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Implementation guidance for the materiality assessment

Disclaimer

This implementation guidance is non-authoritative and accompanies ESRS but does not form part of it. This means that if anything in this guidance appears to contradict any requirement or explanation in ESRS, ESRS takes precedence. This implementation guidance is issued following EFRAG's due process for such non-authoritative documents and under the sole responsibility of EFRAG.



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Summary in 12 key points

1. The materiality assessment is the process by which the undertaking determines material information on sustainability impacts, risks and opportunities. This is achieved by the determination of material matters and material information to be reported ~~on~~ in ~~the~~ the undertaking's sustainability statement. The performance of ~~an~~ a materiality assessment based on objective ~~materiality assessment criteria~~ is pivotal to sustainability reporting which shall include relevant and faithful information about all impacts, risks and opportunities (IROs) across environmental, social and governance matters determined to be material from the impact materiality perspective or the financial materiality perspective or both.
2. The assessment ~~is not limited to~~ covers the undertaking's ~~own operations as entire value chain, i.e.,~~ it ~~also includes~~ the undertaking's upstream and downstream value chain~~-, in addition to its own operations.~~
3. Once an impact, risk or opportunity ~~have~~ related to a sustainability matter has been identified as material, the undertaking (a) refers to the requirements in the related ESRS to identify the relevant information to be considered for disclosure on the matter or (b), when the impact, risk or opportunity is not covered or insufficiently covered by the ESRS, shall ~~design~~ provide a relevant entity-specific disclosure. Relevance is the ~~entire~~ criteria ~~criteria~~ to support the identification of the information to be disclosed. Relevance is based on (a) the significance of the information in relation to the matter it depicts or (b) its decision-usefulness.
4. The determination of the information to be reported depends on whether the information relates to (a) policies, actions and targets; or (b) metrics. For policies, actions and targets, information shall be disclosed according to the Disclosure Requirements, or it shall be stated that the undertaking does not have policies, actions and/or targets. ~~For metrics, it is possible to omit them when they~~ Metrics are subject to materiality assessment whereby these are omitted if assessed as not material ~~based on the materiality assessment~~. Such an omission is in itself useful sustainability-related information. Omitting datapoints derived from EU legislation based on materiality requires stating explicitly that they are not material. ESRS 2 Disclosure Requirements which address cross-cutting matters are to be reported ~~on~~ in all cases (irrespective of the outcome of the materiality assessment).
5. ~~The ESRS do not mandate a specific process or sequence of steps to follow when performing the materiality assessment process shall be designed to identify all material impacts, risks and opportunities and consequently also, as this is left to exclude those that are not material. At the judgement of the undertaking which has to define the process that better reflects its facts and circumstances:~~
- 5.6. As an illustration, a materiality assessment that would meet the requirements of ESRS could include the following steps:
 - a. ~~a~~ understanding the context and definition of the stakeholder engagement strategy;
 - b. ~~identification of the list of~~ actual and potential material impacts, risks and opportunities related to sustainability matters and impacts, risks and opportunities; and
 - c. assessment and determination of the ~~final list of material matters based on an assessment of the materiality of the impacts, risks and opportunities—~~ related to sustainability matters; and
 - d. ~~Following the performance of~~ reporting.
6. ~~Engagement with affected stakeholders informs the materiality assessment process, and it is consistent with the practice suggested by the undertaking shall disclose:~~
 - a. ~~international instruments of due diligence that are referenced in the process to identify and assess its material impacts risks and opportunities (ESRS 2 IRO-1),~~
 - b. ~~the interaction of impacts, risks and opportunities with its strategy and business model (ESRS 2 SBM-3), and~~
 - c. ~~the Disclosure Requirements in ESRS covered by its sustainability statement (ESRS 2 IRO-2).~~
- 6.7. ~~Stakeholder engagement CSRD. This entails seeking input and feedback to understand the concerns and the evidence of about actual and potential impacts of the undertaking on people and the environment and it. It also helps to substantiate the importance of the sustainability matters from the lenses perspectives of the affected stakeholder groups. Equally, ESRS do not mandate specific behaviour on stakeholder engagement and do not pre-empt the content of the CSDDD currently being defined in the EU legislative process.~~
- 7.8. To assess the materiality of impacts ~~for reporting purposes,~~ the undertaking, assesses them against criteria of severity and likelihood and sets appropriate quantitative and/or qualitative thresholds ~~based on severity for actual negative impacts and severity and likelihood for potential negative impacts are used for reporting purposes.~~

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Severity is based on the scale, scope and irremediable character of negative impacts and the scale and scope of positive impacts.

~~8.9.~~ Material risks and opportunities for the undertaking generally derive either from impacts or from dependencies. To assess their materiality, appropriate quantitative and/or qualitative thresholds based upon anticipated financial effects in terms of performance, financial situation, cash flows, access to finance and cost of capital are used.~

~~10.~~ An assessment performed under GRI constitutes a good basis for the assessment of impacts under ESRS. The due diligence process, as defined in the related international instruments, can help an undertaking both (a) to identify and assess its actual and potential negative impacts, as well as (b) to assess their materiality for reporting purposes based on the criteria of severity and likelihood.

~~9.11.~~ Reflecting the equivalence of the scope of financial materiality in ISSB standards and ESRS, an undertaking that applies ESRS is expected to be able to comply with the identification of the risks and opportunities to be disclosed under IFRS. The due diligence process, as defined in the international instruments, can help an undertaking both (a) to identify and assess its potential and actual negative impacts, as well as (b) to assess their materiality for reporting purposes based on the criteria of severity and likelihood. sustainability related information on risks and opportunities under IFRS.

12. Following the performance of the materiality assessment process, the undertaking shall disclose:

- a. the process to identify and assess its material impacts risks and opportunities (ESRS 2 IRO1),
- b. the interaction of impacts, risks and opportunities with its strategy and business model (ESRS 2 SBM-3), and
- c. the Disclosure Requirements under ESRS covered by its sustainability statement (ESRS 2 IRO2).



1 ~~Objective~~ Introduction

~~13.~~ The objective of this non-authoritative guidance is to support the implementation activities of preparers and others using or analysing ESRS reports with regard to the double materiality assessment (referred to as “materiality assessment” in this document). Hence, this guidance does not introduce new provisions to the ESRS, as these can only result from future standard setting activities (e.g., future possible amendments to draft ESRS) conducted in accordance with the EFRAG due process. When content of this guidance is seen to contradict the requirements in ESRS, those requirements prevail.

~~10.~~~~14.~~ The content of this document has been developed by EFRAG on the basis of the July 2023 Delegated Act on ESRS adopted in accordance with the requirements of Articles 19a or 29a of the Directive 2013/34/EU (referred to as the “Accounting Directive”) as amended following the Corporate Sustainability Reporting Directive (referred to as “the CSRD”).

~~11.~~ The content of this document has been developed on the basis of the July 2023 Delegated Act on ESRS.

~~12.~~ In its implementation support function, EFRAG cannot develop concepts and reporting requirements that go beyond the content of the July 2023 Delegated Act. The purpose of the implementation support material is to illustrate how the provisions of the delegated act may be implemented without introducing new provisions. New provisions can read as illustrative only result from future standard setting activities (e.g., future amendments to draft ESRS) in accordance with the EFRAG due process.

~~11.~~~~15.~~ As an illustration, when the implementation support documents point to, When this guidance describes a specific approach or methodology that is not detailed in the Delegated Act, this has to be framed as one of the possible implementation other alternative approaches without excluding other possibilities, compliant with the Delegated Act are also possible.

~~12.~~~~16.~~ This guidance includes FAQs on interoperability with ISSB and GRI Universal Standards, illustrating the interactions of the corresponding materiality concepts and assessment processes when applicable.

~~13.~~~~17.~~ This guidance also includes FAQs related to international instruments or reporting standards that will be useful to perform the materiality assessment and that are referenced in the CSRD. In the case of due diligence these are the *Guiding Principles on Business and Human Rights* issued by the United Nations and *OECD Guidelines for multinational enterprises* and *OECD Due diligence guidance for responsible business conduct* which have been used as a basis for the preparation of this document.

~~14.~~~~18.~~ Finally, this guidance acknowledges that market practice is currently developing for double materiality assessment and that there is no single solution for all undertakings in terms of designing processes and adopting methodologies. Hence, this guidance is aimed at providing tools and mechanisms for undertakings to apply the materiality assessment requirements and disclosures set out in ESRS ~~1 and 2~~ while taking full account of their specific facts and circumstances, including their business model, strategy, structure, complexity, governance and other contextual information.

~~15.~~~~19.~~ This ~~paper~~ Guidance is organised as follows:

- a. ~~chapter 2 explains what double~~ the ESRS approach to materiality is;
- a. ~~chapter 3 explains the need for the materiality assessment;~~
- b. ~~chapter 4 explains~~ illustrates how the materiality assessment is performed;
- c. ~~chapter 54~~ explains how undertakings could leverage from take account of other frameworks/standards or sources; and
- d. ~~chapter 65~~ complements chapter 2 to 54 with FAQs on:
 - i. ~~i.~~ —impact materiality;
 - ii. ~~ii.~~ —financial materiality;
 - iii. ~~iii.~~ —the materiality assessment process;
 - iv. ~~iv.~~ —stakeholder engagement;
 - v. aggregation / disaggregation; and

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vi. reporting.

~~16.~~20. Acronyms used in this document are:

- a. CSRD – Corporate Sustainability Reporting Directive;
- b. ESRS – European Sustainability Reporting Standards;
- ~~b.c.~~ CSDD – Corporate Sustainability Due Diligence Directive;
- ~~c.d.~~ GHG – ~~greenhouse gases or the GHG protocol,~~ – Greenhouse gases protocol;
- ~~d.e.~~ GRI – Global Reporting Initiative; ~~and~~
- ~~b.~~ IROs – ~~impacts, risks and opportunities,~~ and
- e.f. ISSB – International Sustainability Standards Board.

2 The ESRS approach to materiality

- 21. ESRS require that the sustainability statement include sustainability information related to material impacts, risks and opportunities identified through a materiality assessment process that applies the principles of double materiality.
- 22. Double materiality has two dimensions: impact materiality (covering material information about the undertaking's impacts on sustainability matters) and financial materiality (covering material information about risks and opportunities for the undertaking resulting from sustainability matters). The terms "material" and "materiality" are used throughout ESRS to refer to double materiality, unless specified otherwise.
- 23. The materiality assessment serves to identify the material information to be included in the sustainability statement. During the materiality assessment process, the undertaking shall identify all material impacts, risks and opportunities across the environmental, social and governance topics in their own operations as well as in upstream and downstream value chain, and consequently also exclude those topics that are not material. If the process is not appropriately designed, it may expose the undertaking to incomplete reporting (i.e., material impacts, risks or opportunities not being disclosed). This process is the starting point to determine the material information to be disclosed in the sustainability statement on these material impacts, risks and opportunities.
- 24. If, for management purposes, the undertaking identifies a large number of impacts, risks and opportunities, it may prioritise them over time in a certain order. However, for reporting purposes this prioritisation should not result in material impacts, risks and opportunities being excluded, in particular when they are not addressed or fully addressed by the undertaking through policies, targets and action plans. This is because the undertaking shall report on all its material impacts, risks and opportunities irrespective of whether actions have been undertaken or are planned to address them.

The materiality assessment should be based upon supportable evidence and rely to the maximum extent possible on objective information.

- 25. ~~What is~~ **double** ~~it shall reflect the~~ **double** implementation of the impact materiality and financial materiality criteria specified in the ESRS (ESRS 1 chapters 3.4 and 3.5).

- ~~17.~~26. The ESRS require undertakings to disclose the materiality assessment [?] process and its outcome. This includes the following information with respect to the process: methodologies and assumptions applied, the focus and extent of the process, inputs, and where certain judgements have been made by the undertaking and the use of thresholds (ESRS 2 - IRO 1).
- 27. For the sustainability statement to meet the required characteristics of quality (Appendix B of ESRS 1), the process, the way the criteria (ESRS 1 chapters 3.4 and 3.5) are applied, the thresholds and the conclusions of the materiality assessment should be consistent with internal and other external reporting, business operations and sustainability management policies and actions, including those that are put in place to fulfil obligations related to sustainability related laws and regulations.
- 28. The undertaking is not required to report on all matters described in the topical ESRS, but only on those that are material.

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29. The undertaking may briefly explain the conclusions of its materiality assessment in relation to the omitted topic or topics. The undertaking shall provide explanations if it concludes that it has no material impacts, risks and opportunities with respect to climate change and therefore omits Disclosure Requirements in ESRS E1 Climate Change. The undertaking shall also report on material matters that are not covered or are covered insufficiently in the topical ESRS, according to the requirement provided in the ESRS 1 for entity-specific information.
30. Once the undertaking has identified the material matters to be reported on, it assesses the materiality of the information to determine the information to be reported on each material matter (ESRS 1 paragraphs 30, 31, 33 and 34)¹. The concept of materiality of information is a step that follows the materiality assessment that leads to the identification of material matters to be reported on and is applied to the information to be disclosed at a more granular level, i.e., at Disclosure Requirement or datapoint level.

2.1 ~~Recap on~~ Implementing the concept of double materiality

~~18.31.~~ The CSRD establishes that sustainability reporting shall be based on the principle of double materiality (referred to in this document as “materiality”). This means that a reporting undertaking shall consider both ~~There are two dimensions to double materiality:~~ impact materiality and financial materiality when identifying the material matters, which is the basis for the determination of the material information to be disclosed. ~~ESRS include a definition of these two materiality dimensions, “a sustainability matter is can be material from”: an impact perspective or from a financial perspective or from both (see ESRS 1 chapter 3).~~

~~32.~~ ESRS include a definition of these two materiality dimensions, “a sustainability matter is material from”:

- a. “An impact perspective when it pertains to the undertaking’s material actual or potential, positive or negative impacts on people or the environment over the short-, medium- and long-term. Impacts include those connected with the undertaking’s own operations and upstream and downstream value chain, including through its products and services, as well as through its business relationships.” (ESRS 1 paragraph 43); and
- b. “a financial perspective if it triggers or could reasonably be expected to trigger material financial effects on the undertaking. This is the case when a sustainability matter generates ~~or may generate~~ risks or opportunities that have a material influence, or could reasonably be expected to have a material influence, on the undertaking’s development, financial position, financial performance, cash flows, access to finance or cost of capital over the short-, medium- or long-term.” (ESRS 1 paragraph 49). “The financial materiality assessment corresponds to the identification of information that is considered material for primary users of general-purpose financial reports in making decisions relating to providing resources to the entity. In particular, information is considered material for primary users of general-purpose financial reports if omitting, misstating or obscuring that information could reasonably be expected to influence decisions that they make on the basis of the undertaking’s sustainability statement” (ESRS 1 paragraph 48). In this document the terms “risks and opportunities” are used to identify the financial risks and opportunities that are in the scope of financial materiality.

~~20.~~ A sustainability matter can be material from an impact perspective or from a financial perspective or from both (see ESRS 1 chapter 3).

~~19.33.~~ Impact materiality and financial materiality are often intertwined. The ~~undertaking has or could have~~ undertaking’s impacts on people or the environment ~~which vary, as well as changes to strategy, including investments, and management decisions made to address such impacts,~~ often give rise to risks and opportunities ~~resulting from~~ for the impacts themselves and/or from modifications to its strategy, business model(s) and operational processes which are or will be introduced to manage the impacts. ~~undertaking.~~

¹ The undertaking may also refer to the flowchart in ESRS 1 appendix E for an illustration of this step.

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Figure 1: Impact and financial materiality

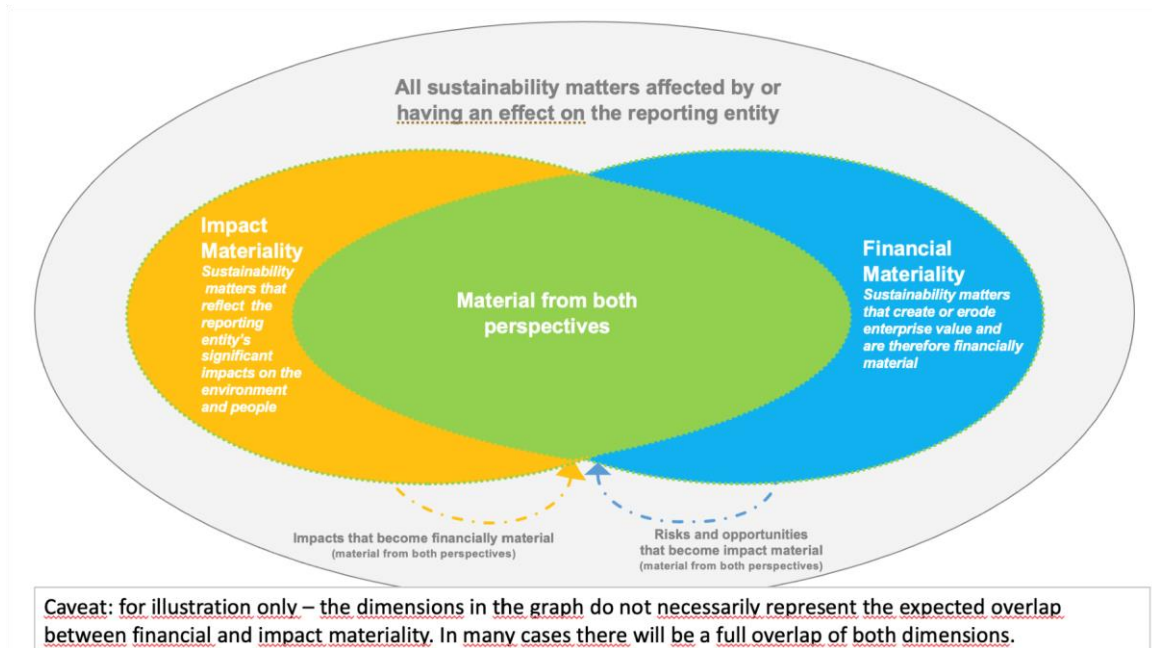
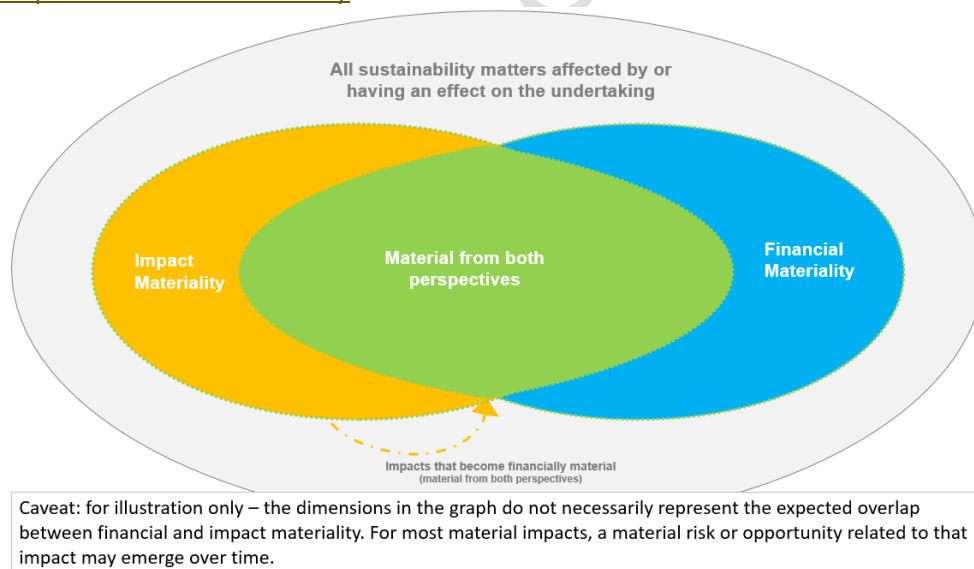


Figure 1: Impact and financial materiality



20.34. For most material impacts, a material risk or opportunity related to that impact may crystallise with the passage of time. For example:

- a. an oil and gas undertaking identifies a material negative impact that arises from not performing the consultation or reaching an agreement with indigenous' people to use their land for the extractions and to relocate the community. Such At the reporting date, the undertaking does not expect that the indigenous community will initiate protests. However, such indigenous community may at a later stage initiate protests that could halt the production of oil and gas at that site and cause material costs for the undertaking due to the days lost to production or the abortion of the project; and
- b. an undertaking has a number of cases of gender discrimination when promoting employees during the current reporting year; At the reporting date, the undertaking does not expect that the employees pursue legal proceedings. However, such group of employees can, individually or as a whole, pursue/pursues at a later stage legal proceedings on the grounds of gender discrimination and seek financial compensation within the medium-term and causing cause reputational damage to the undertaking.

21.35. Beyond risks and opportunities deriving from impacts, material risks and opportunities also arise in the absence of material impacts connected to the undertaking, in particular when they are due to dependencies on the availability of natural and human resources. For example:

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- a. ~~an undertaking is active in the mining sector is dependent on~~ organic agriculture which has dependencies on water and pollinators. The number of pollinators is decreasing due to climate change, hence, water shortages may impact pesticide use by other agricultural entities in its capacity vicinity;
- ~~a-b.~~ an undertaking that has a factory that is running on renewable energy and, thus, does not produce GHG emissions, is in a location subject to generate revenue and increase the risk of becoming a stranded asset due to coastal erosion and could be exposed to climate-related physical risks such as flooding or extreme weather;
- ~~b-c.~~ an undertaking dependent on human resources may experience a high level of staff turnover caused by a local competitor hiring employees at a higher salary, despite the two undertakings having adequate working conditions and practices (i.e., not driven by a material impact) and therefore its operations may be dependent on the availability of human resources; and

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- a. ² an undertaking that has a factory located in a site subject to coastal erosion is exposed to climate physical risk.

2.2 The materiality assessment

21. The undertaking is not required to report on all topics described in the topical ESRS, but only on those that are material. Consequently, the undertaking shall perform a materiality assessment to determine which topics are material and which are not.
22. The materiality assessment is therefore the process organised by the undertaking to identify all material impacts, risks and opportunities across environmental, social and governance topics. It is the starting point to determine the material information to be disclosed in the sustainability statement on these material impacts, risks and opportunities.
23. The materiality assessment shall be designed to identify all material impacts, risks and opportunities and consequently also to exclude those that are not material. If the process is not appropriately designed, it may expose the undertaking to incomplete reporting (i.e., material impacts, risks or opportunities not being disclosed). For example, an undertaking may not have identified a material impact on child labour from its first tier supplier as workers from its value chain were not considered in its materiality assessment.
- ~~22.1.~~ Once the undertaking has identified the material matters to be reported on, it assesses the materiality of the information, to determine the information to be reported on each material matters (ESRS 1 paragraphs 30, ³, 33 and 34)⁴.
- d. ~~The materiality assessment should be based upon supportable evidence and rely to the maximum extent possible on objective information. It shall reflect sustainability-related regulatory developments that address systemic risks may affect the implementation prospects of the impact undertaking's business.~~

². For the sustainability statement to meet the required characteristics of quality (Appendix B of ESRS 1), the process, the way the criteria (ESRS 1 chapters 3.4 and 3.5) are applied, the thresholds and the conclusions of the materiality assessment should be consistent with content and evidences of internal and external reporting, business operations and sustainability management policies and actions, including those that are put in place to fulfil obligations related to sustainability related laws and regulations.

³. If the undertaking identifies a large number of impacts, risks and opportunities, it may prioritise them over time in a certain order for management purposes. However, for reporting purposes this prioritisation should not result in material impacts, risks and opportunities being excluded; in particular, when they are not addressed or fully addressed by the undertaking through policies, targets and action plans. This is because the undertaking is expected to report on all its material impacts, irrespective of whether actions have been undertaken or are planned to address them.

⁴The undertaking may also refer to the flowchart in ESRS 1 appendix E for an illustration of this step.

~~23.36.~~ Impact materiality and financial materiality criteria (ESRS 1 chapters 3.4 are two different concepts, however as illustrated above they are inter-related and 3.5) and it shall leverage the interconnections between them shall be considered. The undertaking is expected to exercise its judgement in organizing its materiality assessment, including on appropriate thresholds, whether the two processes should be separate or should have common steps, however there is merit in maximizing procedural synergies between the two to avoid gaps.

2.3-2 Understanding key concepts for the materiality assessment: matters; topics; and impacts, risks and opportunities

~~24.37.~~ Sustainability matters are defined in the delegated act glossary as environmental, social and human rights, and governance factors, including sustainability factors defined in Article 2, point (24), of Regulation (EU) 2019/2088 (i.e., SFDR).

~~25.38.~~ The level of granularity of the matters to be considered ranges from topic level (for example, own workforce) to sub-topic level (for example, working conditions) and, in some cases, to sub-sub-topic level (for example, health and safety). As described in ESRS 1 paragraph 8, the three levels of granularity are collectively called sustainability matters (please see ESRS 1 paragraph AR 16 for a full list of topics, sub-topics and sub-sub-topics). In particular:

- a. the goal of the materiality assessment is to identify the material impacts, risks and opportunities related to matters that are to be reported (ESRS 2 SBM 3);
- ~~a. the matter is assessed to be material when material impacts and/or material financial effects due to risks and opportunities relate to a matter, and hence that arise from the matter becomes material for the undertaking~~
- b. are identified (ESRS 1 paragraph 43 and 49); and
- c. for each material matter, the undertaking determines the information to be reported in accordance with the cross-cutting or topical standards (ESRS 1 paragraph 30). ~~Figure 2: Sustainability matters, topics, sub-topics and impacts, risks and opportunities~~

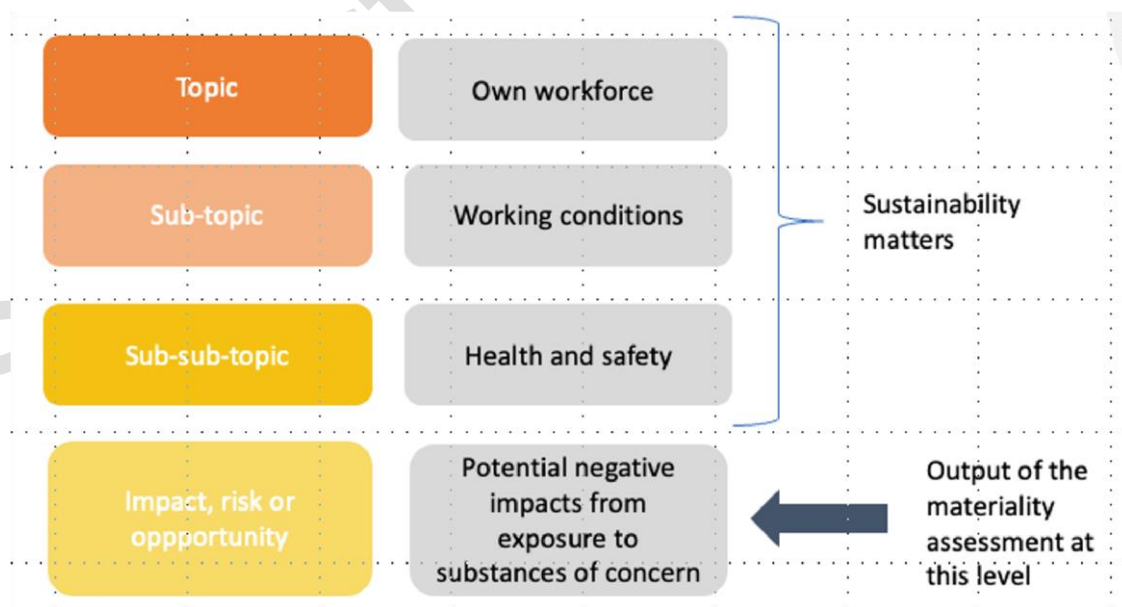
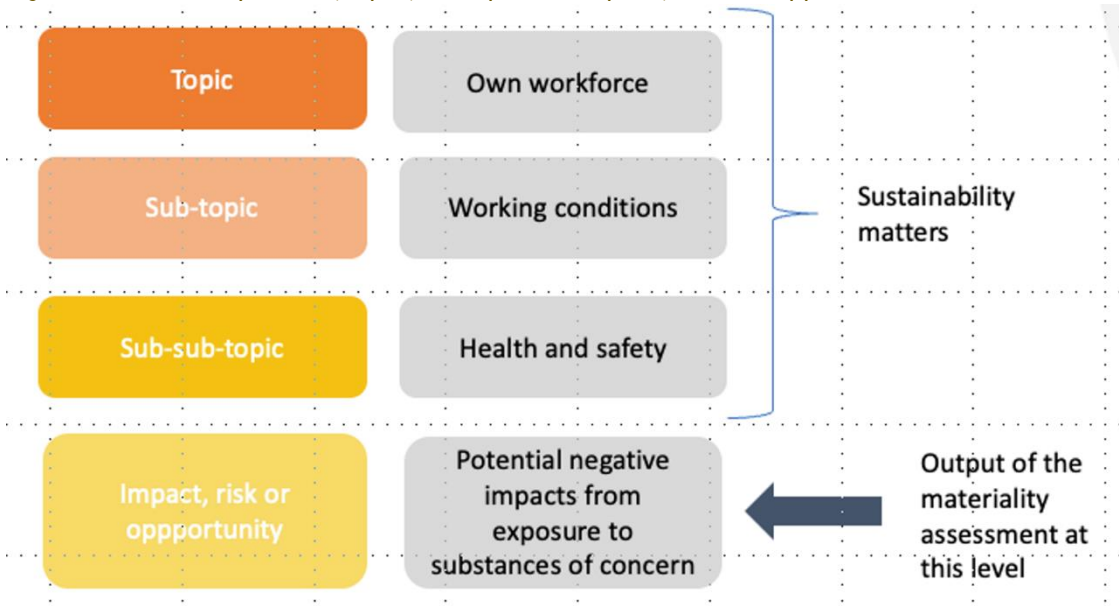


Figure 2: Sustainability matters, topics, sub-topics and impacts, risks and opportunities



~~26.39.~~ The outcome of the materiality assessment is disclosed according to ESRS 2 SBM-3 *Material impacts, risks and opportunities and their interaction with strategy and business model*. The objective of ESRS 2 SBM-3 is to set requirements for the undertaking to disclose its material impacts, risks and opportunities identified at topic, sub-topic or sub-sub-topic level.

~~27.40.~~ The undertaking shall disclose its material impacts, risks and opportunities, which are in turn mapped to sustainability matters (i.e., topics, sub-topics or sub-sub-topics). In preparing its disclosure according to ESRS 2 SBM-3, as per any other disclosure, the undertaking may aggregate information to the extent that it does not obscure material content (ESRS 1 chapter 3.7).

~~28.41.~~ Given that ~~the~~ double materiality considers both impact materiality and financial materiality, the undertaking needs to identify whether a topic, sub-topic or sub-sub-topic is material from any of the two perspectives, or both.

~~29.42.~~ Once a matter has been identified as material, the undertaking refers to the requirements in the respective topical ESRS to identify the information to be disclosed on the matter (ESRS 1 paragraph 30 and 31). For example, health and safety could be material from a negative/positive impact, and/or risk, and/or opportunity perspective. If an undertaking concludes that health and safety of its own workforce is material ~~(because the undertaking is exposed to a material impact, risk or opportunity in relation to that sub-sub-topic)~~, due to the employees' exposure to harmful chemical substances, it shall provide information related to this sustainability matter following the requirements in Disclosure Requirements S1-1 *Policies*, S1-4 *Taking action*, S1-5 *Targets*, and S1-14 *Health and Safety metrics*. Similarly, if an undertaking concludes that pollution of water is material, it shall provide information related to this sustainability matter following the requirements of Disclosure Requirements E2-1 *Policies*, E2-2 *Actions and resources*, E2-3 *Targets*, ~~and~~ E2-4 *Pollution of air, water and soil* ~~and~~ E2-6 *Anticipated financial effects from material polluted-related risks and opportunities*.

~~30.43.~~ In addition, there could be situations where a sustainability matter is identified as material but is not covered by an ESRS (~~refer to~~ see ESRS 1 paragraph AR 16 for a full list of matters) or is not covered with sufficient granularity. In such ~~situations~~ situations, as per ESRS 1 paragraph 11, the undertaking shall disclose additional entity-specific disclosures.

2.3 ~~Materiality assessment – why is it needed?~~

~~39.~~ ~~The materiality assessment in sustainability reporting serves to identify all material impacts, risks and opportunities of the undertaking related to a topic, sub-topic or sub-sub-topic (see ESRS 1 paragraph 25-30), and subsequently, the material information (see ESRS 1 paragraphs 31-36) to be disclosed.~~

~~40. Such assessment is not limited to the undertaking's own operations as it also includes its upstream and downstream value chain (see ESRS 1 paragraph 63).~~

~~3.1 Identification of all material impacts, risks and opportunities of the undertaking~~

~~41. The materiality assessment is the process to identify all material impacts, risks and opportunities across environmental, social and governance matters for disclosure purposes (see chapter 4 *Materiality assessment – how is it performed?*). Accordingly, the materiality assessment should be designed to identify all material impacts, risks or opportunities and also to exclude those that are not material. In other words, the undertaking is not to disclose all matters of the sector-agnostic or sector-specific standards but only those material to them including entity-specific matters.~~

~~42. Once the undertaking has identified its material impacts, risks and opportunities and the sustainability matters associated with them, it shall assess the materiality of information of the related Disclosure Requirements and their datapoints to determine what to include in its sustainability statement (see chapter 3.2 *Identification of material information*).~~

~~43. The ESRS also include a requirement to disclose the materiality assessment process. This is ESRS 2 IRO 1 – *Description of the processes to identify and assess material impacts, risks and opportunities*, whereby the undertaking describes the materiality assessment process put in~~

~~place to identify the information to report on. This disclosure provides transparency on the materiality assessment performed, including judgements made by the undertaking throughout the process (for example, on the use of thresholds to assess materiality).~~

~~44. The outcome of the materiality assessment process is also to be disclosed according to the provisions set in ESRS SBM 3 *Material impacts, risks and opportunities and their interaction with strategy and business model* and ESRS 2 IRO 2 *Disclosure Requirements in ESRS covered by the undertaking's sustainability statement*. This Disclosure Requirement provides an understanding of the Disclosure Requirements included in the sustainability statement, which indirectly allows to identify the topics that have been excluded as not material. It also provides the conclusion of the materiality assessment for datapoints derived from EU law (Appendix B of ESRS 2) and additional explanations when climate change is assessed to be not material.~~

~~45. When the undertaking concludes that a topic is not material, it omits the disclosures required by the corresponding topical ESRS. It may briefly explain the conclusions of its materiality assessment in relation to the omitted topic or topics. However, specific disclosures are to be included in relation to ESRS E1 *Climate Change* when the undertaking concludes that this topic is immaterial and, therefore, it omits all its Disclosure Requirements. According to ESRS 2 IRO 2 Paragraph 57-58, the undertaking shall disclose a detailed explanation of the conclusions of its materiality assessment for ESRS E1 *Climate Change*, including a forward-looking analysis of the conditions that could lead the undertaking to conclude that climate change is material in the future (ESRS 1 paragraph 32).~~

3.2 Criteria for the identification of material information

~~31.44. The concept of Assessing the materiality of information is complementary to a step that follows the materiality assessment that leads leading to the identification of material matters to be reported on (see chapters 2 *What is the double materiality assessment?* and 3.1 *Identification of all material impacts, risks and opportunities of the undertaking*) chapter 3 *Materiality assessment- how is it performed?* and it is applied at the more granular level of Disclosure Requirements or datapoints. ESRS 1 paragraphs 31, 33-35 set requirements on how to assess materiality of information.~~

~~32.45. The criteria to assess the materiality of information are based on relevance as described in ESRS 1 paragraph 31: (a) the significance of the information in relation to the matter it depicts or (b) its decision-usefulness. This is decision-usefulness for the primary users of ~~general purpose~~ general-purpose financial~~

information (i.e., financial materiality ~~focused~~focused) and/or for those users whose interest is on the undertaking's ~~impact~~impacts (i.e., impact materiality). In practice, information that is material under ~~the~~ perspective (b) (decision-usefulness) is in many – if not most - cases also material under ~~the~~ perspective (a) (significance). However, there could be cases where a piece of information is significant to depict the impacts of the undertaking on people or the environment, without necessarily being an input for the ~~user~~users of the sustainability statement in its decision-making, ~~as the ultimate beneficiary is not a user of the sustainability statement.~~ When a matter is material from both an impact and a financial perspective, the information needs of the two groups of users (investors and others) is or can be the same in practice. In other cases, ~~this~~the information may differ: (refer to FAQ 21).

~~33.46.~~ 33.46. These criteria support the identification of the information to be reported, ~~in~~ In addition to, the ~~general requirement~~undertaking needs to apply the general requirements on fundamental qualitative characteristics of information (relevance and faithful representation) and the enhancing qualitative characteristics of information (comparability, verifiability and understandability) ~~(see), refer to~~ ESRS 1 Appendix B).

~~34.47.~~ 34.47. ESRS 2 IRO 2 requires an explanation of how the undertaking has determined the material information to be disclosed in relation to the impacts, risks and opportunities that it has assessed to be material, including the use of thresholds and/or how it has implemented the criteria in ESRS 1 chapter 3.2 *Material matters and materiality of information.*

~~3.3~~ 2.4 Scope of application of the materiality of information

~~35.48.~~ 35.48. The following paragraphs illustrate how the undertaking shall apply the filter of materiality of information (see ESRS 1 paragraphs 31, 33-35) when disclosing the information on material sustainability matters.

~~36.49.~~ 36.49. The determination of the information to be reported for policies, actions and targets in relation to a material matter is ~~expected to follow~~set out in the list of Minimum Disclosure Requirements on policies, actions, and targets (see ESRS 2, chapter 4.2 *Minimum Disclosure Requirements on policies and actions* and chapter 5 *Metrics and targets*). ~~In this context, it is important to note that no disclosure is required when~~ If the undertaking ~~does~~has not ~~have~~adopted such policies, actions ~~and/or~~ and/or targets, ~~it is mandatory to state it, but no specific information is required, apart from an optional disclosure on the timeline to report on, except for stating this fact~~adopt such policies, actions or targets. (ESRS 1 paragraph 33). The datapoints in the Minimum Disclosure Requirements have been defined to depict the relevant information that a user would require to assess the policies, actions and targets in relation to a material matter. ~~At the same time~~Conversely, reporting that the undertaking does not have policies, actions or targets for a material matter is per se a material piece of information even if the undertaking is not required to include any information in relation to the datapoints prescribed by the Disclosure Requirements relating to the absent policies, actions, and/or targets. ~~In addition, it has an option to include, on a voluntary basis, the timeframe in which it aims to put in place the respective policies, actions and/or targets.~~

~~37.50.~~ 37.50. The determination of information to be reported for metrics is informed by the assessment of material information, ~~as it is possible to omit Disclosure Requirements and/or datapoints when they are not material (ESRS 1 paragraph 34).~~ This is generally performed starting first at the level of the Disclosure Requirement, and ~~then it follows to~~second at the level of the related datapoints located either in the Disclosure ~~Requirement~~²Requirement⁵ or, when applicable, in Application Requirements. When the information required by a Disclosure Requirement or a datapoint is assessed to be not material (as per criteria of ESRS 1 paragraph 31), and for datapoints not needed to meet the objective of the Disclosure Requirement, the undertaking does not disclose (*may omit*) such information. ~~(ESRS 1 paragraph 34).~~

~~38.51.~~ 38.51. The criteria to assess the materiality of information (ESRS 1 paragraph 31) are also expected to support the determination of ~~the~~ entity-specific disclosure~~disclosures~~ (ESRS 1 paragraph 30 b) and ESRS 1 paragraph 11 and paragraphs AR 1-5). This is to ensure that entity-specific disclosures (a) meet the qualitative characteristics of information and (b) include all material information related to the four reporting areas.

⁵ For ESRS E1 this applies also for datapoints located in Application Requirements.

~~39.52.~~ The Disclosure Requirements and datapoints in ESRS 2 are to be reported irrespective of the outcome of the materiality assessment. ~~However~~In this case, the criteria to assess the materiality of information (ESRS 1 paragraph 31) are expected to support the determination of the level of detail of narrative disclosure that is necessary to meet the Disclosure Requirements in ESRS 2 (ESRS paragraph 31 refer to the 'applicable information', so also to this case).

~~3.4~~ 2.5 Datapoints derived from EU legislation

~~46.~~ When the undertaking omits a datapoint derived from other EU legislation listed in ESRS 2 Appendix B *List of datapoints in cross-cutting and topical standards that derive from other EU legislation*, because it is not material~~;~~, the undertaking has to include an explicit statement that such

~~2~~ For ESRS E1 this applies also for datapoints located in Application Requirements.

~~40.53.~~ A datapoint is "not material". ESRS 2 paragraph 56 requires that the undertaking includes in the sustainability statement a table of all the datapoints in ESRS 2 Appendix B, specifying where they can be found in the statement and for those that are omitted as not material, reporting that the respective datapoint is not material.

~~41.54.~~ Such datapoints are treated in the same way as any other datapoint for the purposes of assessing the information to be reported on a material matter, i.e., when they relate to policies, targets and actions they follow ESRS 1 paragraph 33 and when they relate to metrics, they follow ESRS 1 paragraph 34 ~~applies and omissions of datapoints, whereby these are possible, omitted if assessed as not material.~~

~~3.5~~ 2.6 Considerations for upstream/downstream value chain

~~42.55.~~ The materiality assessment is also used to identify material impacts, risks and opportunities connected with the undertaking through its direct and indirect business relationships in the upstream and/or downstream value chain (for further detail see Value Chain Implementation Guidance).

~~4~~ 3 Materiality assessment – how is it performed?

~~43.56.~~ ESRS do not mandate how the materiality assessment process shall be designed or conducted by an undertaking, ~~or how the process should be designed. No. This is because no~~ one process would suit all types of economic activities, organisational structure, location(s), business relationships of operations or value chains (upstream and/or downstream) value chains of all ~~the~~ undertakings applying ESRS.

~~44.57.~~ An undertaking, based on its specific facts and circumstances, shall design a process that is fit for purpose considering the requirements of ESRS 1 Chapter 3, and ~~what needs to be disclosed~~ the disclosure requirements regarding the materiality assessment and its outcome (see ESRS 2 IRO-1, IRO-2 and SBM-3). ~~Therefore, the ESRS provide several aspects that~~ Regardless of the process applied, an undertaking takes account of when designing it shall consider the full scope of environmental, social and governance matters (ESRS 1 paragraph AR16) under the double materiality assessment process approach.

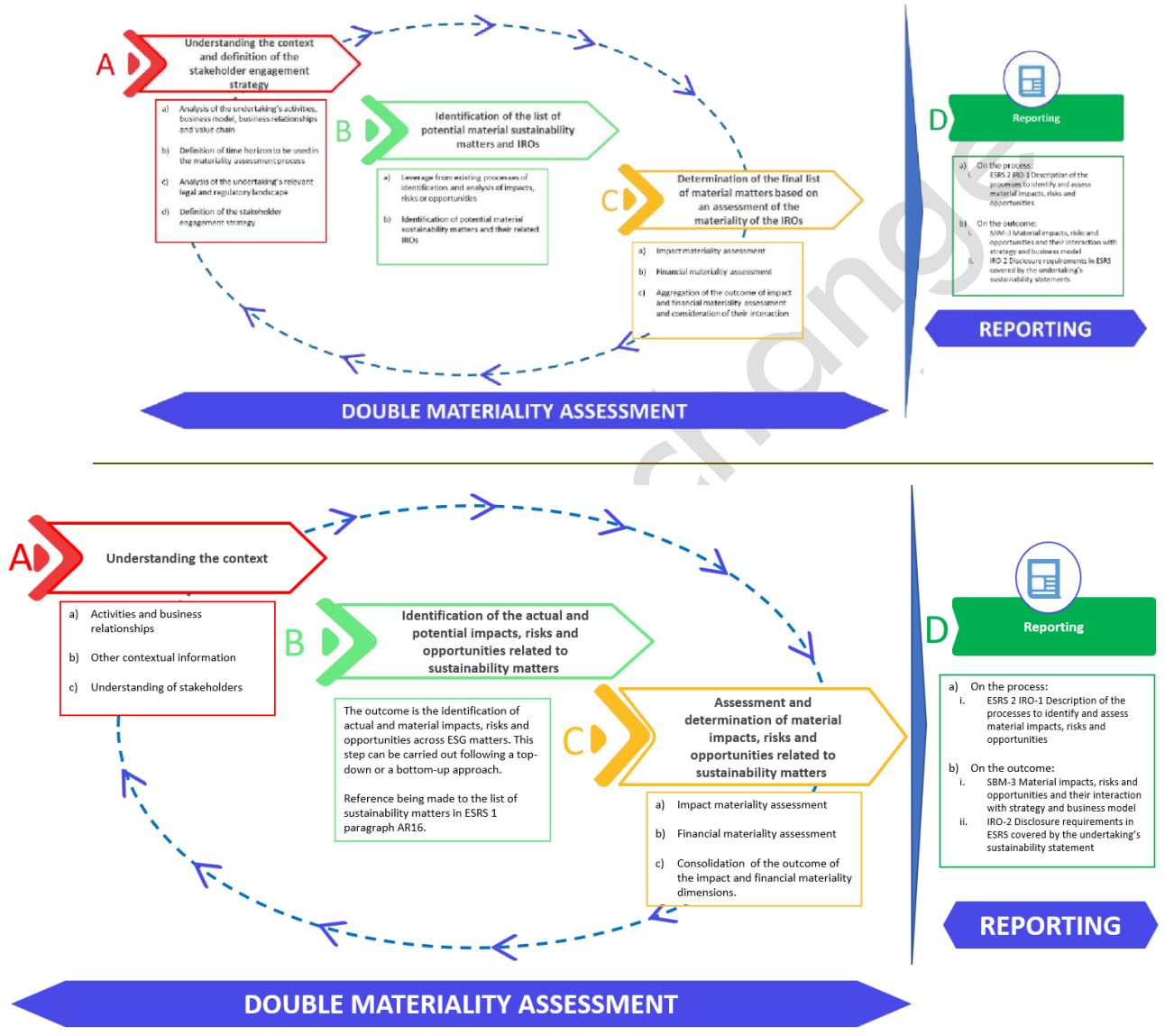
~~45.58.~~ The undertaking's materiality assessment shall reflect the impact and financial materiality perspectives, as well as ~~possible interlinkages~~ interconnections between the two. This means that the undertaking does not need to perform two separate and independent materiality assessments. The identification of material impacts is generally a starting point since the financial materiality assessment shall consider the outcome of the impact materiality assessment (see ESRS 1 chapter 3.3 Double materiality) as material impacts may trigger material risks and opportunities. ~~Nevertheless~~ In addition, the undertaking shall also consider the possible matters that are financially material without being material from the impact perspective.

~~59.~~ As an illustration, the process below includes four possible steps that undertakings may follow when conducting a materiality assessment that would meet aligned with ESRS:

~~-~~ Step A: Understanding the requirements context

- Step B: Identification of ESRS 1 (see chapter 3 the actual and paragraphs AR 6 potential impacts, risks and opportunities related to AR 16) could include the following steps which are derived from current best practices, alternative approaches being equally possible- sustainability matters
- Step C: Assessment and determination of the material impacts, risks and related to sustainability matters
- Step D: Reporting

Figure 3: Example of a materiality assessment process



46-60. Chapter 65.3 FAQ on the materiality assessment process has further guidance on the process.

43.1 Step A: Understanding the context and definition of the stakeholder engagement strategy

58. This step may consist of the following:

61. a. the analysis of the undertaking's activities, business model, In this step, the undertaking develops an overview of its activities and business relationships, the context in which these take place and the understanding of its key affected stakeholders. This overview provides key inputs to the undertaking for identifying its impacts, risks and opportunities.

Activities and business relationships and value chain (upstream and/or downstream) (linked to

~~47-62.~~ The aspects that are considered in relation to activities and business relationships relate to those disclosed in ESRS 2_SBM-1 which includes, but is not limited to, and are as follows:

- a. the analysis of the undertaking's business plan, strategy, financial statements and, when applicable, other information provided to investors;
- b. ~~the mapping of~~ the undertaking's activities, products/services, and the geographic locations of these activities;
- c. the mapping of the undertaking's business relationships and upstream and/or downstream value chain, including type and nature of business relationships; ~~and~~
 - i. ~~the identification of the perimeter of the information to be reported (beyond its own operations: expansion of the perimeter to reflect impacts, risks and opportunities arising from business relationships upstream/downstream value chain) for the materiality assessment.~~
- d. ~~the definition of time horizon (short-, medium- and long-term) to be used in the materiality assessment process (see ESRS 1 Chapter 6.4);~~

Other contextual information

63. There are other factors that can help identify particular sources of impacts, risks and opportunities such as:

- a. the analysis of the undertaking's relevant legal and regulatory landscape. ~~This analysis should factor in the relevant EU regulation and other sector specific regulations. The undertaking may also extend the analysis to, and~~
 - i. ~~the analysis of published documentation such as media reports;~~
 - ii. ~~peers', analysis of peers, existing sector-specific benchmarks, and~~
- b. , other publications on general sustainability trends and scientific articles;

Understanding of affected stakeholders

- iii. This step is aiming at understanding which are the stakeholders that are or are likely to be affected by the undertaking's own operations and

~~48-64.~~ d. the definition of the stakeholder engagement strategy upstream and downstream value chain (see chapter 4-23.5 Role and approach to stakeholder engagement in the materiality assessment) which includes the identification of the and what their views and interests are (this should be consistent with the disclosures in ESRS SBM-2 Interests and views of stakeholders). Based on this, the undertaking can identify its key affected stakeholders. This strategy is determined by To obtain this understanding, the following aspects can be considered:

- a. the analysis of the existing stakeholder engagement initiatives (for example, those with the communications or communication, investor relations, business management, sales and procurement teams of the undertaking);
- b. ~~the definition a~~ mapping of a list of key groups of affected stakeholders that are or could be affected by across the undertaking's own operations or upstream/downstream value chain whilst considering the nature of the relationship, activities and business relationships. It may be the case that ~~different~~ separate groups of stakeholders can be identified per activity, product or service and are to be prioritised for a particular sustainability matter; and
- c. the definition of the stage of the materiality assessment process in which the engagement will take place. For example, the engagement could be to validate the list of potentially identified material matters. Similarly, for impact materiality, the engagement could be focussed on the scale aspect of severity and on time horizons (i.e., short-, medium- or long-term).

49-65. Chapter 65.4 FAQ on stakeholder engagement ~~has~~ provides further guidance on the role of stakeholders.

4.3.2 Step B: Identification of the ~~list of~~ actual and potential ~~material sustainability matters and impact, risk~~ impacts, risks and opportunities

~~59. This step may consist of the following:~~

~~a. building on existing processes of identification and analysis of impacts, risks or opportunities such as those listed below:~~

- ~~i. the outcome of existing materiality assessment processes based on other frameworks. In this context, ESRS 1 paragraph AR 16 provides the universe of ESRS sustainability matters, therefore a mapping exercise could be conducted for completeness.~~
- ~~ii. the outcome of the existing due diligence process;~~
- ~~iii. the feedback or inputs received from stakeholder engagement processes already in place, i.e., customer / employee satisfaction surveys, grievance mechanisms, etc.; and~~
- ~~iv. benchmark analysis of material topics for peers/ the sector specific matters.~~

~~b. identification of potential material sustainability matters and their related impacts, risks and opportunities. To do so, the undertaking may follow one of the following approaches: to sustainability matters~~

- ~~i. "Top-down" approach: This is the identification of the list of potential material sustainability matters at topic / sub-topic / sub-sub-topic level followed by the assessment of the existence of the related potential material impacts (actual / potential, negative or positive), risks or opportunities. Depending on the level of maturity of such assessments by the undertaking, the identification of the potential matters could have two different starting points:
 - ~~• the list in ESRS 1 paragraph AR 16 as it summarises the sustainability matters covered by ESRS (see FAQ 9 *Is it sufficient to evaluate the list of sustainability matters of ESRS 1?*). This list of topics/sub-topics could be enhanced to include the results of step A above, for example, information gathered from engagement initiatives with relevant stakeholders and experts, scientific and analytical research performed; or~~
 - ~~• the list of potential material topics/sub-topics/ sub-sub-topics that the undertaking has developed using external and internal such as its own Enterprise Risk Management system, when it covers sustainability matters for risks and opportunities; or the output of the due diligence process for impact materiality. This list is to be compared with the list of ESRS 1 paragraph AR 16 for completeness, to ensure that all potential material topics/subtopics have been considered.~~~~
- ~~ii. "Bottom-up" approach: This is the identification of the list of potential material matters on the basis of the impacts, risks and opportunities which are identified at a granular level. The undertaking may then group these impacts, risks and opportunities into topics or sub-topics, which become the list of potential material matters to be compared with the classification defined in ESRS 1 paragraph AR 16.~~

~~66. The outcome of this step is the definition of a list of potential material matters (topics and subtopics) and their related impacts, risks and opportunities. In this step, the undertaking identifies the material impacts, risks and opportunities relating to environmental, social and governance matters across its own operations and upstream and downstream value chain. The outcome will be a "long list" of impacts, risks and opportunities for further assessment and analysis in subsequent steps.~~

~~67. The undertaking should use the list of the sustainability matters in ESRS 1 paragraph AR16 to support this process and to ensure completeness. It is equally important for the undertaking to consider entity-specific sustainability matters and sector-specific standards; currently, until the sector standards are issued, sector~~

sustainability matters shall be identified and assessed as entity-specific. The available best practices and/or available frameworks and/or other reporting standards, such as the IFRS industry-based guidance and GRI Sector Standards, are possible sources of relevant disclosures (ESRS 1 paragraph 131 b) for entity-specific matters.

68. For each identified impact, risks or opportunity, the undertaking should consider, and where necessary determine, what these relate to (i.e., own operations, upstream or downstream value chain) and time horizon (short-, medium-, or long-term) as per ESRS 1 Chapter 6.4.

Top-down approach

69. In terms of process, an undertaking could start to identify the matters from the list of topics summarised in ESRS 1 paragraph AR 16. This list could then be completed by additional entity-specific matters that follow from either internal processes already in place (i.e., due diligence, risk management or grievance mechanisms) or external sources such as those described in para 63 above and stakeholder engagement.

70. The identified long list of matters could then be aggregated following the structure of ESRS 1 paragraph AR 16. Also, to note that some cases, the undertaking may, for undertakings may use different terms to those sub-topics (or sub-sub-topics) in ESRS 1 paragraph AR 16 for the top-down approach and, hence, a further harmonisation of terms should be performed.

71. The approach detailed in para 67 above could typically be effective for undertakings that are new to preparing the sustainability statement and have not material on an individual basis, aggregate them at a higher level (topic level or sub-topic level), if that higher level is material due to another sub-topic (or sub-sub-topic) being material at the level below. An example is working conditions where for yet developed a full sustainability reporting roadmap. Alternatively, an undertaking could start from the matters as informed by existing reporting (e.g., GRI, due diligence, risk management) in place. In this case, the undertaking would compare the matters identified with the list of ESRS 1 AR16 for completeness.

72. For this top-down process, the undertaking would then identify any additional impact, risk and opportunity for each matter to complete the materiality assessment and disclose it according to ESRS 2 SBM-3.

Bottom-up approach

50-73. An undertaking may also decide to start from a list of impacts, risks and opportunities that it identifies from a review of its business model, strategy, own operations and upstream/downstream value chain and further research. This list would subsequently be linked to a list of matters that cover these IROs. For example, an undertaking that has identified social dialogue, collective bargaining and freedom of association areas not material on an individual basis but altogether may assess these three factors combined as material for the undertaking— within working conditions.

51-74. Chapter 6-5.5 FAQ on aggregation/disaggregation has provides further guidance on aggregation/disaggregation.

4.3.3 Step C: Assessment and determination of the final list of material matters based on an assessment of the materiality of the impacts, risks and opportunities related to sustainability matters

52-75. ThisIn this illustration, this is the last step of the materiality assessment process whose the outcome of which is the list of material impacts, risks and opportunities- and which consolidates the results of the previous steps. This list will be the basis for preparation of the sustainability statement and the information provided therein. This may include the following:

43.3.1 Impact materiality assessment

~~53-76.~~ The undertaking shall apply objective criteria set out under chapter 3.4 of ESRS 1 using appropriate quantitative and/or qualitative thresholds to assess the materiality of current and potential impacts, which is based on severity and, for potential impacts, also likelihood (see chapter ~~43.6~~ *Setting thresholds for impact materiality*).

~~54-77.~~ Therefore, the undertaking shall go through the list of ~~potentially material~~ impacts defined in step B above and apply the criteria determined ~~by~~for severity, which ~~is~~are scale, scope and irremediable character of the impact for actual negative impacts. For potential negative impacts, the undertaking estimates ~~also~~ the likelihood of the impact occurring and maps it to the relevant time horizon. For actual positive impacts, the criteria are scale and scope and for ~~potential future~~ positive impacts, the undertaking shall ~~also~~ estimate the likelihood of occurrence.

~~55-78.~~ Stakeholder engagement (~~including workers and their representatives~~) informs this step of the materiality assessment as key ~~affected~~ stakeholders could ~~help~~ assess, validate and ensure completeness of the final list of material impacts; in particular, for the scale and irremediable character determination and ~~the estimation of likelihood within impact materiality. for the estimation of likelihood. Likewise, internal engagement with the undertaking's business functions and employees could also help to assess, validate and ensure completeness of the outcome.~~

~~56-79.~~ Chapter ~~65.1~~ FAQ on *impact materiality* provides further guidance on impact materiality. See also chapter ~~54.3~~ *Leverage from international instruments of due diligence*.

43.3.2 Financial materiality assessment

~~57-80.~~ Material risks and opportunities for the undertaking generally derive either from impacts or from dependencies. To assess their materiality, appropriate quantitative and/or qualitative thresholds based upon ~~anticipated~~ financial effects in terms of performance, financial situation, cash flows, access to and cost of capital are used.~~-~~

~~81.~~ Sustainability risks and opportunities are assessed based on their likelihood of occurrence and the potential magnitude of their financial effects in the short-, medium-, and long-term. Therefore, the undertaking shall go through the list of ~~potentially potential~~ material risks and opportunities from step B above and apply ~~an~~ a set of objective ~~set of~~ thresholds for likelihood and magnitude.

~~82.~~ Reflecting the fact that most impacts give rise to financial risks and opportunities, the undertaking may in this step assess whether material financial effects do derive from the impacts identified above (including the outcome of step B). Beyond risks and opportunities associated to impacts, the undertaking shall also consider other sources of risks and opportunities, such as dependencies, changes in regulations or climate hazards, etc.

~~58-83.~~ When applicable, the undertaking may compare ~~these~~the material risks and opportunities in the list prepared in step B to the ones used in its risk management process (for example, ERM⁶ processes~~-~~), when the latter also covers ~~also~~ sustainability risks⁶, and estimate the likelihood of occurrence of the risks and opportunities or their related financial effects accordingly.

~~60.~~ ~~In addition, the undertaking shall consider the list of potential material impacts to assess whether they are sources of current or potential risks and opportunities.~~

~~59-84.~~ Engagement with the undertaking's business unit functions may be appropriate to assess, validate and ensure completeness of the list of material risk and opportunities together with investors of the undertaking and other financial counterparties (e.g., banks).

~~85.~~ Once a matter has been assessed to be material from a financial perspective (and therefore to be reported on), the undertaking determines the information to be reported based on its materiality (see chapter 2.3 *Criteria for the identification of material information*). In both cases, information is considered material if omitting, misstating or obscuring that information could reasonably be expected to influence

⁶ Enterprise Risk Management, see https://docs.wbcsd.org/2018/10/COSO_WBCSD_ESGERM_Guidance.pdf

decisions that primary users of general-purpose financial reports take on the basis of the undertaking's sustainability statement, relating to providing resources to the undertaking.

~~60.86.~~ Chapters ~~65.2~~ FAQ on financial materiality ~~has~~provides further guidance on financial materiality.

4.3.3 ~~Aggregation.~~ 3 Consolidation of the outcome of the impact and financial materiality dimensions and consideration of their interaction

~~61.87.~~ The objective of this ~~final~~last step is to consolidate the results of the previous steps and obtain the list of material impacts, risks and opportunities which will be the basis for the preparation of the sustainability statement. The analysis performed at material topic/sub-topic or sub-~~sub-topics~~sub-topic level is to be converted into material impacts, risks and opportunities if this has not taken place previously. ~~This would comprise:~~

- ~~a. application of the defined thresholds to the results of the impact materiality assessment;~~
- ~~b. application of the defined thresholds to the results of financial materiality assessment;~~
- ~~c. aggregation of the results of impact and financial materiality assessment with an identification of those material~~Once the undertaking has assessed individual impacts that will lead to material, risks and opportunities;
- ~~d. where based on appropriate, the undertaking, thresholds and methodologies, it may further aggregate or group the identified~~resulting material impacts, risks and opportunities ~~into sub-topics or even topics (following the criteria set in Step B), to ensure the most appropriate level of granularity; and~~

~~62.88.~~ ~~validation of~~for reporting purposes. The undertaking ~~may also validate~~ the aggregated double materiality results with management (to assess and validate the completeness of the list of material impacts, risks and opportunities).

3.4 ~~4~~ Step D: Reporting

~~63.89.~~ Following the performance of the materiality assessment process, the undertaking shall report the assessment process and its ~~output~~outcome based on:

- a. ESRS 2 IRO-1 – *Description of the processes to identify and assess material impacts, risks and opportunities;*
- b. ESRS 2 SBM-3 *Material impacts, risks and opportunities and their interaction with strategy and business model;* and
- c. ESRS 2 IRO-2 *Disclosure requirements in ESRS covered by the undertaking's sustainability statements.* Paragraph 59 of ESRS 2 requires the undertaking to disclose how it has determined the material information to be disclosed, including thresholds and criteria used to assess such information.

~~64.90.~~ Chapter ~~65.6~~ FAQ on reporting ~~has~~provides further guidance on reporting.

43.5 Role and approach to stakeholders in the materiality assessment process

~~91.~~ ~~The concept~~ For ESRS reporting purposes, stakeholders are classified into the following two groups as per ESRS 1 paragraph 22: affected stakeholders and users of stakeholder engagement has been highlighted by sustainability statement.

~~65.92.~~ ESRS clarify that the materiality assessment process is informed by the due diligence process laid out in the international instruments of due diligence, namely the OECD MNE and UNGP. ~~The due diligence~~

~~process enables the undertaking to determine its impact on people or the environment.~~ ESRS 1 paragraph 24 describes that engagement with affected stakeholders is central to the undertaking's due diligence and impact assessment, insofar that their perspectives inform the materiality process.

~~66.93.~~ Stakeholder engagement ~~Engagement with affected stakeholders~~ entails seeking input and feedback to understand ~~the~~their concerns and ~~the, in turn,~~ evidence of actual or potential impacts on people and environment connected with the undertaking from those stakeholders that could be affected.

~~67.94.~~ Consulting with affected stakeholders and incorporating their views into the materiality assessment process helps the undertaking to substantiate the perspectives of the affected stakeholder groups in determining how relevant the sustainability matters are for them. For example, engaging with the undertaking's employees or their representatives on health and safety matters. This includes feedback received from stakeholders within its ongoing engagement with them as part of the undertaking's business practices.

~~68.95.~~ On impact materiality, the focus of the stakeholder's engagement could be on the scale (i.e., how grave the negative impact is or how beneficial the positive impact is for people or the environment – see ESRS 1 AR 10) and the time horizons when impacts are expected to materialise. The undertaking ~~shall consider engaging them~~may engage with affected stakeholders in step ~~C~~B of the ~~materiality assessment process,~~ when the ~~potential list~~identification of sustainability matters / IROs is being assessed, rather than ~~at an initial~~impacts take place or a later stage of the process when assessing such impacts in step C.

~~69.96.~~ Stakeholder engagement may equally corroborate the evidence that support financial materiality of sustainability matters. Users of the sustainability statement may play a role in helping companies assess financial materiality. The conclusions of the ESRS financial materiality assessment should be based on supportable evidence, which include views and interests of stakeholders. This is aligned with current practice for the financial reporting materiality processes, where notes to the financial statements and presentations to investors are adjusted regularly to reflect emerging issues and other matters of interest to investors. To this extent, the undertaking ~~is expected to~~could leverage existing mechanisms of dialogue with shareholders, other investors, and lenders, to support its financial materiality assessment process.

~~70.97.~~ In its approach to stakeholders' dialogue, the undertaking shall consider that stakeholders other than investors may also be interested in general-purpose sustainability-related financial information. ~~For example, as such information may be useful to assess how the undertaking manages its material impacts.~~ For example:

- ~~a. suppliers are keen to understand whether an undertaking will be financially stable enough to remain its customer in the future;~~
- a. affected communities ~~are~~may be interested in whether the provisions set aside to rehabilitate ~~a~~ polluted production ~~sites~~sites are sufficient to cover the necessary rehabilitation activities; and
- b. current and prospective employees may want to learn ~~how long an undertaking is likely to be financially stable given the~~about anticipated financial risks ~~it is exposed to.~~ effects that could impact their prospects within the organisation (e.g., pensions or training).

~~71.98.~~ In situations when consultation with stakeholders is not possible, ~~(for instance, because such engagements would put them at risk),~~ the undertaking may consider appropriate alternatives such as consulting credible independent experts ~~such as,~~ for example (ESRS S3 ~~Affected communities,~~ where) an Non-Governmental Organisation (NGO) representing this affected community ~~could~~which can provide valuable feedback ~~or, for environmental matters, scientific articles and reports.~~

~~72.99.~~ ESRS 2 requires ~~an explanation of whether and how the process to identify, assess and prioritise the undertaking's potential and actual impacts includes~~ transparency on consultation ~~conducted by the undertaking~~ with affected stakeholders (Disclosure Requirement IRO-1, paragraph 53 (b) iii). This means that, even though ESRS do not mandate behaviour, the undertaking will be required to disclose engagement with stakeholders when identifying and assessing actual and potential negative impacts. ~~The impacts, risks and opportunities identified and assessed at this stage will then inform the determination of those that are material for reporting purposes.~~

~~73.100.~~ Chapter ~~65.4~~ FAQ on stakeholder engagement provides further guidance.

4.6-3.6 Deep dive on impact materiality - Setting thresholds for impact materiality

~~74.101.~~ ~~To assess the materiality of impacts,~~This section illustrates in more detail the methodologies or criteria that could be used for step C on impact materiality. ESRS 1 paragraph 42 states that an undertaking shall apply criteria set under ESRS 1 chapter 3.4 using appropriate quantitative and/or qualitative thresholds ~~to assess the materiality of impacts connected to its activities, as well as those that are directly linked to its operations, products and services, including through the upstream and downstream value chain.~~

102. ~~Impact materiality is determined by~~The severity ~~for of an~~ actual negative impacts ~~and severity and likelihood for or~~ potential negative impacts. Severity is based on factors ~~impact is determined by the following characteristics that are scale, scope and irremediable character for negative impacts, and scale and scope for positive impacts. Therefore, these factors should be inform~~ the basis for determining the thresholds. ~~Also, when defining the threshold,~~

a. ~~scale: how grave the undertaking may consider~~impact is (i.e., extent of infringement of access to basic life necessities or freedoms (e.g., education, livelihood etc.);

~~a.b.~~ ~~scope: how widespread the overall~~impact is (i.e., number of potential impacts across individuals affected or the extent of the environmental, ~~social~~ damage); and ~~governance.~~

c. ~~irremediable character: the extent to which the impact can be remediated (e.g., through compensation or restitution; whether the people affected can be restored to their exercise of the right in question). The underlying question is: are there any limits on the ability to restore the environment or those affected to a situation at least the same as, or equivalent to, their situation before the negative impact?~~

However, ESRS 1 does not prescribe how to set such thresholds.

~~75.103.~~ ~~#ESRS 1~~ also states that the undertaking's due diligence process informs the impact materiality assessment. In this context, the undertaking may use its ongoing due diligence process or other risk management processes to inform its thresholds setting and determine whether impacts are material for reporting purposes. In those processes, the undertaking's management of adverse impacts is driven by an analysis of severity and/or risk prioritisation, which may inform the assessment of impact materiality.

~~61.~~ Such concept of establishing a threshold commensurate with the overall number of potentially material matters may mirror the principle of prioritisation for action of the most severe impacts

~~under the international due diligence instruments. However, in the case of ESRS such threshold is not set to define how to sequence or prioritise the actions but rather to define a "cut off" for information to be disclosed as material.~~

~~76.104.~~ When setting up the threshold, attention should be paid to any supportable evidence that provides as much objectivity as possible to the materiality conclusion. However, reasonable quantification of the potential impacts may not always be available to support the materiality assessment.

~~62.~~ For negative impacts, ~~Any of the~~ starting point for determining a threshold should be the scale (how grave) and scope (how widespread). This means that the gravity of an impact and the number of individuals or perimeter that are or will be affected will both be relevant considerations.

~~63.~~ ~~three characteristics~~Irremediability is the third relevant factor of severity, ~~used here to mean any limits on the ability to restore those affected to a situation at least the same as, or equivalent to, their situation before the negative impact.~~

~~77.105.~~ It is to be noted that if one of these factors (scale, scope and irremediable ~~can make an impact severe, but often the characteristics are interdependent. Irremediable character~~) is significant, the impact would become "severe". Typically, there is an interrelation between these factors; hence, the ~~could impact the severity by increasing its gravity or scale. In turn, it is often the case that the greater the scale or the scope of an impact, the less it is remediable.~~

43.6.1 Current Actual impacts

78.106. In terms of applying the concepts described above and as an illustration, an undertaking could map its actual impacts in a two-dimensional graph where scale and severity are the axis, categorised in a range from low to high impact and combined with irremediability as symbolized by the arrow (figure 4a); or all three are arranged in column form (figure 4b), to the three characteristics of severity in a column format (figure 4).

Figure 4a: Graphical representation of impact severity for current actual impacts

(scale, scope combined with irremediability)

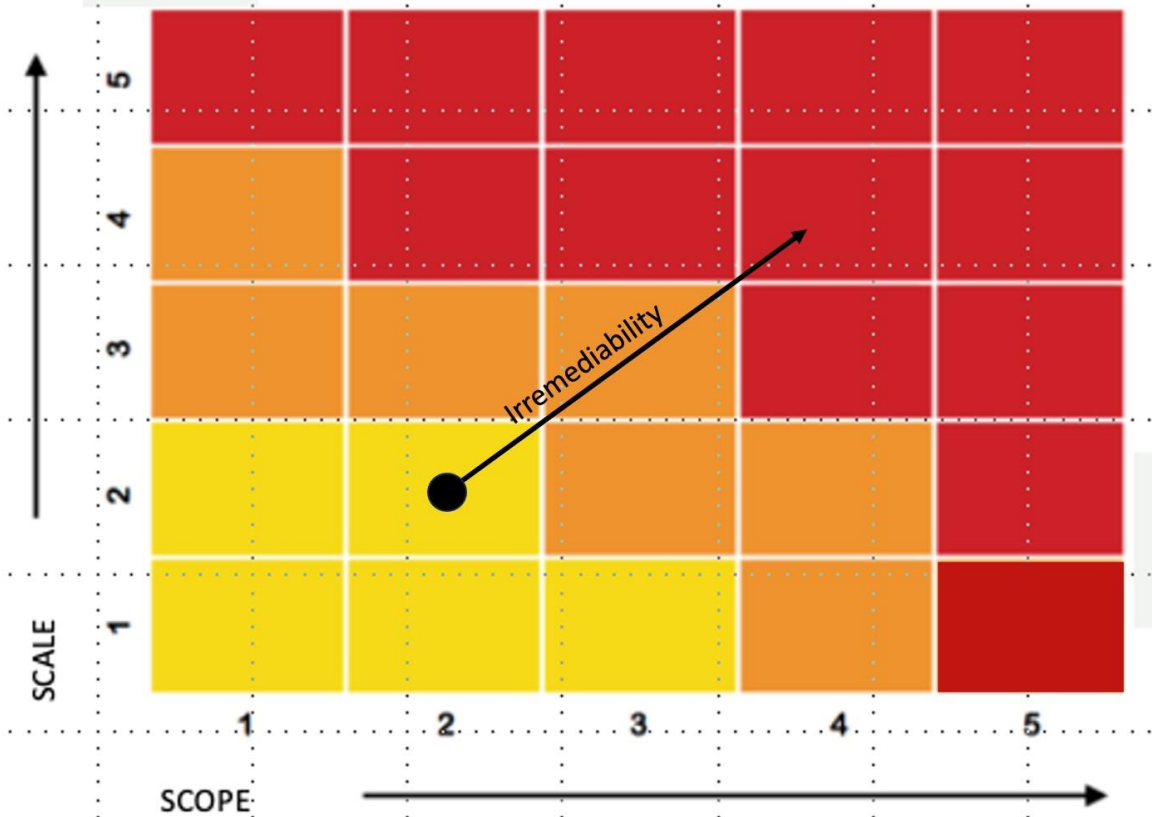


Figure 4b: Graphical representation of impact severity for current impacts (scale, scope, and irremediability-arranged] in column form) columnar format

potential material impact	Severity assessment			Conclusion on materiality
	Scale	Scope	Irremediability	
impact 1				no
impact 2				yes
impact 3				yes
...				
impact N				yes-No
Impact 1				Yes
Impact 2				Yes
Impact 3				
...				



100. In terms of scale, this represents how grave is the impact for negative impacts and how beneficial the impact is or could be for positive impacts. ~~Aspects that affect the scale can be whether the impact leads to non-compliance with laws and regulations can be an indication of the scale;~~ for example, if a negative impact leads to a violation of human rights. In this context, a reasonable objective measure ~~of impacts to be used in the categorisation of~~ assess the various impacts may not be available (i.e., a quantitative measure). ~~Hence the relevance of using the principle of relative~~

~~79.107. severity amongst the various impacts); hence, the need to categorise them. The scale is also linked to the irremediable character. In the case of positive impacts, the irredeemable character is not a factor to consider. define thresholds (in some cases, qualitative ones).~~

~~80.108. In terms of scope, the measurement may vary depending on the sustainability matter in question. In some cases, the number of individuals affected could be the appropriate basis (, for example, percent of employees) or in other cases the number of countries /factories affected by such matter may be relevant (for example, 40 percent of the suppliers are in countries where such negative impact arises). The scope factor could be assessed on a more quantitative basis than the other factors; and hence translating this value into a soft quantitative scale such as the colour coding or 1 to 5 scale mentioned above could can be more direct. useful.~~

109. ⁴For positive impacts, the criteria are scale and scope and apply analogously.

3.6.2 Potential impacts

~~81.110. For potential impacts, the likelihood dimension is to be considered together with the severity of the impacts. However, in the case of human rights impacts, as specified in ESRS 1 paragraph 45, severity takes precedence over likelihood when identifying material matters.~~

~~82.111. Following on the illustration above, the methodology would be the same and the likelihood dimension would be added. To this extent and to simplify its representation, the three factors within severity would be combined altogether into the severity axis and likelihood of occurrence would be represented in the horizontal axis.~~

~~83.112. In terms of likelihood, the likelihood of a potential negative impact refers to the probability of the impact happening. The likelihood of an impact can be measured or determined qualitatively or quantitatively, depending on the available information. It could be described using general terms (e.g., unlikely, highly likely) or mathematically using probability (e.g., 10 in 100, 10 percent) or a frequency over a given time-period (e.g., once every 10 years).~~

~~84.113. A similar approach to the currentactual impacts could be applied whereby the threshold for reporting material impacts is defined as the red area in the graph. Figure 5: Thresholds for materiality~~

Example

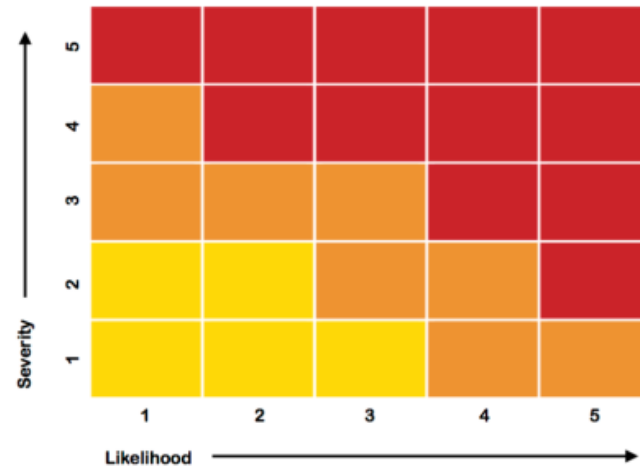
A large undertaking, A, has a material pollution matter regarding a river next to its factory due to its scale and irremediable character. In the following year, A is acquired by group B.

The scale of the pollution of the river impact of A is not affected by the fact that group B has several subsidiaries with other material environmental matters, some of them classified as medium on scale but higher on scope as it affects a higher number of factories.

Therefore, the fact that an undertaking is acquired, and forms part of a group does not change the severity categorisation of scale or irremediable character.

of potential impacts illustrative graph below. In this illustrative example, the undertaking has assessed that high severity (scale 5), and low likelihood (scale 1) negative impacts are material for environmental matters; such decision is based on the judgement of the undertaking.

Figure 5: Thresholds for materiality of potential impacts for illustrative purposes only (i.e., the colour coding of the matrix is to be determined by each undertaking following the criteria pursuant ESRS 1 Chapter 3.4 Impact materiality)

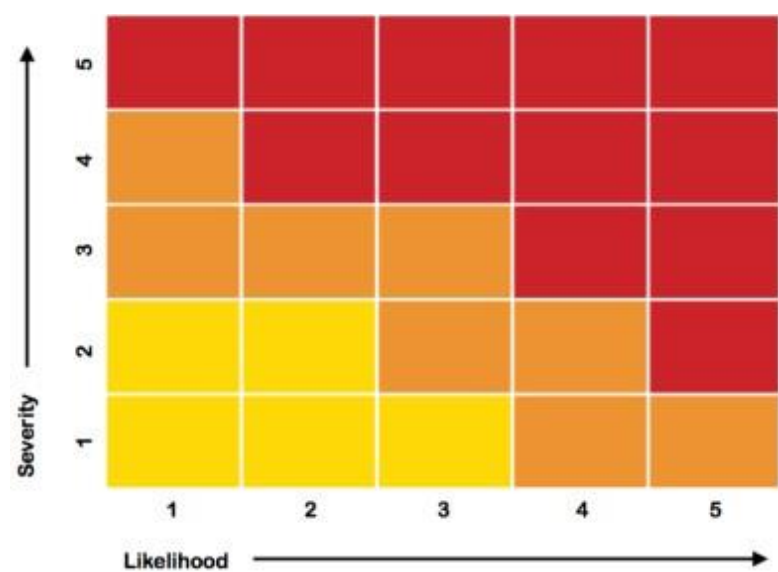


3.7 Deep dive on financial materiality - Setting thresholds for financial materiality

114. ESRS do not describe how to define financial materiality thresholds. However, ESRS 1 paragraph AR 15 states in that respect: “Once the undertaking has identified its risks and opportunities, it shall determine which of them are material for reporting. This shall be based on a combination of (i) the likelihood of occurrence and (ii) the potential magnitude of financial effects determined in the basis of appropriate thresholds. In this step it shall consider the contribution of those risks and opportunities to financial effects in the short-, medium- and long-term.”
115. The undertaking may refer to absolute monetary thresholds or to relative monetary thresholds, such as a percentage of the amount corresponding to a line item of its primary financial statements, its revenues, costs, total assets, net equity. Similar approaches are in practice used to assess materiality of an item for the preparation of financial statements and may be a possible source of inspiration. However, the undertaking shall consider that the time horizon for financial materiality assessment in sustainability reporting is longer than the typical time horizon factored in financial statements and management commentary. As an illustration, this may result in the need to consider the cumulative effect of a sustainability matter on revenues, costs, etc. over a lengthy period. Similarly, a threshold for likelihood needs to consider the cumulative probability over a lengthy period of time, to cover the long-term horizon.
116. In this context, the materiality assessment cannot be limited to the scope of financial effects that affect (or will affect in the future) items recognised in the financial statements. The undertaking shall as well consider financial effects associated with dependencies on natural and social resources that do not meet (or do not meet yet) the criteria for accounting recognition (ESRS 1 paragraph AR 14 and AR 15).
117. The undertaking should also consider that a sustainability matter may be financially material despite its financial effects not being (reliably) measurable at the reporting date. In this case the thresholds will rely on qualitative factors and ranges of possible effects (high/medium/low). In this case, there is a similarity with financial reporting, where materiality is not confined to quantitative aspects, but a narrative information may be material due to its nature, i.e., reflecting a qualitative approach to materiality.
118. With reference to the qualitative approach to materiality, there are circumstances in which, depending on the sector the undertaking is active in or depending on characteristics of its business model or operations, the undertaking is exposed to reputational risks that are of interest for investors. In this

case, while an effect on cash flows cannot be quantified, the reputational risk may influence the availability of finance and/or cost of funding and, therefore, be financially material.

When the undertaking has in place mechanisms of dialogue with its shareholders, investors and lenders, it may corroborate the determination of its materiality threshold with input from their users' needs.



4.6.3 Examples

101. ~~The assessment of the three factors of severity for a negative impact on violations of human rights could be as follows:~~

- ~~a. scale: extent of infringement of access to basic life necessities or freedoms (e.g., education, livelihood etc);~~
- ~~b. scope: number of people impacted, percentage of identifiable groups of people impacted; and~~
- ~~c. irremediable character: the extent to which the impact can be remediated (e.g., through compensation or restitution, whether the people affected can be restored to their exercise of the right in question).~~

102. ~~Another example could be undertaking A that is a large undertaking with a material pollution matter regarding a river next to its factory. In the following year, undertaking A is acquired by group B. The scale of the pollution of the river impact of undertaking A is not affected by the fact that group B has several subsidiaries with other material environmental matters, some of them classified as medium on scale but high on scope as it affects a higher number of factories. Therefore, the fact that an undertaking is acquired, and forms part of a group does not change the categorisation of scale or irremediable character.~~

119. This is because the goal of financial materiality is to report on information that, if omitted, misstated or obscured, could reasonably be expected to influence decisions that those stakeholders make on the basis of the undertaking's sustainability statement (ESRS 1 paragraph 48).

120. As in many cases sustainability matters that generate material impacts are also sources of material risks and opportunities, in its financial materiality assessment (refer to chapter 3 Step B and C), the undertaking shall carefully consider the linkages.

4. Materiality assessment – how to leverage other sources⁷?

54.1 Leveraging the GRI standards

~~85.121.~~ An assessment performed under GRI is focussed on the impact materiality dimension but not on the financial materiality dimension (see chapter 2.1), Implementing the concept of double materiality. The GRI framework is not based on double materiality like ESRS. However, the impact dimension is the same ~~for~~under GRI and ESRS even if the scope of environmental, social and governance matters under GRI may not exactly be the same with that of ESRS. Therefore, an assessment performed under GRI Universal Standards constitutes a good basis for the assessment of impacts under ESRS and the financial materiality dimension is to be added when moving from the GRI Universal Standards reporting framework to that of ESRS.

~~86.122.~~ Several synergies can be observed for those undertakings that are currently reporting under the GRI Universal Standards 2021 framework in terms of:

- a. impact materiality assessment process: ESRS 2 IRO-1 and IRO-2 are aligned in substance with GRI Universal Standards and the GRI materiality assessment can be the starting point for the ESRS double materiality assessment, with appropriate integration of financial materiality;
- b. universe of potential impacts identified using the GRI Universal standards: they are compatible in principle with the list of matters in ESRS 1 paragraph AR 16 (and as a result with the ESRS architecture of topics). In addition, GRI materiality assessment can inform the process of identifying the entity-specific impacts; and
- c. role of due diligence and stakeholder engagement: it is central in both GRI and ESRS frameworks in informing the impact materiality assessment.

54.2 Leveraging the ISSB standards

~~87.123.~~ In the intentions and expectations of EFRAG, as illustrated in the paragraphs below, the criteria for financial materiality and materiality of information in ESRS and the corresponding materiality approach in IFRS S1 are, in principle, aligned. The following paragraphs illustrate such alignment.

~~88.124.~~ The financial materiality assessment in ESRS 1 corresponds to the identification of information that is considered material for primary users of general-purpose financial reports in making decisions relating to providing resources to the entity (ESRS 1 paragraph 48, aligned with IFRS S1 paragraph 1). The definition of financial materiality is aligned in the two standards⁸.

~~89.125.~~ Reflecting the equivalence of the scope of financial materiality in the two frameworks, an undertaking that applies ESRS is expected to be able to comply with the identification of the risks and opportunities to be disclosed under IFRS⁷; using the outcome of its ESRS assessment of financial materiality. In other terms, the same financial materiality assessment process can support the identification of the risks and opportunities for both IFRS and ESRS purposes.

~~90.126.~~ The general criterion for assessing the materiality of information and therefore to support the identification of the information to be reported on a material matter (ESRS 1 paragraph 31) is expected, in most cases, to rely on decision-usefulness (see chapter ~~3.2~~), which 2.3 Criteria for the identification of

⁷ The content of this chapter reflects the thinking of the EFRAG Secretariat and has not been validated by GRI nor by ISSB.

⁸ For both IFRS S1 and ESRS 1, information is considered material for primary users of general-purpose financial reports if omitting, misstating or obscuring that information could reasonably be expected to influence decisions that they make on the basis of the undertaking's sustainability statement. In addition, IFRS S1 requires to disclose information about all sustainability-related risks and opportunities that could reasonably be expected to affect the entity's cash flows, its access to finance or cost of capital over the short, medium or long term. Under ESRS 2 SBM-3, the undertaking shall disclose its material impacts, risks and opportunities. Under ESRS 1, "A sustainability matter is material from a financial perspective if it generates risks or opportunities that have a material influence, or could reasonably be expected to have a material influence, on the undertaking's development, financial position, financial performance, cash flows, access to finance or cost of capital over the short-, medium- or long-term" (ESRS 1 paragraph 49).

material information); this is also the criterion used in IFRS S1 to identify the information to be reported (as material). While in ESRS the double materiality assessment of what is decision-useful considers both investors and other stakeholders, in IFRS this is limited to the users' needs of investors. However, for the financial materiality component of ESRS, the two perspectives are expected to be equivalent.

127. ~~5~~ Finally, IFRS S1 (paragraph 55) requires an entity to refer to and consider the applicability of the disclosure topics in the SASB Standards. Similarly, ESRS 1 (paragraph 131 b) identifies, as a source of disclosure that an undertaking may use in the definition of its entity-specific disclosures, the available frameworks or reporting standards, such as IFRS industry-based guidance (i.e., SASB Standards) and GRI Sector Standards. While for ESRS preparers the use of SASB standards is optional (as this is a possible source of disclosure, but not the only one), the provision of entity-specific disclosure including sector metrics is a requirement (see ESRS 1 paragraph 11).

4.3 Leveraging international instruments of due diligence

~~91~~.128. The materiality assessment of an undertaking's impacts, risks and opportunities is informed by the outcome of its due diligence process, as defined in the international instruments of the UN Guiding Principles on Business and Human Rights and the OECD Guidelines for Multinational Enterprises.

~~92~~.129. The due diligence process includes steps to identify and assess negative impacts caused and contributed to by the undertaking, as well as those connected to its own operations, products or services through its business relationships. This can be particularly useful when analysing the undertaking's upstream and downstream value chain and identifying the impacts originated there. Additionally, the due diligence instruments provide criteria to prioritise actions, based on the severity and likelihood of the impacts previously identified, ~~for management.~~

~~93~~.130. In that sense, the due diligence process can help an undertaking both (a) to identify its negative actual and ~~assess its potential and actual negative~~ impacts (see step B in chapter 4.3.2), as well as (b) to assess their materiality for reporting purposes based on the criteria of severity and likelihood (see step C in chapter 4.3.1). The identification of material impacts also supports the identification of material sustainability risks and opportunities, which are often a consequence of such impacts.

~~94~~.131. Through this process the undertaking can also identify affected stakeholders, ~~which should be engaged when assessing~~ whose engagement informs the materiality assessment of ~~the~~ impacts, risks and opportunities.

5 Frequently Asked Questions (FAQ)

65.1 FAQ on impact materiality

FAQ ~~1~~.1: Is impact materiality based on materiality to the undertaking or to stakeholders?

~~95~~.132. It is based on its impact to people or the environment, which are in turn stakeholders for the undertaking.

~~96~~.133. Impact materiality means the impacts on people and/or the environment connected with the undertaking's own operations and value chain, including through its products and services, as well as through its business relationships. ~~Hence, it is assessed by reference to~~ the severity of such impacts on the people and/or environment for actual or potential impacts. To assess such impacts stakeholder engagement is critical as described in FAQ 16 Do ESRS mandate to actively engage with stakeholders?

~~97~~.134. In contrast, financial materiality is focussed on ~~the materiality to the undertaking, because it is reflecting~~ the effects of sustainability matters on the undertaking's cash flows, financial performance, financial position, access to finance in the short-, medium- or long term or cost of capital, ~~as such effects are material to the undertaking's investors.~~

~~98.135.~~ In ~~many~~most cases material impacts are also associated with material risks and opportunities and, as a result, they are also 'material for the undertaking'. However, impact materiality is assessed based on severity for people and the environment, and not on the basis of the effects it has on the undertaking and its financial prospects.

FAQ ~~2:2:~~ What is meant by the undertaking being “connected” with an impact?

~~99.136.~~ Impact materiality ~~includes~~covers impacts connected with the undertaking's own operations and value chain, including through its products and services, as well as through its business relationships. An undertaking can be connected with impacts in ~~various~~several ways as described below.

~~100.137.~~ The undertaking may be single-handedly responsible for the impacts, as the **impacts are directly caused** by its operations, products or services to people or the environment. For example:

- a. exposure of the undertaking's own workers to hazardous working conditions without adequate safety equipment in own operations;
- b. being the sole source of pollution in a community's drinking water supply due to chemical effluents from production processes;
- ~~a. long-term pattern of failing to hire, support and promote qualified women;~~
- ~~b. failing to protect the confidentiality of personal data held about employees or contract workers, customers or other individuals; and~~
- c. for a positive impact, an undertaking in the energy production sector adopting measures that lower the cost of renewable energy for customers, thereby allowing more customers to switch to renewable energy, and thus contributing to mitigating climate change.

~~118.~~**Impacts to which the undertaking has contributed** to are those not caused directly and solely by the undertaking's operations, products or services.

~~101.138.~~ When the impact is not caused solely by the undertaking but in conjunction with a third party: the undertaking's action or omission would not, single-handedly, cause the impact, but together with others' actions or omissions, it leads to the impact. For example: several factories/sites in an area release harmful emissions into the air. Each release is below the harmful limit, but together they lead to the air being so polluted that a local community's air quality is affected, ~~and.~~

- ~~a. a clothing undertaking has its own production line in a supplier factory with standard eight-hour shifts; after working on this production line, the workers work on a parallel production line of a competitor for another eight hours.~~

~~102.139.~~ When the undertaking facilitates or incentivises another party to cause or contribute to the impact. For example: changing buying requirements for suppliers repeatedly without adjusting production deadlines and prices, thus pushing suppliers to breach labour standards in order to deliver, ~~and.~~

- ~~a. sending a negotiation team to drive down price with the supplier, without considering impact this may have on working conditions.~~

~~103.140.~~ **Impacts directly linked to the undertaking's** operations, products, and services ~~through its business relationships may arise in situations where such impacts are not be~~but caused ~~nor contributed by the undertaking, but the entities~~a business relationship. The entity that caused or contributed to the impact ~~are linked to the undertaking. Consequently, the undertaking is linked to the impact.~~undertaking. For example: ~~Embroidery~~The supplier subcontracting the embroidery on a retail undertaking's clothing products ~~being subcontracted by the supplier to child labourers in homes, counter to contractual obligations.~~

~~104.141.~~ Distinguishing the type of involvement is important given that it could lead to a different assessment or categorisation of the negative impact ~~and it is linked to international instruments on due diligence and human rights will require different responses to it and this may need to be reflected in the different types of policies, actions and targets that the undertaking has in place and that are to be reported.~~

FAQ 3:3: What are material impacts, risks or opportunities in the value chain?

~~105.142.~~ See Value chain implementation guidance: FAQ 3: How should the materiality assessment process be organised to properly capture material impacts, risks and opportunities that arise in the value chain?

FAQ 4:4: Can ~~positive~~negative impacts be netted against ~~negative~~positive impacts?

~~106.143.~~ No. Impacts are to be assessed on a gross basis. Positive impacts on the environment and people cannot be netted against negative impacts. –

~~107.144.~~ The following non exhaustive list of principles should be applied:

- a. different nature of impacts (~~negative vs. positive~~): an undertaking shall not net negative impacts with positive impacts of a different nature (in the reporting year or in future years) – this would contradict ESRS 1 paragraph 56: “... *The undertaking shall not aggregate material items that differ in nature.*” and the qualitative characteristics of quality (Appendix B of ESRS 1);
- b. timing of impacts (current vs. future): an undertaking shall not net negative/positive impacts in the reporting year with positive/negative impacts of the same nature in future years; and.
- c. location (in own operations vs. in the value chain): an undertaking shall not net negative/positive impacts in own operations with positive/negative impacts of the same nature in the value chain (in the reporting year or in future years).

~~108.145.~~ Netting should not be confused with compensation/offsetting. While netting negative with positive impacts in own operations and the upstream/downstream value chain is to be avoided, it should be noted that ESRS E1 –Climate change and ESRS E4 –Biodiversity and ecosystems have include specific requirements in that respect, on how to report on carbon credits and biodiversity credits.

6.5.2 FAQ on financial materiality

FAQ 5:5: Is materiality for financial statements and management commentary the same as financial materiality for the sustainability statement?

~~109.146.~~ No, it is not the same. However, the objective remains the same.

~~110.147.~~ The materiality assessment as to of information depends on whether the information is considered to be material for decision-making of those who provide, or may provide in the future, resources to the undertaking ~~remains the same. However,~~ ESRS 1 (paragraph 47) clarifies that the scope of financial materiality for the sustainability statement goes beyond is an expansion of the scope of the materiality used for in the process of determining which information should be included in the undertaking’s financial statements. This means that, whilst the concept of materiality does not differ between the two reporting frameworks. Its application on the information that is likely to be material does since the principles applied for the preparation of the financial statements, as illustrated by the financial reporting conceptual framework, establish a clear delineation of what should be accounted for on the basis of criteria for recognition of assets and liabilities (including in relation to control and/or obligations). As a result, when defining the thresholds for financial materiality used in the preparation of the sustainability statement, inspiration could be drawn from criteria and thresholds used in the preparation of the financial statements.

~~111.148.~~ The differences between financial information that is likely to be financially materiality for financial statements and financial management commentary and the information that is likely to be financially materiality for sustainability statement relate to the following aspects:

- a. sustainability reporting includes disclosures of potential financial effects of material risks or opportunities that are not captured or not yet fully captured by financial reporting at the reporting date and that could be reasonably expected to result in financial effects for the undertaking. Therefore, it is more likely that risks and opportunities that are not limited yet to be material for financial statements and management commentary, could be material for the

- ~~definition of sustainability statement where there are different underlying principles to provide information on assets and liabilities for the financial reporting;~~
- b. the information on the parent and its subsidiaries ~~are~~ expanded in the sustainability statement to include information about material risks and opportunities arising from the undertaking's ~~(parent and subsidiaries)~~ business relationships in the upstream/downstream value chain. Therefore, it is more likely that information about risks and opportunities arising from the undertaking's upstream/downstream value chain become material for the sustainability statement; and
 - c. future events may trigger anticipated sustainability-related risks and opportunities while ~~financial risks are based upon past events;~~ statements typically account for risks based upon past events. Therefore, it is more likely that forward looking information (for example, about anticipated financial effects) become material in sustainability statement;
 - d. time horizons ~~are~~ may be looking at longer timeframes in sustainability reporting as ~~mid-term and long-term are considered for risks and opportunities and~~ they are not constrained by the financial planning horizon or by the historical cost convention.

FAQ 6: Is financial materiality for sustainability reporting limited to effects presented in financial statements?

~~112.149.~~ 112.149. No. As described in FAQ 5 *Is materiality for financial statements and management commentary the same as financial materiality for the sustainability statement?*, the basis for preparation and time horizons of financial and sustainability reporting ~~differ~~ differ. The concept of current and anticipated financial effects defined in the glossary distinguishes between:

- a. financial effects that have already crystallised and are recognised in the primary financial statements or disclosed in the notes to financial statements (i.e., current financial effects); and
- b. financial effects that do not meet the recognition criteria for inclusion in the financial statements in the reporting period (i.e., anticipated financial effects).

~~113.150.~~ 113.150. Reporting certain financial effects associated with material sustainability matters in sustainability reporting goes beyond what is required to be recognised and measured in the primary financial statements and disclosed in the notes for those matters. In particular, financial effects that arise from risks and opportunities that have or could reasonably be expected to have a material influence on the undertaking's financial position, financial performance and cash flows, over the short-, medium- and long-term are to be reported irrespective of their accounting treatment. Sustainability risks or opportunities may derive from past or future events and may have financial effects in relation to:

- a. assets and liabilities already recognised in financial reporting. In this case potential adjustments to the carrying amount that are of interest for users of sustainability statement may not meet the accounting criteria for recognition in financial statements at the reporting date; albeit these anticipated financial effects are recognised in sustainability statement
- b. future assets, liabilities, income and expenses that are of interest to users of sustainability statement may have to be recognised in financial reporting at a later stage, when the accounting recognition criteria will be met; and
- c. factors of value creation that do not meet the financial accounting definition of assets and liabilities and/or the related recognition criteria but contribute to the generation of cash flows and more generally to the development of the undertaking; (for example, internally generated intangibles such as human capital that could be described in sustainability reporting).

FAQ 7: How should the undertaking set thresholds for financial materiality?

~~119. ESRS do not describe how to define financial materiality thresholds. However, ESRS 1 paragraph AR 15 states in that respect: "Once the undertaking has identified its risks and opportunities, it shall determine which of them are material for reporting. This shall be based~~

~~114.1. on a combination of (i) the likelihood of occurrence and (ii) the potential magnitude of financial effects determined in the basis of appropriate thresholds. In this step it shall consider the contribution of those risks and opportunities to financial effects in the short, medium and long term."~~

~~115.1. The undertaking may refer to absolute monetary thresholds or to relative monetary thresholds, such as a percentage of the amount corresponding to a line item of its primary financial statements, its revenues, costs, total assets, net equity. Similar approaches are in practice used to assess materiality of an item for the preparation of financial statements and may be a possible source of inspiration. However, the undertaking shall consider that the time horizon for financial materiality assessment in sustainability reporting is longer than the typical time horizon factored in the preparation of financial statements. As an illustration, this may result in the need to consider the cumulative effect of a sustainability matter on revenues, costs, etc. over a long period. Similarly, a threshold for likelihood needs to consider the cumulative probability over a long period of time, to cover the long-term horizon.~~

~~116.1. In this context, the materiality assessment cannot be limited to the scope of financial effects that affect (or will affect in the future) items recognised in the financial statements. The undertaking shall as well consider financial effects associated with dependencies on natural and social resources that do not meet (or do not meet yet) the criteria for accounting recognition (ESRS 1 paragraph AR 14 and AR 15).~~

~~117.1. The undertaking should also consider that a sustainability matter may be financially material despite its financial effects not being (reliably) measurable at the reporting date. In this case the thresholds will rely on qualitative factors and ranges of possible effects (high/medium/low). Also in this case, there is a similarity with financial reporting, where materiality is not confined to quantitative aspects, but an information may be material due to its nature, i.e., reflecting a qualitative approach to materiality.~~

~~120. When the undertaking has in place mechanisms of dialogue with its shareholders, investors and lenders, it may corroborate the determination of its materiality threshold with input from their users' needs. This is because the ultimate goal of financial materiality is to report on information that, if omitted, misstated or obscured, could reasonably be expected to influence decisions that those stakeholders make on the basis of the undertaking's sustainability statement (ESRS 1 paragraph 48).~~

~~121. As in many cases sustainability matters that generate material impacts are also sources of material risks and opportunities, in its financial materiality assessment. The undertaking may assume that sustainability matters are financially material when they have been assessed to be material from an impact perspective, unless there is evidence that this is not true at the level of a specific matter.~~

65.3 FAQ on the materiality assessment process

FAQ 87: How frequently should an undertaking update its sustainability materiality assessment?

~~118.151.~~ The CSRD defines the frequency of sustainability reporting under ESRS which is annual as the sustainability statement forms part of the undertaking's management report. Accordingly, the undertaking is required to determine at each reporting date its material impacts, risks and opportunities, as well as the material information to be included in the sustainability statement.

~~119.152.~~ However, if the undertaking ~~has performed a thorough materiality assessment in the previous periods and can conclude~~concludes based on appropriate evidence that the outcome of ~~that~~the materiality assessment performed in the prior reporting period is confirmed also at the reporting date, the preparation of the sustainability statement may leverage the conclusions previously reached. This may be the case when, for example, the undertaking assesses that there have been no material changes in the organisational and operational structure of the undertaking and there have been no material changes in the external factors that could generate new, or modify existing impacts, risks and opportunities or that could impact the relevance of a specific disclosure. Examples of changed material facts and circumstances could be:

- a. a major M&A transaction leading to a new activity, entering a new sector or a significant change in operations;

- b. a significant change of key suppliers or in the supply chain practices;
- c. a global event such as a pandemic or entering ~~into~~ a new material business relationship that is likely to have a severe impact on human rights; and
- a. ~~a shift in social conventions, scientific evidence or users' needs, such as when that could affect the characteristics of severity (e.g., the level of public scrutiny on a given matter significantly increases compared to previous periods;~~

~~122;~~ recent studies that provide evidence of the toxicity of a substance). The analysis performed for the preparation of the sustainability statement ~~at~~for each reporting period should be sufficiently robust and proportionate to capture the possible changes, ~~from the previous period(s),~~ including in the value chain. If so, the undertaking may limit the analysis to an annual update of its previous materiality assessment.

- d. ~~Practices may vary, as some undertakings may prefer fully updating their materiality analysis (i.e., process, criteria, research on sustainability matters, multi-stakeholder engagement...) on a 2 or 3-years cycle, whilst others may prefer performing targeted updates on an annual basis (i.e., list of impacts or risks and opportunities, while not repeating the initial materiality steps), focusing on the impacts, risks and opportunities that are affected by the identified changes (e.g., as a result of the changes some of them may cease to be material and other material impacts risks and opportunities may arise).~~

~~120;~~ 153. The materiality assessment is a dynamic process that will be subject to the inherent evolution of the undertaking and needs to be updated on an ongoing basis.

FAQ 98: Is it sufficient to evaluate the list of sustainability matters of ESRS 1 paragraph AR 16 to identify material matters?

~~121;~~ 154. No.

~~122;~~ 155. ESRS 1 paragraph AR 16 states: "Using this list is not a substitute for the process of determining material matters. This list is a tool to support the undertaking's materiality assessment. The undertaking still needs to consider its own specific circumstances when determining its material matters." Some undertakings may have their own list of material topics from previous impact materiality assessments (for instance, GRI Universal Standards reporting) and will use the list from ESRS 1 paragraph AR 16 as described in step B of the Materiality assessment process, chapter 3.2.

~~123;~~ The list in ESRS paragraph AR 16 is a good starting point for the identification of sustainability matters, but it should not be applied as a checklist approach substituting a materiality assessment. It is an inventory of the sustainability matters covered in sector agnostic topical ESRS. Sector-~~specific~~^{specific}⁹ and entity-specific sustainability matters (see ESRS 1 paragraph 11) should also be considered on top of this list.

~~123;~~ 156. ⁵ Future sector specific ESRS will identify where appropriate additional sustainability matters.

~~124;~~ 157. Given that sector-specific ESRS have not been finalised yet, sector-specific sustainability matters shall be identified and assessed on an entity-specific basis as long as the sector standards are ~~not~~ released (see ESRS 1 paragraph 131 (b))~~1~~.

⁹ Future sector specific ESRS will identify where appropriate additional sustainability matters.

FAQ ~~109~~: How to consider time horizon in the double materiality analysis?

~~158.~~ A sustainability matter might be material from an impact or financial perspective in the short-, medium- or long-term. As such, time horizon is an essential component of the materiality assessment and shall be factored into the process. ESRS 1 paragraph 77 to 81 define the standardised terms for time horizon, and it also provides an option to select entity-specific horizons for medium- and long- term.

~~125,159.~~ In the steps of the double materiality analysis the short-, medium- and long-term time horizon may be considered:

- a. for a proper **understanding** of the undertaking's facts and circumstances: in this step it is necessary to set an appropriate time horizon based on the context of the undertaking;
- b. for a proper **identification** of the list of sustainability matters: the undertaking needs to reflect over the entire time horizon (short/medium/long) to determine whether the impact, risk or opportunity may occur or not;
- c. for the **assessment** of material matters based on materiality of impacts, risks and opportunities: the undertaking may consider that the financial effects linked to material impacts may materialise on a different time horizon from the one of the ~~impact~~impacts. In addition, when determining which of the impacts, risks and opportunities are material, thresholds and dependencies might be affected by the time horizon.

Examples:

~~124.~~The undertaking might for instance conclude that:

- ~~a.~~ the financial effect of assets currently used that could become stranded assets in the long-term due to environmental risks to be not material as they will be fully amortised at that future point in time;
- ~~b.~~ the financial effect of a risk probable to occur in the long-term to be not material due to discounting; or
- ~~c.~~ an environmental impact to be material in the short-term but not in the long-term as it reasonably expects technology to be available in the long-term due to innovation to avoid the impact once it is developed.

FAQ ~~1170~~: Should the assessment of impacts, risks or opportunities rely on quantitative information?

if

Example

The undertaking might for instance conclude that:

- a. the financial effect of assets currently used that could become stranded assets in the long-term due to environmental risks to be not material as they will be fully amortised at that future point in time;
- b. the financial effect of a risk likely to occur in the long-term to be not material due to discounting.



~~126.160.~~ Where possible, yes, as quantitative measures of impacts, risks and opportunities are the most objective evidence of how ~~severe an impact is material~~ they are.

161. However, The level of comfort sought by the undertaking from quantitative information also depends on scientific validated data and consensus reached on the given impact; for example, global reports or industry information on a given topic, such as negative impacts on biodiversity loss, could provide the quantitative information needed without the need for the undertaking to incur in additional research or data collection costs.

Example

If the undertaking concludes, based on qualitative criteria, that an impact connected to the undertaking is on the edge of the material/non-material border, it may consider quantitative information on severity (i.e., scale or scope) as described below to prioritise the impacts. For example:

1. the amount of water used in production in a particular water-stressed area; or
2. the number of people possibly affected in a community where it has a production site.

~~127.162.~~ Quantitative information is not ~~always~~ always available or may result in additional costs. Whenever a qualitative analysis is sufficient for the undertaking to reasonably conclude that a matter is “not material” (or “material”), adding quantitative information to the analysis would not bring much value to the materiality assessment. As mentioned above, the materiality assessment process evolves over time and the undertaking may be redefining the qualitative vs quantitative information balance.

~~128.163.~~ Quantitative information would however be of interest where a topic is on the edge of the material/non-material border based on qualitative information and/or where there are many diverse views. In that case, quantification could be relevant to corroborate the conclusion. This could include impact valuation, which would also have the advantage to make different impacts comparable.

~~129.164.~~ In this context, the undertaking may consider adopting measures of impacts inspired by the indicators that are included in the Metrics and Targets section of the topical ESRS.

Examples:

~~125.~~ If the undertaking concludes, based on qualitative criteria, that an impact connected to the undertaking is on the edge of the material/non-material border, it may consider:

- a. the amount of water used in production in a particular water-stressed area; or
- b. the number of people possibly affected in a community where it has a production site.

FAQ 12: ~~Is it necessary to “consolidate/aggregate”~~ 81: Should the impact and the financial risks and opportunities dimensions of a sustainability matter to assess its be aggregated for the materiality? assessment?

~~130.165.~~ No.

~~131.166.~~ Despite that impact and financial materiality are inter-related and that the ~~interdependencies~~ interconnections between the two dimensions shall be considered (see ESRS 1 chapter 3.3. Double materiality), ~~it is sufficient that~~ a sustainability matter is not required to be material from ~~one of the two~~ both dimensions to be treated as a material ~~sustainability matter~~ for reporting purposes.

~~126.~~ If there is a relationship on a given sub-sub-topic between a current negative impact and risks in the medium- or long-term, ESRS 2 SBM 3 requires providing a description of the impact on one hand, and of the risks on the other hand.

167. FAQ 13 For example, an undertaking in the extractive industry has assessed health and safety as a material negative impact due to the frequency and severity of work-related accidents in its location. However, the current financial effects have not been considered financially material. Therefore, there is no aggregation of impacts and risks and opportunities on this matter.

FAQ 12: Should the materiality assessment be documented/evidenced? ~~And, if so, how?~~

~~132.168.~~ ESRS do not prescribe a specific documentation, however it is reasonable to expect a certain level of documentation to be produced for internal purposes, such as to inform those in charge of the governance over the process of sustainability reporting (see ESRS 2 GOV- 5), in order to be able to prepare the disclosure prescribed by ESRS 1 IRO-1 and to allow assurance providers to perform their work.

~~133.169.~~ The CSRD modifies the Accounting Directive with respect to the definition of the content of the management report in relation to sustainability information and its digitisation (namely Art 19a and Art 29a) and also ~~to the level of~~ has introduced mandatory assurance related to of the sustainability reporting statement (in particular, Art 34).

~~134.170.~~ In this regard, EFRAG is the technical advisor to the European Commission for the content of the management report as it develops the draft ESRS; however, the EFRAG's mandate does not cover the ~~advice on assurance requirements.~~ The requirements with respect to the documentation and level of evidence supporting the materiality assessment (i.e., ESRS 2 IRO- 1 and 2 and ESRS SBM-3) is outside the remit of the ESRS.

~~127.~~ It is worthwhile to note that the Accounting Directive requires an assurance provider to “express an opinion based on a limited assurance engagement as regards the compliance of the sustainability reporting adopted pursuant to Article 29b or Article 29c, i.e. the sustainability reporting prepared using ESRS] including ... the process carried out by the undertaking to identify the information reported pursuant to those sustainability reporting standards, ...” (see Article 34 (aa) of Directive 2013/34/EU added by the CSRD).

FAQ ~~14~~13: How to do the materiality assessment in diversified undertakings that operate across different ~~businesses?~~ sectors?

~~135.171.~~ ESRS do not prescribe a specific process for the Materiality Assessment (MA). There is no one process for the materiality assessment that fits all undertakings, including ~~diverse or multiple~~ diversified global undertakings.

~~136.172.~~ A parent undertaking of a large group (according to CSRD art. 29a) has to disclose in its consolidated sustainability statement the group's impacts, risks and opportunities. For this purpose, the parent undertaking (as defined in ESRS 1 chapter 7.6) is to perform its materiality assessment for the consolidated group, irrespective of its group legal structure.

~~137.173.~~ The parent undertaking may perform its materiality assessment using different approaches. As an illustration, two possible approaches could be:

- a. top-down approach, with an assessment at group level with engagement or consultation with the subsidiaries for specific matters; or
- b. bottom-up approach, involving the subsidiaries and ~~consolidate~~ consolidating the results.

~~138.174.~~ In defining the thresholds (see step C in chapter ~~4~~3.3), the parent undertaking of a large group which operates in different sectors, has to consider an appropriate level of consistency in scoring methodologies and in defining the thresholds (as defined in ESRS 1 chapter 3) ~~across its group.~~ the entire group. An example of a trade-off that an undertaking may face is between a high severity impact from a small revenue stream and a medium severity impact from its main revenue stream; refer to chapter 3.7 deep dive on impact materiality for the criteria to be used.

~~139.175.~~ As part of its initial assessment (see Step A in chapter 4.1), the undertaking can consider impacts, risks and opportunities (or alternatively subtopics) commonly associated with its sectors, geographic locations, or with a specific subsidiary of the undertaking's organisation and define its perimeter. On this regard, the sector-standards will help identifying the impacts, risks and opportunities and subsequently assess them.

FAQ ~~15~~14: Will the implementation of sector-specific standards create any new sub-topics or sub-sub-topics to be considered in the materiality assessment?

~~140~~176. Yes, this could be the case. The sector-specific standards represent another layer built upon the sector-agnostic standards and complement those in terms of depth for a given sub-sub-topic or can, when appropriate, add sub-sub-topics.

~~141~~177. The intention is to achieve a consistent architecture between both sets of standards. The sector specific standards will provide a list and description of sustainability matters (namely at sub-sub-topic level) that are common in the sector and built upon ESRS 1 paragraph AR 16.

~~142~~178. As a temporary measure whilst sector-specific standards have not been adopted, the undertaking shall make use of the Transitional provisions (see ESRS 1 chapter 10.1) related to entity-specific disclosures for material sector-specific matters not covered by a sector-agnostic standards or covered with insufficient granularity. This provision allows undertakings to carry forward sustainability information that it disclosed before adopting ESRS or design additional disclosures using best practice or other frameworks (e.g., IFRS industry-based guidance or GRI), when they prepare the entity-specific disclosure to be included in the sustainability statement following ESRS 1 paragraph 11. It is applicable for the first three sustainability statements of the undertaking.

65.4 FAQ on stakeholder engagement

FAQ ~~16~~15: Do ESRS mandate to actively engage in dialogue with affected stakeholders for the materiality assessment process?

~~stakeholders for reporting purposes?~~

~~143~~179. ESRS require disclosure on the materiality process and its outcome but do not mandate specific behaviour on stakeholder engagement or the broader due diligence process.

~~144~~180. However, ESRS 1 paragraph 45 emphasises states how the impact materiality assessment is informed by the undertaking's due diligence process. In addition, ESRS 1 paragraph 24 points to affected stakeholders' engagement as central to the materiality assessment. Engagement with affected stakeholders is, first, a tool that supports the undertaking's business processes as well as the management of sustainability matters. The undertaking in its preparation of the sustainability statement will be able to leverage the stakeholder's engagement put in place in the context of the due diligence process, if applicable.

~~145~~181. Stakeholder engagement ~~should inform~~informs the identification and assessment of material impacts (see step A in chapter ~~4~~3). It ~~is~~could be generally beneficial if the analysis of the undertaking's actual and potential impacts is mature and granular enough, to result in a meaningful level of engagement when assessing the impacts. This can help ~~in~~with the assessment of the scale and time horizons and also ~~help~~ to ensure the completeness of the material impacts identified.

FAQ ~~17~~16: Should all the categories of stakeholders be considered, or can the undertaking prioritise some of them? for the materiality assessment process?
On which basis?

~~146~~182. ~~Stakeholder engagement~~Engagement with affected stakeholders helps the undertaking to understand which sustainability matters are sources of concern for the respective stakeholders and how they are affected, and this information is useful input to the materiality assessment. ~~The undertaking is not expected to engage or dialogue with stakeholders that are not affected stakeholders for the sustainability matter in question.~~

~~147~~183. ESRS 1 paragraph 22 (a) states: "affected stakeholders: the individuals or groups whose interests are affected or could be affected – positively or negatively – by the undertaking's activities and its direct and indirect business relationships across its value chain". The concept of key stakeholder (or relevant stakeholders in international instruments) rests on the idea that ~~adverse impacts on people or the~~

environment are related to the degree of affection on stakeholders including stakeholders who cannot raise their concerns (also referred to as silent stakeholders, see ESRS 1, paragraph AR 7). not all stakeholders will be affected by all activities of the organisation and the undertaking is to identify the stakeholders whose views are to be taken into account in connection with an activity. It also builds upon the basis that the degree of impact on stakeholders may inform the degree of engagement in terms of prioritisation.

~~148.184.~~ It is not necessary to engage with stakeholders that are not affected but, if not obvious, it might be necessary to haveThe undertaking may consider having a dialogue with stakeholders or representatives to determine whether they are affected or not-, if not obvious.

FAQ 18: How to involve/consult stakeholders?

128.ESRS do not prescribe how to involve/consult stakeholders (including stakeholder who cannot voice their concerns, see FAQ 16 *Do ESRS mandate to actively engage in dialogue with stakeholders?*).

129.AA1000 Stakeholder Engagement Standard⁴⁰ describes possible methods of engagement depending on the level of engagement of the respective stakeholders:

LEVEL OF ENGAGEMENT	POSSIBLE METHODS OF ENGAGEMENT
Remain Passive <i>No active communication</i>	<ul style="list-style-type: none"> • Stakeholder concern expressed through protest • Letters • Media • Websites etc.
Monitor <i>One-way communication: stakeholder to organisation</i>	<ul style="list-style-type: none"> • Media and internet tracking. • Second-hand reports from other stakeholders possibly via targeted interviews.
Advocate <i>One-way communication: organisation to stakeholder</i>	<ul style="list-style-type: none"> • Pressure on regulatory bodies • Other advocacy efforts through social media • Lobbying efforts
Inform <i>One-way communication: organisation to stakeholder, there is no invitation to reply</i>	<ul style="list-style-type: none"> • Bulletins and letters • Brochures • Reports and websites • Speeches, conference and public presentations
Transact <i>Limited two-way engagement: setting and monitoring performance according to terms of contract</i>	<ul style="list-style-type: none"> • 'Public-Private partnerships' • Private Finance Initiatives • Grant making • Cause-related marketing
Consult <i>Limited two-way engagement: organisation asks questions, stakeholders answer</i>	<ul style="list-style-type: none"> • Surveys • Focus groups • Meetings with selected stakeholder/s • Public meetings • Workshops
Negotiate <i>Limited two-way engagement: discuss a specific issue or range of issues with the objective of reaching consensus</i>	<ul style="list-style-type: none"> • Collective bargaining with workers through their trade unions

⁴⁰ Source : https://www.accountability.org/static/940dc017198458fed647f73ad5d47a95/aa1000ses_2015.pdf

<p>Involve Two-way or multi-way engagement: learning on all sides but stakeholders and organisation act independently</p>	<ul style="list-style-type: none"> • Multi-stakeholder forums • Advisory panels • Consensus-building processes • Participatory decision-making processes • Focus groups • Online engagement tools
<p>Collaborate Two-way or multi-way engagement: joint learning, decision making and actions</p>	<ul style="list-style-type: none"> • Joint projects • Joint ventures • Partnerships • Multi-stakeholder initiatives • Online collaborative platforms
<p>Empower New forms of accountability; decisions delegated to stakeholders; stakeholders play a role in shaping organisational agendas</p>	<ul style="list-style-type: none"> • Integration of stakeholders into governance, strategy and operations of the organisation

FAQ 1917: What is the role of silent stakeholders and how to **engage with** consider them?

149.185. There might be stakeholders who cannot voice their concerns. For instance, nature has been identified as a silent stakeholder (see in ESRS 1 paragraph AR 7). Views of silent stakeholders should, however, be considered through the channels that are dedicated to monitor their concerns and therefore are able to provide valuable input to the materiality assessment.

150.186. Examples ~~of~~ to illustrate how to **engage with** consider silent stakeholders could be ~~as~~:

- a. Identifying the silent stakeholders that are likely to be impacted by the undertaking's activities, and consider the actual and potential impacts of the undertaking associated with each of them;
- b. Conducting research to better understand the impacts that affect or could affect these stakeholders through reviewing scientific studies, articles, environmental impact assessments, and other relevant bibliographic documents;
- c. Using proxies such as organisations that are legitimate representatives or are considered by the undertaking to appropriately represent the silent stakeholder. In case of nature, the undertaking may consider, for example carbon footprint analysis, organisations that assess the current and future state of the ecosystem, water footprint analysis, habitat mapping, and soil assessment to estimate the actual resources or climate; and potential impacts of the undertaking on stakeholders; and
- d. Testing the results of the estimated potential impacts based on experts' consultation, collaborative partnership with NGOs, and other stakeholders' engagement.



6.5.5 FAQ on aggregation / disaggregation

FAQ 2018: Does the undertaking use the same level of disaggregation across all the impacts, risks and opportunities?

~~151.~~187. No. The disaggregation of reported information on material impacts should fairly reflect the severity of actual impacts or the severity and likelihood of potential impacts. For risks and opportunities, it should reflect the magnitude of current financial effects and the magnitude and likelihood of anticipated financial effects. ~~The~~In both dimensions, the principle to follow is to avoid obscuring the specificity and context necessary to interpret the information and to avoid aggregating material items that differ in nature as specified by ERS 1 paragraph 54:

“When needed for a proper understanding of its material impacts, risks and opportunities, the undertaking shall disaggregate the reported information:

- a. by country, when there are significant variations of material impacts, risks and opportunities across countries and when presenting the information at a higher level of aggregation (for instance, region) would obscure material information about impacts, risks or opportunities;
- b. or by significant site or by significant asset, when material impacts, risks and opportunities are highly dependent on a specific location or asset,” rather than presenting the information at a higher level of aggregation (for instance, countries).”

~~152.~~188. Where the severity of impacts could be obscured by aggregating data, the undertaking should disaggregate per country, site, asset or subsidiary to meet the qualitative characteristics of information, namely relevance and faithful representation and, in this way, provide the most accurate and truthful representation when disclosing the severity of the related impact. The question of how data should be disaggregated should focus on the specific facts and circumstances of the undertaking where the actual or potential negative impacts occur. Hence, there are situations whereby the undertaking adopts a different level of disaggregation for two separate sustainability matters within the same topic (e.g., own workforce ~~for~~ adequate wages and training and development) and this would be appropriate.

~~189.~~ For risks and opportunity, the focus is on whether the aggregation could obscure information that could have an influence on the investor’s decisions to provide funds to the undertaking.

~~153.~~190. As described in ERS 1 para 55, ~~in preparing the disclosure~~ disclosures in the undertakings sustainability statement i shall consider the level of disaggregation adopted in its materiality assessment. ~~Examples:~~

~~130.~~For example, for water usage a criterion for disaggregation could be based on the vulnerability to water-stress by geographical area or site. However, in the case of collective bargaining, disaggregation at country level is more appropriate, as laws and regulations and labour market practices vary at that level.

~~131.~~An undertaking in the garment industry manufactures in its subsidiaries in different countries where decent working conditions and adequate wages are not a particular pertinent challenge. However, if there is

Examples

- When reporting on impacts relating to water usage a criterion for disaggregation could be based on the vulnerability to water-stress by geographical area or, if appropriate, site.
- Child labour impacts whose severity can depend on country specific laws and regulations and labour market practices; therefore, country level disaggregation could be the criterion.
- An undertaking in the garment industry manufacturing has subsidiaries in different countries and adequate wages and collective bargaining have not been considered material impacts overall. However, there is one country, where its subsidiary with 15% of its workforce does pay below the adequate wages for the country and collective bargaining agreements do not take place, the materiality assessment should consider that level of disaggregation at country to identify material negative impact. Similar disaggregation might be considered for an undertaking that has production sites in different countries or regions for impacts related to pollution or doing business in countries where higher risks of corruption and bribery are observed compared to others.

~~one site, for example in a country, where its subsidiary does pay below the adequate wages for the country, the materiality assessment should be performed at that level of disaggregation to identify material negative impact. Similar disaggregation might be necessary for an undertaking that has production sites in different countries or regions for impacts related to pollution or doing business in countries where higher risks of corruption and bribery are observed compared to others.~~

FAQ ~~21~~19: Is an IFRS or local GAAP segment an appropriate level of disaggregation for the materiality assessment?

~~154.191.~~ 154.191. In general no. The purpose of the disaggregation objectives for financial reporting and sustainability reporting are not different (also refer to FAQ 5 “Is materiality for financial statements and management commentary the same as financial materiality for the sustainability statements?” and FAQ 6 “Is financial materiality for sustainability reporting limited to effects presented in terms of content or time horizons financial statements?”). In general, the sector classification of the undertaking’s activities is more appropriate as a starting point (refer to ESRS 2 IRO 1 paragraph 53 (b) (i)).

Example

A multinational group that prepares consolidated accounts bases its segments for financial reporting on products and services offered worldwide. When performing its sustainability materiality assessment on water, the undertaking determines that the material negative impacts are correlated to the levels of water stress in the geographical areas where the factories are located. Therefore, it identifies that the disaggregation is to be performed at geographical level and conclude that the financial reporting segments are not appropriate.

~~155.192.~~ 155.192. Segment reporting under IFRS or local GAAP is based on a “management approach” (as defined in the IFRS) or based on another approach as the case might be for the segment reporting required under local GAAP. The criterion for financial reporting segmentation groups business activities or, in some cases, subsidiaries into segments that are as much as possible homogenous within the segment and non-homogenous as compared to the remaining segments ~~from a financial reporting perspective.~~ The level of disaggregation or reportable segments are consistently applied in the financial reporting without variation between the different reported items.

~~156.193.~~ 156.193. The disaggregation for financial reporting segments is designed for a different purpose and, in general, it is not appropriate to reflect the significant material impacts, risks and opportunities across the undertaking. The appropriate disaggregation unit may be a country, site, or significant asset when material impacts, risks and opportunities are linked to arise in a specific country, specific location or asset. In addition, the level of disaggregation should reflect the nature of the different sub-topics and, and as such, should be adjusted from one sub-topic to another when this is necessary to properly portray the material impacts, risks and opportunities (see ESRS 1 paragraph 54).

~~157.194.~~ 157.194. Therefore, a disaggregation following the segments used for financial reporting may not be granular enough or relevant for sustainability reporting¹¹.

Example:

~~132. A multinational group that prepares consolidated accounts has established that its segment reporting for financial reporting is based on products and services offered worldwide.~~

~~133. When performing its sustainability materiality assessment on the environmental topic of water, the undertaking determines that the material negative impacts are correlated to the levels of water stress in the geographical areas where the factories are located. Therefore, it identifies that the disaggregation is to be performed at geographical level and conclude that the financial reporting segments are not appropriate.~~

¹¹ ESRS 1 SBM 1 requires the identification of the ESRS sectors in which the undertaking operates (ESRS 2 paragraph b) and c)) and requires to disclose the revenues by ESRS sectors. EFRAG will consult in the last quarter of 2023 or in 2024 on a proposed ESRS sector classification. However, the undertaking has to determine the necessary level of disaggregation of its disclosure following chapter 3.7 of ESRS 1 and cannot assume that the ESRS sector disaggregation is appropriate for all the disclosures.

5.6 ~~6~~ FAQ on reporting

FAQ ~~220~~: Do ESRS require to disclose respectively severity, scale, scope, and irreparable character of material impacts, respectively and likelihood of occurrence and potential magnitude of material risks and opportunities?

~~158.195.~~ No. ESRS do not require to disclose ~~these the detailed outcome for each criterion, however an appropriate explanation of criteria in the undertaking's sustainability statement and thresholds used is expected.~~ The undertaking has to report on the processes to identify and assess material impacts, risks and opportunities as required by ESRS 2 IRO-1 and on the outcome as required by ESRS 2 SBM-3 and IRO-2. However, ESRS 2 SBM 3 Paragraph 48 (g) requires disclosure on changes to the material impacts, risks and opportunities since the prior year. For instance, the scale and irreparable character of a negative impact could have been assessed as high in the current period versus medium in the prior year and, hence, this negative impact became material and such information is to be disclosed.

~~159.196.~~ As reported in FAQ 13 *Should the materiality assessment be documented/evidenced? And, if so, how?*^{7,8} ESRS do not prescribe a specific documentation, however it is reasonable to expect a certain level of documentation to be produced for internal purposes and for the auditors within the assurance engagement on the undertaking's sustainability statement.

~~160.197.~~ ~~The necessary~~Such documentation can also include a description of respectively severity, scale, scope, and irreparable character of material impacts, respectively and likelihood of occurrence and potential magnitude of material risks and opportunities. This documentation can help the undertaking's management and the auditor (i.e., as ~~an~~ audit evidence) to better understand the materiality assessment process and the related results.

FAQ ~~231~~: If a matter is material from the financial (or impact) perspective only, shall disclosures cover all the requirements, or only information about financial (or impact) materiality?

~~134.~~Information aboutThe determination of information to be reported for metrics is informed by the assessment of material information to disclose (refer to chapter 2.3). Hence, information disclosed on metrics may be limited to information that is relevant either under the financial (or impact) materiality perspective only when the undertaking decides to omit disclosure requirements or and those datapoints that it has assessed to be do not material⁸.

2024 on a proposed ESRS sector classification. However, relate to the undertaking has to determine the necessary level of disaggregation of its disclosure following chapter 3.7 of ESRS 1 and cannot assume that the ESRS sector disaggregation is appropriate for all the disclosures.

~~161.198.~~ ⁸ A datapoint of a Disclosure Requirement in metrics may be material impact or risk and opportunity are omitted when the corresponding information is assessed to be not material provided that the omitted information is not needed to meet the objective of the Disclosure Requirement (ESRS 1 paragraph 34).¹²

~~162.199.~~ When a matter is assessed to be material from the financial (or impact) perspective only:

- a. ~~the~~ information about policies, actions and targets shall cover all the datapoints in the minimum disclosure ~~requirements~~⁹requirements¹³ and the topical standards (ESRS 1 paragraph 33). The level of detail of such information (as in general for narrative information) will reflect the general

¹² A datapoint of a Disclosure Requirement in metrics may be omitted when the corresponding information is assessed to be not material provided that the omitted information is not needed to meet the objective of the Disclosure Requirement (ESRS 1 paragraph 34).

¹³ See ESRS 2 chapter 4.2 *Minimum Disclosure Requirements on policies and actions* and *Minimum Disclosure Requirements on targets in chapter 5 Metrics and targets.*

approach to information materiality (ESRS 1 paragraph 31) but the reported information should not be limited to financial or impact perspective only; and

- b. ~~b.~~ the information about metrics will reflect the assessment of materiality of the information required by the corresponding requirements in the topical standards (ESRS 1 paragraph 34), which is performed adopting the criteria in ESRS 1 paragraph 31. In such assessment, the undertaking considers the capacity of the information to meet the users' decision-making needs and may conclude that a disclosure requirement or a datapoint is not material, and therefore omit it. Accordingly, it might be the case that for a matter material from the financial (or impact) perspective only, the undertaking may conclude that a metrics related to the impact (or financial) perspective only can be omitted.

~~163.200.~~ It is also important to note that impact information disclosure that informs about actual or potential impacts is of interest for investors when a matter is financially material. Similarly, financial information is also relevant for other stakeholders other than investors when a matter is material from the impact perspective, as it supports accountability.

FAQ ~~2422~~: Is a group active in different sectors required to include data for the entire group in the metrics or only data for the entities/sectors of the group related to the material impact, risk or opportunity?

~~164.201.~~ Once metrics have been assessed for materiality and the conclusion is that the metric is to be disclosed, the data for the entire group shall be included in the metrics, ~~it~~ except for when specified differently in sector-agnostic topical or sector-specific standards (refer to the example below).

~~165.202.~~ ESRS 1 stipulates that the sustainability statement shall be for the same reporting undertaking as the financial statements (ESRS 1 paragraph 62). If the undertaking prepares consolidated financial statements, the reporting entity is the entire group. For the assessment of material impacts, risks and opportunities, ESRS 1 clarifies that it is performed "for the entire consolidated group, regardless of its group legal structure" (ESRS 1 paragraph 102). The group legal structure is also irrelevant for reporting on metrics, as it cannot make a difference whether an undertaking is doing its business activities using multiple legal entities as a group or is organised doing the same business activities using only one legal entity.

~~166.203.~~ However, ESRS 1 also stipulates that, "(w)hen a topical or sector-specific ESRS requires that a specific level of disaggregation is adopted in preparing a specific item of information, the requirements in the topical or sector-specific ESRS shall prevail" (ESRS 1 paragraph 57). Therefore, undertakings can disaggregate the metric information further rather than at group level.

~~135.~~ Disclosure regarding impact, risk and opportunity management related to policies, actions and targets will reflect the extent of the activities within the group that are covered by those policies, actions and targets. As such, they may only cover the "problem area" of the material impact, risk and opportunity, when appropriate.

~~167.204.~~ ⁹ See ESRS 2 chapter 4.2 *Minimum Disclosure Requirements on policies and actions* and *Minimum Disclosure Requirements on targets* in chapter 5 *Metrics and targets*. Likewise for entity-specific metrics, the metric could be focussed on the parts of the group where such material impact, risk or opportunity arises.

~~168.205.~~ In addition, ESRS 1 also stipulates for the level of disaggregation that "when needed for a proper understanding of its material impacts, risks and opportunities, the undertaking shall disaggregate the reported information ..." (ESRS 1 paragraph 54).

Example:

~~169.206.~~ Assume Group is active in sector A and B, respectively with two subsidiaries, A and B. Group has a material impact, risk or opportunity in relation to water consumption. However, the impact, risk or opportunity is only material for sector A, respectively subsidiary A.

~~170.207.~~ ESRS E3-4 requires that:

- a. total water consumption in m³ is disclosed for own operations, so this shall be for the entire Group (ESRS E3 paragraph 28 (a), same for paragraph 28 (c) total water recycled and reused and paragraph 28 (d) total water stored and changes in the storage); and
- b. total water consumption in areas at water risks (ESRS E3 paragraph 28 (b)) would ~~depending~~depend on the areas at water risks only relate to sector A, respectively subsidiary A.

~~171.208.~~ According to ESRS E3-1, the undertaking shall describe its policies that address the management of its material impacts, risks and opportunities related to water and marine resources. As water consumption is only material for sector A, subsidiary A will have put in place appropriate policies and the disclosure would cover them. Similarly, it would be appropriate to only disclose on actions and targets for sector A, respectively subsidiary A, if actions are taken and targets are set at that level.

FAQ ~~25~~23: When an undertaking has already put in place actions to avoid, minimise, mitigate or rehabilitate environmental impacts, shall it nevertheless report on the impacts before those actions? SUBJECT TO REDRAFTING

~~209.~~ Yes. The undertaking has This will depend on the specific facts and circumstances of the undertaking as well as the negative impact. Two categories to ~~report~~ be considered carefully, are:

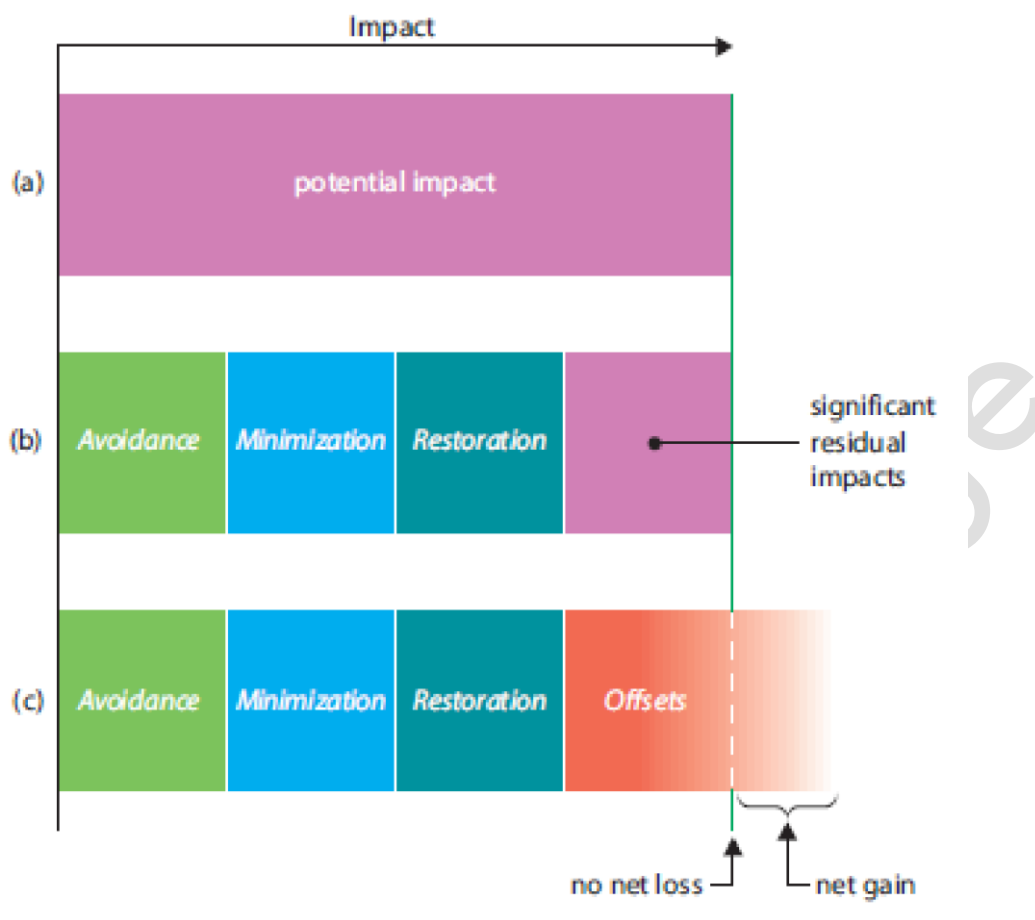
- a. the time dimension that distinguishes between the period when the activity had not started and when it is ongoing; and
- b. the likelihood of occurrence of uncertain events.

~~136.~~ These categories give rise to four potential scenarios which are further illustrated below with the example of an undertaking's decision of building a chemical plant. In all scenarios, the undertaking shall disclose the material negative impact irrespective of the actions implemented to avoid, minimize, mitigate or rehabilitate it (see point (a) in. Given that policies, actions and targets (or the figure below).

~~172.210.~~ In addition ~~lack of them) are to be disclosed for material impacts, the undertaking can include a description of~~ shall describe the actions taken (according to the mitigation hierarchy) and can provide information on the effects on the impact in terms of severity and likelihood.

Figure 6: Impacts, residual impacts and net loss/gain¹⁴

¹⁴Source: A cross-sector guide for implementing the Mitigation Hierarchy – Cross Sector Biodiversity Initiative (CSBI) pg. 12).



137. As defined by the CSBI (CSBI, 2013a), the mitigation hierarchy is:

- a. “the sequence of actions to anticipate and avoid impacts on biodiversity and ecosystem services; and
- b. where avoidance is not possible, minimize, and,
- c. when impacts occur, rehabilitate, or restore, and
- d. where significant residual impacts remain, offset.”

138. Restoration and offsetting actions begin once impacts have already occurred. In these cases, the undertaking has nevertheless to report on the impacts before those actions, describing the concrete effects of the actions on the impacts.

Examples:

139. An undertaking active in the mining sector has planned to open a new site in a region with valuable natural habitats for some species protected under national laws. The undertaking worked with biodiversity experts to evaluate the potential impacts of its planned activity in this region. The analysis identified areas where the undertaking activity can create material negative potential impacts on biodiversity. The undertaking has identified areas where it needs

to avoid future development and areas where efforts to mitigate impacts on species and habitats can have the greatest benefits. Based on this information, the undertaking has defined the Wildlife Mitigation Plan to preserve existing habitats and to offset any loss of habitat by taking steps to restore or enhance habitat conditions nearby. When defining its sustainability statement, the undertaking has to disclose its material potential negative impact on biodiversity, adding information on the actions implemented to avoid and mitigate it (i.e. describing its Wildlife Mitigation Plan).

140. An undertaking active in the oil & gas sector has a big onshore oil field in a biodiversity-rich area. Low-intensity mixed farming is the main land use on the valley bottom and lower slopes, giving way to natural grassland, woodland and rocky habitats at higher elevations. The onshore oil field construction has caused important effects on biodiversity, in particular on forest and upland grassland, with implication also on the farming activities. The outcome was a targeted biodiversity action plan for impact restoration and long-term monitoring, which has been implemented in the site. Several key approaches were adopted to restore pipeline and flowline disturbances: 1) directly re-seeding with locally sourced seeds; 2) spreading seed-rich grass cuttings from the undisturbed area. The monitoring activity showed that the prairies had recovered their original structure, composition and ecological functions, without any increase in non-native species. In this case the undertaking has nevertheless report on the impacts caused by the oil field on biodiversity before the restoration activities, describing the results obtained through the aforementioned actions.
211. **Stage 1 – impact assessment stage:** The undertaking is considering whether or not to build the chemical plant. The undertaking has made an impact assessment which identifies and assesses the impacts. Some of these impacts are permanent and other temporary and some impacts are certain and other uncertain. In this example, the impacts relate to the volume of pollutants emitted to water from a certain activity. The recommendations from the impact assessment are the use of a certain production technology (pollution prevention, a form of minimization) and the use of a wastewater treatment plant ('WWTP') (minimization) to achieve final emissions at the discharge point compliant with Best Available Technology reference levels.
212. Furthermore, the impact assessment has concluded that due to the volume of water which will be withdrawn from a local river and discharged back to it, there will be severe hydrological impacts. Hence, the undertaking should withdraw water downstream from where it discharges it, and it should implement special restoration measures in the river section between discharge and withdrawal.
213. At this point, the undertaking still has all four steps of the mitigation hierarchy available: 1) it can build the plant or not; 2) it can mitigate it by implementing BAT; 3) it can decide on which restoration measures to apply or not; and 4) it can decide on implementation of certain offsetting measures. From a reporting standpoint, if the (potential) impacts are considered material, the undertaking shall disclose both the (potential) unmitigated impacts, together with its mitigation measures (i.e., actions in ESRS language) and the expected final (potential) impact because of the actions planned or undertaken. If the undertaking decides not to advance with the project, the negative impacts described in this paragraph would not have taken place and no reporting would be performed.
214. **Stage 2 – impact mitigation stage:** The undertaking decided to advance with the project and has built the plant. This decision leads to a number of impacts, which the undertaking shall disclose from both a mitigated and unmitigated perspective. Specifically, during the first year of operations of the plant, the undertaking discloses both the potential impact of pollution in case that no WWTP exists or of its breakdown or malfunction; and its actual pollutant emissions to water after the WWTP. After that first year of plant operations, the undertaking shall only report on its emissions.
215. In this example, the undertaking also reports on the impacts caused by the construction of the chemical plant on the river in the first year; the effects of the increase of water pollutants at that cross-section of the river, any restoration measures being implemented and any offsetting measures it is taking. This phase is the start of the reporting on business-as-usual activities of the plant and when the undertaking is implementing its impact mitigation strategy – minimizing pollution, restoring ecosystems and offsetting where needed.
216. **Stage 3 – risk management stage:** This business-as-usual activity phase, the undertaking acknowledges that uncertain events may cause impacts. Through its risk management process, the undertaking has identified the following critical risks to its operations: a breakdown of its chemical storage tanks and leak of its chemical products into the local river; the accidental release of untreated wastewater; risk of flooding affecting its production facility. For the potential negative impacts assessed as material following the impact materiality criteria established in chapter 3 of this guidance, the undertaking shall report its unmitigated impacts, as well as mitigation measures in place (i.e., actions).
217. **Stage 4 – impact remediation stage:** In case one of the risks detailed in the paragraph above crystallises and become a material actual impact, the undertaking shall report the unmitigated impact in

the year such accident occurs together with any actions taken (i.e., remediation efforts). In subsequent years, if the impact is still assessed as material, it shall report the impact together with its on-going remediation activities that minimises its effects and restoring the environment to its previous conditions.

218. To summarise the key considerations illustrated in the example above:

- Impact assessment stage: disclosure of unmitigated material impacts of projects and mitigation measures;
- Impact mitigation stage: disclosure of material unmitigated material impacts in the first year of operations as well as material mitigated impacts; report only mitigated effects in the following years;
- Risk management stage: report unmitigated material impacts (gross risk), as well as risk management actions in place;
- Impact remediation: if risk materializes, report unmitigated impact in first year and on-going remediation efforts. In subsequent years, material mitigated impacts subsisting, as well as remediation activities.

FAQ ~~26~~24: Shall the undertaking report also on material matters that have not been managed and/or for which there are no actions?

~~173-219.~~ Yes. The materiality assessment is performed by the undertaking to identify the material impacts, risks and opportunities to be reported, which are classified into ESGsustainability topics, subtopicsub-topics or sub-sub-topics (also referred as “matters”).

~~174-220.~~ ESRS 1 paragraph 33 establishes that for the material impacts, risks or opportunities identified, the undertaking is to disclose its policies, actions and targets to manage those. And it specifies that if the undertaking has not implemented a policy, action or target, this fact is to be disclosed. The requirements of information to be disclosed for policies, actions and targets are detailed in ESRS 2 chapter 4.2 and 5.

Example

A hotel has identified the lack of training and development on health and safety as a material impact. However, it does not have a formal training policy or actions related to this matter. In this case, health and safety training is a material matter which is disclosed by the undertaking together with the fact that there are no policies or actions at the end of the reporting year. The undertaking may disclose that they are working on drafting and implementing such policies and actions in the future.

Example:

~~141.~~ An undertaking in the hotel services sector has identified training and development on health and safety as a material impact. However, it does not have a formal training policy or actions related to this matter. In this case, health and safety training is a material matter which is disclosed by the undertaking together with the fact that there are no policies or actions at the end of the reporting year, but the undertaking may disclose that they are working on drafting and implementing such policies and actions in the future.

FAQ 27: Is there a recommended format or matrix to graphically present the material matters?

~~142.~~ ESRS do not mandate a specific format or matrix to present or visualise the material matters. Given the wide scope of ESRS 2 SBM 3, which lays out the general requirements of reporting on material impacts, risks, and opportunities, it may be feasible to present only certain aspects of these requirements in a visual matrix.

~~143.~~ The following approaches are examples of possible formats of visualisation, each highlighting certain aspects of the double materiality assessment:

- a. a graph that presents “impact materiality” on one axis and “financial materiality” on the other axis, thereby outlining for each material matters its weight for the two dimensions of double materiality;
- b. going a step further, a more detailed option may be to use two separate graphs for (1) impact materiality and (2) financial materiality and present material matters according to “IRO Timeline” (on the x-axis) and “Magnitude of IRO” (y-axis), thus incorporating time horizons to the visualisation;

- c. ~~same as in b, but with a single graph that combines the outcome of the two perspectives (impact and financial materiality) in a single graph;~~
- d. ~~a graph that portrays “Likelihood of IRO” on the x-axis and the “Magnitude of IRO” on the y-axis. This graph may also visualize a threshold that will position material matters above a certain cut-off point (easily displayed by a line, or by the upper corner of the graph); and~~
- e. ~~tables are also a way to present the many disclosures required for each material matters. Pictograms can be used in the different columns of the table to help visualize the information (e.g. where the impacts / risk is concentrated in the value chain, whether the matter is financially material, material from the impact perspective, or both,);~~

~~144. To provide a more comprehensive overview of the outcome of the double materiality assessment, it is also possible to use several different visualisations.~~

5.7 FAQ on Art. 8 EU Taxonomy



FAQ 25: What is the relationship between taxonomy eligible activities and materiality? SUBJECT TO ENHANCEMENTS

221. The EU Taxonomy Regulation and its Delegated Acts define criteria for a number of economic activities (eligible activities) that need to be fulfilled in order to substantially contribute to one of six environmental objectives. In addition, these activities must do no significant harm (DNSH) to the other environmental objectives and fulfil minimum social safeguards to be considered taxonomy aligned. The environmental objectives of the Taxonomy Regulation are fully reflected in the environmental topics covered by the ESRS.
222. If an undertaking engages in activities that are eligible for the EU Taxonomy, this indicates that it impacts the environmental objective for which the Taxonomy defines substantial contribution. This gives rise to three scenarios:
- a. If the activity complies with the criteria for substantial contribution, this indicates a reduced or even positive impact on the respective environmental objective;
 - b. If the activity does not comply with the substantial contribution criteria but the undertaking has a Capex plan to comply in future, this indicates a reduced negative or positive impact and may be a source of opportunity for the undertaking.
 - c. If the activity does not comply with the substantial contribution criteria and has no Capex plan to do so, this provides an indication of a negative impact on the respective environmental objective, and an associated risk.
223. When an undertaking with taxonomy eligible activities does not comply with one or more of the DNSH criteria, there is a strong indication that it has negative impacts on the respective environmental objective to which the non-compliant DNSH criteria relate, which may also translate into material risks for the undertaking. If the activity complies with the DNSH criteria, negative impacts may still occur and require consideration.
224. Activity-based Capex invested by the undertaking in the reporting year is also an indicator of its risks and opportunities, regardless of whether the activities are eligible from a revenue perspective. Disclosing the Capex plans, and how they fit within the undertaking's wider transition plan, which may lead to changes to the undertaking's strategy, business model or creation of a new revenue stream can be information that is considered material for primary users of general-purpose financial reports (i.e., investors of the undertaking).
225. As an example, an undertaking in the energy sector where its current activities are not covered by the taxonomy delegated acts. The undertaking could be investing in renewable energy as part of a Capex plan to provide renewable energy to its customers by creating a new revenue stream and such information could be financially material.
226. The undertaking is expected to consider this in its materiality assessment when identifying actual and potential impacts, risks and opportunities and related sustainability matters for the materiality assessment, refer to chapter 3.2 (step B) of this Guidance. Engaging in taxonomy eligible activities, for those undertakings under the scope of Art 8 Taxonomy, can trigger the need to apply the respective topical ESRS and report on the positive or negative environmental impacts and associated risks and opportunities. In turn, however, an undertaking cannot preclude that taxonomy alignment in terms of substantial contribution and complying with DNSH criteria implies that it has no actual or potential impacts or risks in relation to the respective environmental topics. Such triggers are inputs to the double materiality assessment that the undertaking has to perform.
- Example of an undertaking constructing new buildings
227. An undertaking constructs new buildings which is a Taxonomy eligible activity. The substantial contribution criteria (SC criteria) for the Climate Change Mitigation (CCM) objective set taxonomy-related thresholds for, among others, the Primary Energy Demand (PED) of the building. If the new buildings fulfil the SC criteria, the economic activity has a reduced negative impact or even positive. If they do not comply with the SC criteria, the impact on the SC objective can be reduced or be positive with a capex plan and could become an opportunity. Without the Capex plan, the impact would instead be either actual or potential negative on the SC objective. Either way, the impact of the activity on the SC objective

should be included in the list of potential impacts and the opportunity should be included in the list of potential material opportunities in the materiality assessment for ESRS E1.

228. Further, the DNSH criteria for the Biodiversity objective (BIO) require the new building not to be constructed on certain types of land. As this new building is built on arable land, the building does not comply with the DNSH criteria for the BIO objective. The activity therefore has an actual negative impact on biodiversity. This impact should be included in the list of potential impacts in the materiality assessment for ESRS E4.

Example of a manufacturer of electrical equipment

229. An undertaking manufactures high, medium, and low voltage electrical equipment for electrical transmission and distribution, which is a Taxonomy eligible activity. As an enabling activity, the SC criteria for the Climate Change Mitigation (CCM) objective set taxonomy-related requirements, among others, for low voltage circuit breakers, switchgears, switchboards, panel boards to meet certain energy efficiency standards. The undertaking does not comply with these requirements. As the manufacturing of high, medium, and low voltage electrical equipment is an enabling activity, it cannot automatically be assumed that the activity has potential or actual negative impact on the SC objective. The undertaking needs to conduct its materiality assessment.

230. The DNSH criteria for the Pollution Prevention and Control (PPC) objective for this activity require the undertaking to comply with all elements of Appendix C. As the activity fails to comply with one of the requirements in Appendix C, the undertaking may have potential or actual negative impact on the PPC objective, that has to be included in the list of potential impacts in the materiality assessment of ESRS E2.

Subject to change

