**Materiality guidance**

**Summary**

**Chapter 1: Introduction**

**Chapter 2: The ESRS approach to materiality**

**Chapter 3: How is the materiality assessment performed?**

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| Comment ID | #1 |
| Section | 3. How is the materiality assessment performed? |
| Specific paragraph/sentence | §64; *Figure 3* |
| Comment | In the example outlined on §64, **we would like to highlight risks relating to step B.**  As described in the section 3.2, the outcome of step B is a ‘long list’ of IROs that are to be assessed further (step C). When screening the list provided in ESRS 1 §AR 16 (and adding entity and sector specific matters), the undertaking shall consider all parts of its value chain. From our interpretation of the guidance, matters can **already be ‘excluded’ from the list during this stage, simply based on an assumption that they do not apply to the undertaking’s business model.** We understand, that such matters would then not have to be assessed further in step C.  We wonder whether undertakings adopting such an approach might **accidentally exclude important matters from the assessment too early on.** We find that sometimes, impacts and their connection to the value chain might not be obvious at first, and might only come to the surface once they have been assessed in more detail. How does EFRAG view this pitfall?  With our clients, we **mitigate this risk by rigorously scoring every sustainability matter on the list provided in ESRS 1 §AR 16 (along with entity and sector specific matters).**In other words, we skip step B entirely, and use step C to determine which topics are material to the undertaking and which are not. This way, we can be sure than no topics are accidentally excluded. |

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| Comment ID | #2 |
| Section | 3.3.1 Impact materiality assessment |
| Specific paragraph/sentence | Applicable to the entire section |
| Comment | From the guidance it remains **unclear how to approach a sustainability matter that has both negative and a positive impacts. Should in a case like this both sides be assessed separately?** This comment applies particularly to **potential** sustainability matters, which could oftentimes be viewed from both angles.    For instance, in the example of diversity, there might a potential negative impact in the short- or medium-term, should an undertaking not be able to perform on their diversity-related initiatives and goals during within that time period. However, a positive impact might be achieved in the long-term through progress on these same initiatives and goals.    Some clarification on how to approach this (as has been done – although only briefly – for risks/opportunities in the following section on financial materiality, §93) would be helpful. |

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| Comment ID | #3 |
| Section | 3.3.1 Impact materiality assessment |
| Specific paragraph/sentence | §84: *"For example, when there is an established scientific consensus about the severity of a particular kind of global and localised environmental impact, the undertaking can conclude that it is, indeed, material without an in-depth analysis of scale, scope and irremediability."* |
| Comment | The guidance currently leaves a **lot of room for interpretation** here. It raises i.e. the following questions:    1) If one can conclude that topics as mentioned in the example above are material without an in-depth severity scoring, what implications would this have for the **overall consistency of the assessment?** If other topics are assigned a granular materiality score (based on the severity + likelihood parameters), the approach suggested in §84 would make it more difficult to further sort, compare, or prioritise material topics, if some of them have not received a proper score. Or, does §84 simply mean that such topics would still be assigned a score according to the established thresholds for severity and likelihood, but that the rationale part could be kept shorter (e.g. just with a reference to an industry assessment as described below)?    2) Does this mean that one could use **industry research conducted by reputable sources as a basis for the entire impact assessment of material topics in the value chain**, particularly in cases where there is no entity-specific data (e.g. from suppliers) available yet? Would it be sufficient to use e.g. the SASB Industry Research Briefs (<https://sasb.org/standards/archive/>) as one of the main contributing sources to determining material impacts in the VC? |

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| Comment ID | #4 |
| Section | 3.3.2 Financial materiality assessment |
| Specific paragraph/sentence | §87: *"To assess their materiality, appropriate quantitative and/or qualitative thresholds based upon financial effects in terms of performance, financial position, cash flows, access to and cost of capital are used."* |
| Comment | The **wording of this sentence is slightly misleading**, as it implies that all of the parameters shall be used to determine the financial magnitude. Based on our understanding, it is up to the undertaking to select the parameters, and as such, the guidance should make clear that the parameters stated above are only examples. |

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| Comment ID | #5 |
| Section | 3.3.2 Financial materiality assessment |
| Specific paragraph/sentence | §88: *"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."* |
| Comment | The **wording of this sentence is slightly misleading**, as it implies that the likelihood and potential magnitude needs to be evaluated three separate times; once for each of the three time horizons. |

**Chapter 4: How to leverage other sources?**

**Chapter 5.1: FAQs on impact materiality**

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| Comment ID | #6 |
| Section | FAQ 2: What is meant by the undertaking being “connected” with an impact? |
| Specific paragraph/sentence | §149: *"The type of involvement (i.e. directly caused, contributed to or directly linked) is important given that it could lead to a different assessment or categorisation of the negative impact."* |
| Comment | The guidance **lacks clarification** on how to integrate this aspect into the scoring. Does it **imply, that if an undertaking "directly causes" an impact, it could be assigned a higher score (thereby ranking "more material") than if the undertaking was only "directly linked" with the very same impact?** If so, does this not **contradict the statements on leverage** within the Value Chain Implementation Guidance (see VC IG §29-31: "*In some cases, an undertaking may have leverage or be able to exert influence over actors in its VC. Examples include where the undertaking is a large supplier or customer and so exert influence on the business relationships to manage its impacts. In other cases, its ability to obtain the necessary VC information as well as its capacity to contribute to or influence the management of IROs arising in the VC, may be limited given the nature or the absence of direct contractual arrangements, the level of control that it exercises on the operations outside the consolidation scope and its buying power. However, leverage does not affect whether IROs that arise in the VC are material or not.")* |

**Chapter 5.2: FAQs on financial materiality**

**Chapter 5.3: FAQs on the materiality assessment process**

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| Comment ID | #7 |
| Section | FAQ 9 |
| Specific paragraph/sentence | §167: *"Also, materiality thresholds might be affected by the time horizon."* |
| Comment | Does this imply, that **time horizons do not *have* to be integrated into the more concrete scoring thresholds**, but that they nonetheless can serve as valuable information for the assessment (as demonstrated in examples 1 and 2 of the FAQ9)? A clarification of whether this holds true would add to the section. |

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| Comment ID | #8 |
| Section | FAQ 9 |
| Specific paragraph/sentence | *Examples 1 and 2* |
| Comment | Furthermore, the case of **sustainability matters that cannot be assigned a time horizon have not been addressed in the guidance.** For instance, health and safety, violence and harassment, and other social topics might always be at risk of having some negative impacts on the workforce, as it could be argued they can never be fully eliminated. For instance, even with the best health and safety measures in place, an accident could occur. With impacts/risks that are continuously present, it becomes difficult to categorize them into long- medium-, or short-term. From the guidance, it is unclear how the time horizon of such topics should be treated. |

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| Comment ID | #9 |
| Section | FAQ 9 |
| Specific paragraph/sentence | Applicable to the entire section |
| Comment | It should be **stated more clearly that time horizons only apply for potential impacts** (as well as the risks/opportunities angle), as actual impacts are those that have already occurred in the reporting period or in the past (but that due to long-term effects remain material for a number of years). It is briefly mentioned in §83 for impact materiality, and §88 for financial materiality, but it would be recommendable to clearly restate it in FAQ9. |

**Chapter 5.4: FAQs on stakeholder engagement**

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| Comment ID | #10 |
| Section | 5.4 FAQs on stakeholder engagement |
| Specific paragraph/sentence | Applicable to the entire chapter |
| Comment | Our clients often wonder **how many external stakeholders should be engaged with** and how much input should be sought on a minimum; a concern further amplified due differing interpretations of the matter among auditors.  While we recognize that what could be viewed as “sufficient” stakeholder engagement varies widely across organisations, it would be helpful if this point was addressed in the guidance, given that it is a frequently occurring topic. Although the ESRS does not directly mandate stakeholder engagement, we see that it might be helpful for EFRAG to formulate some guidance on best practices, for instance that ideally, the views of every affected stakeholder group should be represented in one way or another. |

**Chapter 5.5: FAQs on aggregation/disaggregation**

**Chapter 5.6: FAQs on reporting**

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| Comment ID | #11 |
| Section | FAQ 23 |
| Specific paragraph/sentence | §215: *"Therefore, the users of the sustainability statement will receive information on the actual impacts where no distinction is made between gross and net."* |
| Comment | If that is the case and any type of netting / future remediation measures should not be factored into the assessment of actual impacts, it becomes **unclear what purpose the impact parameter of "irremediable character" serves.** From §217, one might assume that it is only past mitigation activities, but not future ones, that should be factored in here. However, the guidance should specify this further. |

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| Comment ID | #12 |
| Section | FAQ 23 |
| Specific paragraph/sentence | §217 a): "*Any remediation or rehabilitation activities put in place*  *after the event but in the same period is not taken into account in the materiality assessment."*    *§217 b) "For severe negative impacts in the past, these are expected to be considered in the materiality assessment and assessed whether still material in the current reporting period. In this example of the oil spill, aquatic and coastal ecosystems may be materially negatively affected by oil pollution for many years and remain in the materiality assessment for a number of years."* |
| Comment | It remains **unclear on how to approach actual impacts that have occurred in the past, but where mitigating factors have been put in place afterwards**, which subsequently have lessened the negative impact in the years following the occurrence of the impact. Paragraph §217 b) simply states that severe impacts should be considered in the assessment for a number of years, but not how. Should a negative impact that has occurred in the past be assessed according to its gross impact, even if mitigating actions (e.g. in the form of a clean up) have been put in place after?  Furthermore, the guidance does not specify what should serve as the **basis for determining the number of years an impact should remain in the materiality assessment.** |

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| Comment ID | #13 |
| Section | FAQ 23 |
| Specific paragraph/sentence | §215: "*And, for potential impacts the following applies: (a) information on the gross impact (i.e., before taking into account the mitigation hierarchy); (b) the management of such impacts (i.e., policies, actions and targets); and (c) understanding the net impact (i.e., after the application of the mitigation hierarchy)."*    §218: *"The materiality assessment of potential impacts can also consider the effect of technical or other management measures for avoiding or mitigating impacts in the future."* |
| Comment | While it is stated that information on both 1) gross impact, 2) management of the impact, and 3) net impact shall be disclosed, it **remains unclear whether the final materiality score should be determined based on a gross or net basis (paragraph §218 suggests the latter), when the impact is potential.**    Furthermore, this section raises the question of **whether the way in which an impact is managed should be factored into the materiality thresholds and scoring**, for instance by making an impact score higher on severity if it is only compensated for (low on the mitigation hierarchy), versus a parallel scenario in which the same impact is avoided or minimised (higher up on the mitigation hierarchy). |

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| Comment ID | #14 |
| Section | FAQ 23 |
| Specific paragraph/sentence | §220: "*Whilst similar concepts and questions apply to social matters, guidance covering social may be issued in the future to better reflect specific aspects of those matters.”* |
| Comment | It would be helpful if EFRAG could provide references to already existing **resources (similarly to e.g. the mitigation hierarchy) that could help companies apply the concept to social matters.** |

**Chapter 5.7: FAQs on art. 8 EU taxonomy**

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| Comment ID | #15 |
| Section | FAQ 25 |
| Specific paragraph/sentence | Applicable to the entire section, but specifically:    §225: "*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."S* |
| Comment | Does this section suggest that one could **look to the SC and DNSH criteria of the EU Taxonomy when it comes to positive impact definitions?** Is it correct to assume, that the example above indicates that Taxonomy-eligible activities which fulfil all SC and DNSH criteria / a Capex plan has been established could be counted as a positive opportunities in the materiality assessment? Currently it is not clear, as the example states "reduced negative impact or even positive". |

**Value chain guidance**

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| **The summary of the VCIG** |  |  |
| **Chapter 1: Introduction** |  |  |
| **Chapter 2: Navigating value chain under CSRD and ESRS** |  |  |
| **Chapter 3: FAQ 1** |  |  |
| **Chapter 3: FAQ 2** |  |  |
| **Chapter 3: FAQ 3** |  |  |
| **Chapter 3: FAQ 4** |  |  |
| **Chapter 3: FAQ 5** |  |  |
| **Chapter 3: FAQ 6** |  |  |
| **Chapter 3: FAQ 7** |  |  |
| **Chapter 3: FAQ 8** |  |  |
| **Chapter 3: FAQ 9** |  |  |
| **Chapter 3: FAQ 10** |  |  |
| **Chapter 4: VC map** |  |  |