) Directors of companies should at least identify the company's nature-related dependencies and impacts, and consider the potential risks this may pose to the company. Directors who fail to consider nature-related risks could be found liable for breaching their duty of care and diligence.

(d) Particular care should be taken in relation to nature-related *impacts*, to assess whether they do in fact pose a risk of harm to the company and to balance that risk against whatever opportunities or benefits may arise from undertaking a relevant business activity. Evolving societal and market expectations are likely reducing the number of nature-related impacts that can be said to pose no risk of harm to a company, particularly when it is appreciated that "harm" may not be confined to a company's immediate financial interests but extends to *any* of the interests of the company, which includes reputational risk.[3]

(e) Companies are required to disclose nature-related dependencies and impacts that pose a material risk of harm to the company in its directors' report and corporate governance statement.[4] They may also be required to disclose nature-related impacts that do *not* pose a material risk of harm to a company where:

i. those impacts "would, or would be likely to, influence persons who commonly invest in securities in deciding whether to acquire or dispose" of the company's securities;[5] and/or

ii. the company is subject to the European Union's Corporate Sustainability Reporting Directive (**CSRD**), which requires the disclosure of nature-related impacts regardless of their materiality.[6]

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[3] *ASIC v Cassimatis (No 8)* (2016) 336 ALR 209, 301 [480]-[482] (Edelman J); *Cassimatis v ASIC* (2020) 275 FCR 533, 640-641 [459] (Thawley J); *ASIC v GetSwift Ltd* [2021] FCA 1384, [2529] (Lee J).

[4] In relation to directors' reports, see Act s 299A and ASIC, *Regulatory Guide 247: Effective disclosure in an operating and financial review* (August 2019), RG 247.64. In relation to corporate governance statements, see ASX Listing Rule 4.10.3 and ASX Corporate Governance Council, *Corporate Governance Principles and Recommendations (Fourth Edition)* (February 2019), Recommendation 7.4.

[5] Act, ss 674, 677.

[6] *Directive (EU) 2022/2464 of the European Parliament and of the Council of 14 December 2022 amending Regulation (EU) No 537/2014, Directive 2004/109/EC, Directive 2006/43/EC and Directive 2013/34/EU, as regards corporate sustainability reporting* [2022] OJ L 322/15 (**EU Directive**), arts 19a(1) and 29a(1).

(f) These disclosure requirements form part of directors' duties, because, while s 180(1) does not explicitly and directly impose a duty to prevent a company from contravening the law,[7] directors owe a duty to exercise reasonable care and diligence to prevent the harm that a contravention of the law may cause to a company.[8]

4. Important to these conclusions, and to any consideration of the topic of "nature-related risk", are two international developments. The *first* is that, on 19 December 2022, almost 200 countries, including Australia, agreed to the Kunming-Montreal Global Biodiversity Framework (**GBF**). Target 15 of the GBF requires signatories to take "legal, administrative or policy measures to encourage and enable business… [to] monitor, assess and transparently disclose their risks, dependencies and impacts on biodiversity". The *second* is that, on 18 September 2023, the TNFD finalised its framework for nature-related risk and opportunity management and disclosure,[9] which will support corporate reporting in line with Target 15.[10]

5. Neither of these developments creates binding obligations as a matter of domestic law. But they are relevant as recognitions and drivers of the type of market expectations which informs analysis of risk. Thus, in its recommendations, the TNFD observes that "[c]entral banks and financial supervisors are increasingly recognising nature loss as a source of systemic risk to financial systems and economies".[11] The TNFD refers to the conclusion by the Network for Greening the Financial System, a network of over 125 central banks and financial supervisors, that "nature-related risks could have significant macroeconomic implications, and that failure to account for, mitigate and adapt to these implications is a source of risks for individual financial institutions as well as for financial stability."[12]

6. These developments reflect increasing investor and stakeholder focus on "nature-related risk" and underscore the utility of "nature-related risk" as a framework for directors to assess threats. The concept of "nature-related risk" is therefore, at least, a useful

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[7] *ASIC v Maxwell & ors* (2006) 59 ACSR 373, 399 [104] (Brereton J); *ASIC v Cassimatis (No 8)* (2016) 336 ALR 209, [539] (Edelman J); *Cassimatis v ASIC* (2020) 275 FCR 533, 641 [460] (Thawley J).
[8] *DSHE Holdings Ltd v Abboud & ors* (2021) 155 ACSR 1, 113 [447] (Ball J).
[9] 'Final TNFD Recommendation on nature related issues published and corporates and financial institutions begin adopting', *TNFD* (Media Release, 18 September 2023) <https://tnfd.global/wp-content/uploads/2023/09/FINAL-18-09-23-TNFD-final-recommendations-release.pdf>.
[10] TNFD Recommendations, page 18.
[11] TNFD Recommendations, page 7.
[12] TNFD Recommendations, page 7.

organising principle through which directors can assess the implications for a company arising from dependencies and impacts on nature, including: resource availability, disruption of supply chains, regulatory compliance, and reputational damage. Sector-specific guidance from the TNFD, referred to at [38] below, as supplemented by whatever law and regulation follows in Australia,[13] will help companies to analyse the risks faced by their company with more specificity.

7. We understand that this opinion is intended to provide practical guidance to our instructors' clients and a broader audience of directors, managers and practitioners. To that audience, it will not necessarily be helpful for us to focus on the particular circumstances of any sector or company. But addressing this topic at higher levels of abstraction is difficult because of the breadth of the definition of "nature-related risks". Because a given company's nature-related impacts and dependencies are likely to be so broad and wide-ranging, any abstract conclusions about s 180 and "nature-related risk" may seem to lack practical utility. However, closer analysis will reveal that "nature-related risks" often will be a relevant framework for analysis of business risks, and, to that extent, do inform directors' duty of care.

B. ARE NATURE-RELATED RISKS FORESEEABLE?

8. In determining whether a director has breached their duty of due care and diligence, a court will balance "the foreseeable risk of harm against the potential benefits that could reasonably have been expected to accrue to the company from the conduct in question".[14] A risk is "foreseeable" if it is not "far-fetched or fanciful".[15] The foreseeability of a risk is therefore different to its probability: a risk may be foreseeable despite being unlikely to occur.

9. The Australian economy is acutely exposed to risks arising from the deterioration of the natural environment. Recent scientific research has found that all 19 Australian ecosystems under examination in that study have collapsed or are collapsing.[16] It has

[13] Including regulatory standards and guidance from official regulators such as ASIC and the ASX Corporate Governance Council.
[14] *Vrisakis v ASIC* (1993) 9 WAR 395, 449-450 (Ipp J).
[15] *Council of the Shire of Wyong v Shirt* (1980) 146 CLR 40, 47-48 (Mason J); *ASIC v Rich* (2009) 236 FLR 1, 139 [7231] (Austin J).
[16] Dana M. Bergstrom et al., 'Combating ecosystem collapse from the tropics to Antarctica' (2021) 27 *Global Change Biology* 1692, 1694.

been estimated that approximately half of Australia's gross domestic product (**GDP**) has a moderate to very high direct dependence on "ecosystem services".[17]

10. Companies' nature-related risks will vary significantly depending on the sector in which a company operates and other circumstances unique to a company. Determining whether nature-related risks represent a foreseeable risk of harm to any given company will therefore require a close analysis of that company's particular nature-related dependencies and impacts, amongst other things. For reasons developed below, in our opinion, at a general level, companies' nature-related dependencies and impacts are capable of posing risks of harm to the interests of Australian companies, and could be regarded by a court as being foreseeable at this time.

B.1 Risks arising from nature-related dependencies

11. "Nature-related dependencies" are the aspects of ecosystem services that a company relies on to function.[18] Ecosystem services, described as the contributions of ecosystems to the benefits that are used in economic and other human activity, fall into one or more of the following categories:[19]

    (a) **Provisioning services** represent the flow of benefits that are extracted or harvested from ecosystems. For example, the extraction of freshwater from a river or timber from a forest.

    (b) **Regulating and maintenance services** result from the ability of ecosystems to regulate biological processes and to influence climate, hydrological and biochemical cycles, and thereby maintain environmental conditions beneficial to individuals, organisations and society. Provisioning services are dependent on these regulating and maintenance services. For example, the provision of freshwater depends on the ability of forests to absorb carbon and regulate climate change.

    (c) **Cultural services** are the experiential and intangible services related to the perceived or actual qualities of ecosystems whose existence and functioning

[17] Australian Conservation Foundation, *The nature-based economy: How Australia's prosperity depends on nature* (Report, September 2022) page 6.
[18] TNFD Recommendations, page 115.
[19] TNFD Recommendations, pages 26, 118; TNFD, *Guidance on the identification and assessment of nature-related issues: The LEAP approach* (Report, September 2023) page 11.

contributes to a range of cultural benefits. For example, the recreational value of a coral reef for tourism.

12. Australian ecosystem services are uniquely vulnerable. According to the Swiss Re Institute, as at September 2022, 39 countries, including Australia, have ecosystems in a fragile state for more than 30% of the entire country area.[20] The Institute pointedly identified Australia as a country that "should prepare for ecologically driven disturbances".[21] This is consistent with the 2021 State of the Environment Report, which graded Australia's biodiversity as "poor", with an overall deteriorating trend.[22] In particular, it concluded that:

(a) Australia has lost more mammal species than any other continent and continues to have one of the highest rates of species decline among countries in the OECD.[23]

(b) More than 1,900 Australian species and ecological communities are known to be threatened or at risk of extinction, and there is "concern that our current listing processes are failing to keep up with the actual rate of biodiversity loss".[24]

(c) The number of threatened ecological communities listed under the *Environment Protection and Biodiversity Conservation Act 1999* (Cth) (**EPBC Act**) has risen 20% over the last five years. As at June 2021, 87 were listed, of which 41 are Critically Endangered, 44 are Endangered, and 2 are Vulnerable.[25]

13. The nexus between ecosystem services and economic interests is now well established. As noted above, it has been estimated that approximately half of Australia's GDP has a moderate to very high direct dependence on ecosystem services.[26] Industries with a very high direct dependence on nature, such as agriculture, forestry, fisheries, construction, and waste and water services, generate $293.6 billion a year, approximately 15.9% of Australia's GDP.[27] Industries that have a high or very high direct dependence on nature

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[20] Swiss Re Institute, *Biodiversity and Ecosystem Services: A business case for re/insurance* (Report, September 2020) pages 3, 28.
[21] Swiss Re Institute, *Biodiversity and Ecosystem Services: A business case for re/insurance* (Report, September 2020) page 35.
[22] Commonwealth of Australia, *Australia state of the environment 2021: overview* (Report, 2021) page 55.
[23] Commonwealth of Australia, *Australia state of the environment 2021: overview* (Report, 2021) page 56.
[24] Commonwealth of Australia, *Australia state of the environment 2021: overview* (Report, 2021) page 58.
[25] Commonwealth of Australia, *Australia state of the environment 2021: overview* (Report, 2021) page 59.
[26] Australian Conservation Foundation, *The nature-based economy: How Australia's prosperity depends on nature* (Report, September 2022) page 6.
[27] Australian Conservation Foundation, The nature-based economy: How Australia's prosperity depends on nature (Report, September 2022) page 6.

are said to be responsible for more than three quarters of Australia's export earnings, with resources accounting for 68.7% of Australia's export share and agriculture another 11.3%.[28] Industries with a low direct dependence on nature may also be exposed to nature-related dependencies through their supply chains. In this regard, the World Economic Forum identifies six industries with less than 15% of their direct gross value added "highly dependent" on nature, but with more than 50% of the gross value added of their supply chains being highly or moderately dependent on nature: chemicals and materials; aviation; travel and tourism; real estate; mining and metals; supply chain and transport; and retail, consumer goods, and lifestyle.[29]

14. A recent example of a dependency-related risk is the spread of varroa mite in New South Wales (**NSW**), which was the subject of a state-wide emergency order by the NSW Chief Plant Protection Officer on 13 March 2023.[30] According to the NSW Department of Primary Industries, varroa mites are the most serious pest of honey bees worldwide, and, left untreated, will kill all honey bee colonies across Australia.[31] This would seriously reduce the positive impact of honey bees as pollinators of a range of horticultural, broadacre crop and pastoral plants, and, according to some reports, would "dramatically diminish" the range of available food products.[32] This is not just a risk to companies involved in honey-production. It also impacts those with direct and supply chain dependencies on pollination services from honey bees, such as agriculture and food and beverage.

15. The threat to pollinators is an example of a broader threat to Australia's ecosystems. The Australian economy's dependence on Australian ecosystems is obvious. The threat to those ecosystems from and associated with (for example) climate change is obvious. It follows logically, in our opinion, that risks arising from nature-related dependencies have the potential to cause harm to the interests of Australian companies and fall within the ambit of a director's duty.

[28] Australian Conservation Foundation, The nature-based economy: How Australia's prosperity depends on nature (Report, September 2022) page 6.
[29] World Economic Forum, Nature Risk Rising: Why the Crisis Engulfing Nature Matters for Business and the Economy (Report, January 2020) page 14.
[30] Chief Plant Protection Officer (NSW), *Biosecurity (Varroa Mite) Emergency Order (No 7) 2023* (13 March 2023).
[31] NSW Department of Primary Industries, *NSW DPI Primefact – Varroa mites* (Factsheet, June 2022) pages 1-2.
[32] NSW Department of Primary Industries, *NSW DPI Primefact – Varroa mites* (Factsheet, June 2022) page 2.

B.2 Risks arising from nature-related impacts

16. "Nature-related impacts" are changes in the state of nature, which may result in changes to the capacity of nature to provide social and economic functions, including ecosystem services. They can be positive or negative, and can be: direct, i.e., occurring immediately as a result of direct actions such as land clearing; indirect, i.e., occurring as a consequence of another factor with an indirect causal link, such as greenhouse gas emissions contributing to climate change; or cumulative, i.e., occurring due to the interaction of activities of different actors operating in a landscape.[33]

17. Nature-related impacts can create or exacerbate dependency-related risks where those impacts are on the same set of ecosystem services on which a company depends. This can be illustrated by reference to the same example of pollinators. It has been reported that change of land use due to agricultural production is responsible for 70-96% of tropical deforestation and habitat loss.[34] Habitat loss is in turn one of the main drivers of pollinator decline.[35] The intensification of agricultural production in pasture areas has also been associated with a 75% decline in pollinator populations.[36] An agricultural company's contribution to habitat loss is an *impact* on nature that may create or exacerbate the risk posed by the loss or reduction of pollination services on which the company depends.

18. Historically, it might have been logical to claim that a company's adverse impacts *on* nature bear no necessary correlation to financial or reputational risk *to* the company if they do not impact the same ecosystem services on which the company relies. But the international developments to which we refer above show that this logic is now unsound. The GBF aims to "catalyze, enable and galvanize urgent and transformative action by Governments … with the involvement of all society, to halt and reverse biodiversity loss".[37] This gives rise to transition risk. If the GBF aim is *not* achieved, there is profound medium and long term risk to companies due to potential disruptions to the

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[33] TNFD Recommendations, page 122.

[34] Helmut Geist and Eric Lambin, 'Proximate causes and underlying driving forces of tropical deforestation' (2002) 52(2) *BioScience* 143; Holly Gibbs et al., 'Tropical forests were the primary sources of new agricultural land in the 1980s and 1990s' (2010) 107(38) *Proceedings of the National Academy of Sciences* 16732; Noriko Hosonuma et al., 'An assessment of deforestation and forest degradation drivers in developing countries' (2012) 7(4) *Environmental Research Letters* 044009.

[35] Simon Potts et al., 'Global pollinator declines: trends, impacts and drivers' (2010) 25(6) *Science* 345.

[36] Joseph Millard et al., 'Global effects of land-use intensity on local pollinator biodiversity' (2021) 12(2902) *Nature Communications* 1.

[37] *Decision adopted by the Conference of the Parties to the Convention on Biological Diversity* CBD/COP/DEC/15/4 (19 December 2022), Annex [4].

ecosystem services on which they rely. If that aim *is* achieved, then it will be achieved at the expense of any company which has proceeded on the assumption that its impacts on nature present no necessary correlation to financial or reputational risk.

19. The TNFD "strongly recommends" that companies identify and assess their nature-related impacts.[38] If a company seeks to align with Target 15 of the GBF, the TNFD recommends the disclosure of a company's most significant impacts on nature, regardless of whether those impacts pose a risk to the company.[39]

20. The focus on nature-related impacts in the GBF and TNFD will shift market expectations and, ultimately, regulatory requirements. That will in turn exacerbate the risks associated with those impacts.

21. The trajectory of the recommendations of the Taskforce on Climate-related Financial Disclosures (**TCFD**) is informative, especially given its adoption already in Australian regulation, official regulatory guidance, and corporate practices. It has been reported that when the TCFD recommendations were released in 2017, 10.5% of the ASX200 reported against or committed to reporting against those recommendations.[40] From early 2019, Australian regulatory guidance recommended that companies use the TCFD framework when disclosing material climate-related risks in accordance with their disclosure obligations under the Act.[41] International jurisdictions have since introduced mandatory climate-related disclosure frameworks that broadly align with the TCFD,[42] and it appears that Australia will soon follow suit.[43] The influence of the TCFD is such that, as at 31 March 2023, 75% of the ASX200 is said to have reported against or committed to reporting against the TCFD despite the framework still being voluntary.[44] As noted above, there has been litigation alleging that a failure to disclose climate-related risks in

[38] TNFD Recommendations, page 41.
[39] TNFD Recommendations, pages 41-42, 122, 128.
[40] Australian Council of Superannuation Investors, *Promises, Pathways & Performance: Climate Change Disclosure in the ASX200* (Report, August 2023) page 4.
[41] See, for example, ASX Corporate Governance Council, *Corporate Governance Principles and Recommendations* (Fourth Edition, February 2019) Recommendation 7.4.
[42] See, for example, *Companies (Strategic Report) (Climate-related Financial Disclosure) Regulations 2022* (UK); *Financial Sector (Climate-related Disclosures and Other Matters) Amendment Act 2021* (NZ); *Ordinance on Climate Disclosures* (Switzerland) SR 220.
[43] Treasury, Commonwealth of Australia, *Climate-related financial disclosure* (Consultation Paper, June 2023).
[44] Australian Council of Superannuation Investors, *Promises, Pathways & Performance: Climate Change Disclosure in the ASX200* (Report, August 2023) pages 4, 5.

accordance with the TCFD constitutes a breach of statutory duties comparable to s 180(1) of the Act.[45]

22. The TNFD may well follow a similar trajectory. Even before the framework was finalised, there was evidence that it was heightening market expectations in relation to nature-related impacts. On August 2022, Impax Asset Management stated that, in accordance with the TNFD recommendations, its investment decisions would be informed by both the nature-related risks *to* its investments and the potential negative nature-related impacts *of* its investments. It states that the latter allows it to capture "both the potential for liability or loss of license to operate, and also start to identify the knock-on and cumulative effects of biodiversity loss on long-term economic growth".[46] That is consistent with recent research by the Swiss Finance Institute and the European Corporate Governance Institute, which suggests that companies' nature-related impacts are already "beginning to be priced by investors".[47] It concluded that "following the UN Biodiversity Conference (COP15), which raised awareness of biodiversity issues, firms with larger corporate biodiversity footprints lost value".[48] The authors suggest that "[t]his response is consistent with investors revising their valuation of these firms downward upon the prospect that regulations to preserve biodiversity will become more stringent".[49]

23. There is also evidence that the focus on nature-related impacts in the GBF and the TNFD is influencing regulatory requirements in international jurisdictions. As noted above, the European Union's CSRD will require covered entities to disclose nature-related impacts regardless of their materiality to the entity.[50]

24. These trends have been seen before, in relation to climate-related disclosures and the TCFD. They are evidence of increasing consumer and investor interest in nature-related risks, including those that arise from companies' impacts on nature.

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[45] *McVeigh v Retail Employees Superannuation Pty Ltd* (Amended Concise Statement, Federal Court of Australia, NSD1333/2018, 24 September 2018) paragraph 15(b). The claim in that case relevantly concerned s 52(2)(b) of the *Superannuation Industry (Supervision) Act 1993* (Cth), which imposes a duty on superannuation trustees comparable to the duty imposed on company directors by s 180(1) of the Act.
[46] Impax Asset Management, *Impax Policy on Nature, Biodiversity and Deforestation* (Policy Statement, August 2022) page 2.
[47] Swiss Finance Institute and European Corporate Governance Institute, *Do Investors Care About Biodiversity?* (Finance Working Paper No. 905/2023, March 2023) page 7.
[48] Swiss Finance Institute and European Corporate Governance Institute, *Do Investors Care About Biodiversity?* (Finance Working Paper No. 905/2023, March 2023) Abstract.
[49] Swiss Finance Institute and European Corporate Governance Institute, *Do Investors Care About Biodiversity?* (Finance Working Paper No. 905/2023, March 2023) Abstract.
[50] EU Directive, arts 19a(1) and 29a(1).

B.2(a) Possible regulatory developments

25. In our opinion, there are foreseeable risks of regulatory change, increased costs of business, and/or the potential prohibition of certain activities presently important to profit-generation in Australia.

26. The GBF includes four goals for 2050 and 23 targets for 2030. In accordance with Target 2 of the GBF, the Australian government has committed to protecting 30% of Australia's land and ocean by 2030.[51] In December 2022, it foreshadowed the introduction of national environmental standards that will require projects and plans approved under the EPBC Act to "avoid unacceptable and unsustainable impacts on matters of national environmental significance" and deliver "net positive outcomes for matters of national environmental significance".[52] It is intended that national environmental standards will be subject to regular review, with future amendments able to strengthen but not weaken environmental protection.[53] This means that companies undertaking actions that are regulated by the EPBC Act are likely to be required to comply with more stringent environmental requirements in the future.

27. There is also the prospect of risks associated with regulatory change in jurisdictions that are major trading partners, or which otherwise have laws and regulation that affect members of transnational groups including Australian companies. On 29 June 2023, the EU Regulation on deforestation-free supply chains entered into force.[54] This sets mandatory due diligence rules for companies that place specific commodities on the EU market: soya, cattle, palm oil, wood, cocoa, coffee, rubber, charcoal, printed paper, and some derived products, such as leather, chocolate and furniture.[55] Companies will need to prove that such commodities were produced on land that was not subject to deforestation after 31 December 2020,[56] and will be required to provide precise geographical information about the farmland where the commodities have been grown

[51] 'Environment back under the Albanese Government', *Minister for the Environment and Water, Commonwealth of Australia* (Media Release, 25 October 2022) <https://minister.dcceew.gov.au/plibersek/media-releases/environment-back-under-albanese-government>.
[52] Department of Climate Change, Energy, the Environment and Water, Commonwealth of Australia, *Nature Positive Plan: better for the environment, better for business* (December 2022) page 12.
[53] Department of Climate Change, Energy, the Environment and Water, Commonwealth of Australia, *Nature Positive Plan: better for the environment, better for business* (December 2022) page 2.
[54] *Regulation (EU) 2023/1115 of the European Parliament and of the Council of 31 May 2023 on the making available on the Union market and the export from the Union of certain commodities and products associated with deforestation and forest degradation and repealing Regulation* (EU) No 995/2010 (**EU Regulation**).
[55] EU Regulation, Annex I.
[56] EU Regulation, art 2(13).

or sourced, so that the commodities can be checked for compliance.[57] Countries will be classified as high, standard or low risk of deforestation, which will in turn inform companies' obligations under the EU Regulation.[58] This is particularly significant for Australian companies given eastern Australia has been identified as one of 24 global deforestation "hotspots", and is the only developed country on that list.[59] It is reported that American legislators consider the EU Regulation will hasten the passage of a similar law in the United States.[60]

28. This presents clear risks for Australian companies that produce commodities grown on land that has been subject to deforestation, such as those involved in beef production. In 2021, exports represented 72% of total red meat production in Australia.[61] While the EU and US are small destination markets for Australian red meat exports,[62] there is a risk that larger trading partners could introduce similar regulations, which would be of greater significance to Australian exporters. If this were to occur, it could prevent the export of Australian produce to those destination markets, thereby potentially reducing producers' income.

B.2(b) Shifting investor / consumer behaviour

29. There are also risks associated with potential shifts in the behaviour and preferences of investors, consumers, and other stakeholders, including insurers and financiers.

30. At the time of writing this opinion, 153 financial institutions representing €21.4 trillion in assets have signed the Finance for Biodiversity Pledge, which commits signatories to incorporating biodiversity criteria in their ESG policies, assessing the biodiversity impacts of their financing activities and investments, and setting and disclosing

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[57] EU Regulation, arts 2(28), 9(1)(c) and (d).
[58] EU Regulation, arts 13, 29.
[59] World Wide Fund for Nature, *Deforestation Fronts: Drivers and Responses in a Changing World* (Report, January 2021) pages 6-7.
[60] 'EU ban on deforestation-linked goods sets benchmark, says US lawmakers' *The Guardian* (News Article, 6 January 2023) <https://www.theguardian.com/environment/2023/jan/05/eu-ban-on-deforestation-linked-goods-sets-benchmark-say-us-lawmakers#:~:text=From%202024%2C%20the%20EU%20will,date%20of%2031%20December%202020>.
[61] 'Global markets export wrap', *Meat and Livestock Australia* (News Article, 9 March 2022) <https://www.theguardian.com/environment/2023/jan/05/eu-ban-on-deforestation-linked-goods-sets-benchmark-say-us-lawmakers#:~:text=From%202024%2C%20the%20EU%20will,date%20of%2031%20December%202020>.
[62] 'Australian red meat export statistics', *Department of Agriculture, Fisheries and Forestry, Commonwealth of Australia* (Web Page, 3 April 2023) <https://www.agriculture.gov.au/biosecurity-trade/export/controlled-goods/meat/statistics>.

nature-based targets.[63] At COP15, a group of institutional investors announced the formation of Nature Action 100,[64] a new global engagement initiative mirroring the influential Climate Action 100 initiative. In June 2023, Nature Action 100 released a set of investor expectations of corporate actions that will protect and restore nature and ecosystems and mitigate financial risk, which will be sent to focus companies in eight key sectors.[65] Proxy advisors Glass Lewis and Institutional Shareholder Services have indicated that inadequate management and disclosure of material environmental issues could harm shareholder interests and constitute grounds to recommend voting against relevant board members.[66] These developments illustrate the prospect of shifting costs and availability of finance for companies with material nature-related impacts, and decreased consumer demand for their products and services. At the extreme, these developments could result in investor and consumer activism and even abandonment.

31. As noted above, recent research by the Swiss Finance Institute and the European Corporate Governance Institute suggests that companies' nature-related impacts are already "beginning to be priced by investors".[67] It concluded that "following the UN Biodiversity Conference (COP15), which raised awareness of biodiversity issues, firms with larger corporate biodiversity footprints lost value".[68] The authors suggest that "[t]his response is consistent with investors revising their valuation of these firms downward upon the prospect that regulations to preserve biodiversity will become more stringent".[69] This is illustrated by Australian Ethical Super's divestment of its position in Lendlease,

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[63] 'Our mission', *Finance for Biodiversity Foundation* (Web Page, 23 October 2023) <https://www.financeforbiodiversity.org/>.

[64] Nature Action 100, *At COP15, investors announce Nature Action 100 to tackle nature loss and biodiversity decline* (Statement, 11 December 2022). The group of launching investors consists of AXA Investment Managers, Columbia Threadneedle Investments, BNP Paribas Asset Management, Church Commissioners for England, Domini Impact Investments, Federated Hermes Limited, Karner Blue Capital, Robeco, Storebrand Asset Management, Christian Brothers Investment Services, and Vancity Investment Management.

[65] Nature Action 100, *Nature Action 100 releases investor expectations to support urgent corporate action on nature loss* (Statement, 26 June 2023).

[66] Glass Lewis, *2022 Policy Guidelines* (Report, November 2021) pages 26-27, 30-31; International Shareholder Services, *Sustainability Proxy Voting Guidelines: 2023 Policy Recommendations* (Report, 17 January 2023) page 10.

[67] Swiss Finance Institute and European Corporate Governance Institute, *Do Investors Care About Biodiversity?* (Finance Working Paper No. 905/2023, March 2023) page 7.

[68] Swiss Finance Institute and European Corporate Governance Institute, *Do Investors Care About Biodiversity?* (Finance Working Paper No. 905/2023, March 2023) Abstract.

[69] Swiss Finance Institute and European Corporate Governance Institute, *Do Investors Care About Biodiversity?* (Finance Working Paper No. 905/2023, March 2023) Abstract.

in March 2023, due to the potential impact on ecosystems of its new housing development in Mount Gilead, NSW.[70]

32. There has been litigation associated with nature-related impacts, both domestically and internationally. This has included challenges to individual projects due to their nature-related impacts, and shareholder class actions. For example, in November 2022, US investors in the wood pellet production company Enviva Incorporated commenced a shareholder class action against the company and two of its directors for allegedly misrepresenting the environmental sustainability of its wood pellets. The investors claim these misrepresentations contravened the *Securities Exchange Act 1934* (US) and caused them "significant losses and damages" due to a 13% share price drop allegedly related to the publication of information challenging the veracity of those representations.[71]

C. WHAT DOES THE DUTY REQUIRE?

33. It is not feasible to provide any guidance in this opinion on the circumstances of a particular director, company or sector. That is in part because, in determining whether a director has exercised reasonable care and diligence, it is necessary to consider a company's particular circumstances and the position and responsibilities of the director within the company. As Beach J has said:[72]

> *It is not in doubt that the circumstances of the particular company concerned inform the content of the duty. These include the size and type of the company, the size and nature of the business it carries on, the terms of its Constitution, and the composition of the board of directors.*
>
> *It is also not in doubt that in considering the acts or omissions of a particular director, one looks at factors including the director's position and responsibilities, the director's experience and skills, the terms and conditions on which he has undertaken to act as a director, how the responsibility for the company's business has been distributed between the directors and the company's employees, the informational flows and systems in place and the reporting systems and requirements within the company.*

34. However, at a general level, our opinion is that directors should be at least *identifying* the company's dependencies and impacts on nature, *considering* what potential risks this

[70] 'Why we divested from Lendlease', *Australian Ethical* (Media Release, 13 March 2023) <https://www.australianethical.com.au/insights/why-we-divested-from-lendlease/>.
[71] *D. Fagen v Enviva Inc & ors* (Class Action Complaint, United States District Court, District Court of Maryland, Case 8:22-cv-02844, 3 November 2022).
[72] *ASIC v Mariner Corporation Ltd* (2015) 241 FCR 502, 582 [440]-[441] (Beach J).

may pose to the company, and taking steps to ensure that nature-related risks and impacts are disclosed in accordance with the requirements discussed in Section C.2 below.

C.1 Identification and consideration of nature-related risks

35. The duty of care and diligence requires a director to obtain knowledge, sufficiently to place themselves in a position to guide and monitor the management of the company.[73] This has been described as a "core, irreducible requirement".[74] Directors must be familiar with the fundamentals of the business in which the company is engaged, and are under a continuing obligation to keep informed about its activities and "the effect that a changing economy may have on [its] business".[75]

36. In the context of nature-related risks, it would be prudent for directors at least to require management to identify the company's nature-related dependencies and impacts so that they may *consider* what potential risks this may pose to the company.

37. In doing so, we would caution against any assumption that nature-related impacts and financial interests are conceptually distinct. Further, "harm" is not confined to a company's immediate financial interests; it may also extend to *any* of the interests of the company.[76] Those interests include reputational risk and an interest in pursuing lawful activity.[77]

38. The TNFD has provided guidance on the identification and assessment of nature-related issues, known as the "LEAP" approach, which may be of assistance.[78] Sector-specific guidance on applying the TNFD framework and LEAP approach is already available for financial institutions,[79] with further sector-specific guidance due to be released in 2024.[80]

39. In some cases, the duty of care and diligence will require a director to go further than merely considering risks. Some further action may be required. Where directors consider that nature-related impacts and/or dependencies pose a foreseeable risk of harm to the

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[73] *Daniels v Anderson* (1995) 37 NSWLR 438, 495-505 (Clarke and Sheller JJA).
[74] *ASIC v Healey* (2011) 196 FCR 291, 298 [16] (Middleton J).
[75] *AWA Ltd v Daniels (t/a Deloitte Haskins & Sells)* (1992) 7 ACSR 759, 864 (Rogers CJ) at common law; see also *Trilogy Funds Management Ltd v Sullivan (No 2)* (2015) 331 ALR 185, 229 [203] (Wigney J).
[76] *ASIC v Cassimatis (No 8)* (2016) 336 ALR 209, 301 [480]-[482] (Edelman J); *Cassimatis v ASIC* (2020) 275 FCR 533, 640-641 [459] (Thawley J); *ASIC v GetSwift Ltd* [2021] FCA 1384, [2529] (Lee J).
[77] *ASIC v Cassimatis (No 8)* (2016) 336 ALR 209, 301 [482] (Edelman J); *Cassimatis v ASIC* (2020) 275 FCR 533, 640-641 [459] (Thawley J).
[78] TNFD, *Guidance on the identification and assessment of nature-related issues: The LEAP approach* (Report, September 2023).
[79] TNFD, *Sector guidance: Additional guidance for financial institutions* (Report, September 2023).
[80] TNFD Recommendations, page 73.

interests of the company, this does not necessarily require that the company cease any activities giving rise to that risk. As noted above, in determining whether a director has breached their duty of due care and diligence, a court will balance "the foreseeable risk of harm against the potential benefits that could reasonably have been expected to accrue to the company from the conduct in question".[81] This balancing exercise will involve consideration of factors such as the magnitude of the risk, the degree of probability of its occurrence, the expense, difficulty and inconvenience of taking alleviating action, and any other conflicting responsibility which the director may have.[82] In doing so, courts recognise that the management and direction of companies involves "taking decisions and embarking upon actions which may promise much, on the one hand, but which are, at the same time, fraught with risk on the other".[83] The duty of due care and diligence is not intended to "dampen business enterprise and penalise legitimate but unsuccessful entrepreneurial activity".[84]

40. Directors who conduct the balancing exercise themselves, and who act (or decline to act) based upon a rational and informed assessment of the company's best interests, will minimise the risk of being found to have failed to exercise due care and diligence. They may also have the protection of the "business judgment rule".[85] This statutory defence protects management decisions provided certain preconditions are satisfied. One precondition is that the director must have informed themselves about the subject matter of the judgment, to the extent they reasonably believe to be appropriate. Other preconditions are that a director: is acting in good faith and for a proper purpose; has no material personal interest in the subject matter of the judgment; and rationally believes "that the judgment is in the best interests of the corporation".[86]

41. If these preconditions are satisfied, then the director will be protected in respect of "any decision to take <u>or not take action</u> in respect of a matter relevant to the business operations of the corporation" (emphasis added).[87] The underlined words show that the defence is capable of protecting a decision to persist with a strategy despite a nature-related risk.

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81 *Vrisakis v ASIC* (1993) 9 WAR 395, 449-450 (Ipp J).
82 *Vrisakis v ASIC* (1993) 9 WAR 395, 449-450 (Ipp J); *ASIC v Rich* (2009) 236 FLR 1, 128-129 [7193] (Austin J).
83 *Vrisakis v ASIC* (1993) 9 WAR 395, 449 (Ipp J).
84 *Vrisakis v ASIC* (1993) 9 WAR 395, 449 (Ipp J).
85 A "business judgment" is "any decision to take or not take action in respect of a matter relevant to the business operations of the corporation": Act s 180(3).
86 Act s 180(2).
87 Act s 180(3).

However, the defence will not protect directors who are uninformed, who make no conscious decision, or who exercise no judgment.[88]

C.2 Disclosure of nature-related risks

42. Regardless of whether any action is taken, directors who identify nature-related dependencies or impacts should consider whether the company should be disclosing those dependencies and/or impacts in accordance with its periodic reporting and continuous disclosure obligations under the Act.

43. An aspect of the duty of care and diligence is that directors are required to be diligent and careful in their consideration of the resolution to approve the company's accounts and reports.[89] Further, directors are required to take all reasonable steps to comply with, or secure compliance with, a company's periodic reporting obligations under Pt 2M.3 of the Act.[90] This requires directors to at least inquire about any potential deficiency in the company's accounts and reports that they observe or ought to have observed by the exercise of reasonable care and diligence.[91]

44. It is sufficient for present purposes to note that:

    (a) The directors' report must, subject to certain exceptions, contain information that shareholders would reasonably require to make an informed assessment of the entity's operations, financial position, business strategies, and prospects for future financial years.[92] ASIC's *Regulatory Guide 247: Effective disclosure in an operating and financial review* (August 2019) states at RG 247.64 that the operating and financial review in directors' reports should "include a discussion of environmental, social and governance risks where those risks could affect the entity's achievement of its *financial* performance or outcomes disclosed, taking into account the nature and business of the entity and its business strategy" (emphasis in original).

    (b) ASX Listing Rule 4.10.3 requires companies to include a corporate governance statement within their annual report, disclosing the extent to which the company has followed recommendations set by the ASX Corporate Governance Council

[88] *ASIC v Rich* (2009) 236 FLR 1, 151 [7277] (Austin J).
[89] *ASIC v Healey* (2011) 196 FCR 291, 336 [188(a)] (Middleton J).
[90] Act s 344(1).
[91] *ASIC v Healey* (2011) 196 FCR 291, 336 [188(b)] (Middleton J).
[92] Act s 299A.

during the reporting period. Recommendation 7.4 in the ASX Corporate Governance Council's *Corporate Governance Principles and Recommendations (Fourth Edition)* (February 2019) states that "[a] listed entity should disclose whether it has any material exposure to environmental or social risks and, if it does, how it manages or intends to manage those risks". It defines "environmental risks" as:

> *[T]he potential negative consequences (including systemic risks and the risk of consequential regulatory responses) to a listed entity if its activities adversely affect the natural environment or if its activities are adversely affected by changes in the natural environment. This includes the risks associated with the entity polluting or degrading the environment, adding to the carbon levels in the atmosphere, or threatening a region's biodiversity or cultural heritage. It also includes the risks for the entity associated with climate change, reduced air quality and water scarcity.*

(c) Companies' continuous disclosure obligations require them to notify the ASX of information that is not generally available if a "reasonable person would expect the information, if it were generally available, to have a material effect on the price or value" of the company's securities, and provisions of the ASX Listing Rules require disclosure of that information.[93] ASX Listing Rule 3.1 requires companies to immediately disclose information to the ASX if they are or become aware of any information that a "reasonable person would expect to have a material effect on the price or value of the entity's securities", subject to the exceptions in Rule 3.1A. A reasonable person would be taken to expect information to have a material effect on a company's securities if the information "would, or would be likely to, influence persons who commonly invest in securities in deciding whether to acquire or dispose" of the company's securities.[94]

45. The wording of RG 247.64, Recommendation 7.4, and ASX Listing Rule 3.1 extend to material risks that arise due to a company's nature-related dependencies and impacts.

46. Australian companies are not ordinarily required to disclose nature-related impacts if they do *not* pose a material risk of harm to the company. However, there are two key exceptions.

[93] Act s 674.
[94] Act s 677(1).

47. First, if information about a company's nature-related impacts "would, or would be likely to, influence persons who commonly invest in securities in deciding whether to acquire or dispose" of the company's securities,[95] a company's continuous disclosure obligations may require the disclosure of that information even where the relevant impacts do *not* pose a material risk of harm to the company. The reference in s 677 to "persons who commonly invest in securities" requires contemplation of a hypothetical investor who commonly buys securities in general rather than securities of a kind or class to which the company belongs.[96] As noted above, there is evidence to suggest that information about nature-related impacts is already influencing persons who commonly invest in securities in deciding whether to acquire or dispose of companies' securities. Some companies may therefore *already* be required to disclose information about nature-related impacts in accordance with their continuous disclosure obligations.

48. Second, the European Union's CSRD will require covered entities to disclose nature-related impacts regardless of their materiality to the entity.[97] Australian companies may be subject to these requirements where particular conditions are met, such as having listed securities on a regulated market in the European Union.[98] It has been reported that approximately 600 Australian companies may meet these conditions.[99]

49. A contravention of these requirements does not automatically constitute a breach of a director's duty under s 180(1) of the Act. However, liability under s 180(1) may be triggered where a director's failure to exercise reasonable care and diligence has caused or allowed the company to contravene disclosure requirements, at least where it was reasonably foreseeable that such contravention might harm the company's interests.[100]

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[95] Act s 677(1). A different but related obligation potentially applies under s 1013DA in the context of financial products and financial product disclosure, at least for those involved in producing such statements, and whether directly or in the context of supply chain disclosure.

[96] *Grant-Taylor v Babcock & Brown Ltd (in liq)* (2015) 322 ALR 723, 738-739 [68]-[72] (Perram J) cf. *Riley v Jubilee Mines NL* (2006) 59 ACSR 252, 268 [63] (Sanderson M), referred to in *Jubilee Mines NL v Riley* (2009) 40 WAR 299, 328 [121]-[122] (Martin CJ) without approval or disapproval.

[97] EU Directive, arts 19a(1) and 29a(1).

[98] EU Directive, preamble paragraph 19, art 40a.

[99] Dieter Holger, 'At Least 10,000 Foreign Companies to Be Hit by EU Sustainability Rules', *Wall Street Journal* (News Article, 5 April 2023) <https://www.wsj.com/articles/at-least-10-000-foreign-companies-to-be-hit-by-eu-sustainability-rules-307a1406#:~:text=At%20least%2010%2C000%20companies%20based,to%20the%20coming%20EU%20rules.>.

[100] *ASIC v GetSwift Ltd* [2021] FCA 1384, [2538] (Lee J), citing *ASIC v Vocation Ltd (in liq)* (2019) 371 ALR 155, 330 [730] (Nicholas J).

D. CONCLUSION

37. "Nature-related risk" is a broad label. Its breadth gives rise to practical difficulties in identifying and grappling with the specific threats of harm. But the breadth of the definition should not obscure the potential significance of nature-related risks for many companies. There is little doubt nature-related risks will be acute alongside climate-related risks. The TNFD has emphasised that "nature" is a core and strategic risk management issue, which needs "to be brought into the strategy, risk management and capital allocation decisions of business and finance, with fully integrated climate and nature considerations."[101] In turn, the TNFD has provided an apt framework for nature-related risk and opportunity management and disclosure.

38. Directors can take practical steps to identify and manage any nature-related risks. Directors should cause management to put them into a position to consider the materiality of such risks, take advice on how they should be managed and disclosed, and protect themselves from personal risk and liability by informing themselves and taking action appropriately so as to engage available defences.

24 October 2023

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Zoe Bush

[101] TNFD Recommendations, page 8.