



Double Materiality Assessment

A suggested approach by EFRAG

EFRAG's Materiality Assessment Implementation Guidance (Draft version)

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 - Activities and business relationships
 - Other contextual information
 - Understanding affected stakeholders
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 - Impact materiality assessment
 - Financial materiality assessment
 - Consolidation of outcome
- **Step D: Reporting**
 - On the process:
 - IRO-1 Description of the process
 - On the outcome
 - SBM-3 / IRO-2 per ESRS

Materiality Assessment – rules of the game

1. Double materiality covers:

1. Financial materiality: risks and opportunities related to sustainability matters
2. Impact materiality: impact related to sustainability matters

2. The materiality assessment process defines which topics need to be reported, but is also crucial to have a complete, verifiable, comparable reporting

3. When a company has a lot of IRO's, they can be prioritised on a management & strategic level, but shall all be reported

4. The exercise of judgement

1. As any company is unique, an exercise of judgement is crucial. A materiality assessment entails that the management exercises judgement to determine the materiality, based on data, analysis and threshold definition

5. The backbone of a materiality assessment consists of

1. Data & objective information
2. Clear, explained methodologies and assumptions, with transparency over judgement, quantitative or qualitative thresholds, and other criteria

6. The reporting shall be consistent with other regulations relevant to that activity, sector, region or company.

Step A: Understanding the context

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Activities and business relationships

Activities and business relationships related to ESRS 2 SBM-1 are approached as follows:

- a) the analysis of the undertaking's business plan, strategy, financial statements and, when applicable, other information provided to investors;
- b) the undertaking's activities, products/services and the geographic locations of these activities; and
- c) the mapping of the undertaking's business relationships and upstream and/or downstream value chain, including type and nature of business relationships.

Other contextual information

There are other factors that can help identify sources of IRO's, such as:

- a) the analysis of the undertaking's relevant legal and regulatory landscape; and
- b) the analysis of published documentation such as media reports, analysis of peers, existing sector-specific benchmarks, other publications on general sustainability trends and scientific articles.

Step A: Understanding the context

Understanding of affected stakeholders

Goal: understanding which stakeholders are or are likely to be affected by the undertaking's own operations and upstream and downstream value chain. Based on this, the undertaking can identify its key affected stakeholders.

The following can be considered to aid such understanding:

- a) an analysis of the existing stakeholder engagement initiatives (such as by the communication, investor relations, business management, sales and procurement teams); and
- b) a mapping of affected stakeholders across the undertaking's activities and business relationships. Separate groups of affected stakeholders may be identified per activity, product or service and are to be prioritised for a particular sustainability matter.

Role and approach to stakeholders in the materiality assessment process

Stakeholders are those who can affect or be affected by the undertaking. There are two main groups of stakeholders:

- a) **affected stakeholders:** 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; and
- b) **users of sustainability statements:** primary users of general-purpose financial reporting (existing and potential investors, lenders and other creditors, including asset managers, credit institutions, insurance undertakings), and other users of sustainability statements, including the undertaking’s business partners, trade unions and social partners, civil society and non-governmental organisations, governments, analysts and academics.

→ Some, but not all, stakeholders may belong to both groups.

Role and approach to stakeholders in the materiality assessment process

Engagement with affected stakeholders is central to the undertaking's on-going due diligence process and sustainability materiality assessment. This includes its processes to identify and assess actual and potential negative impacts, which then inform the assessment process to identify the material impacts for the purposes of sustainability reporting.

- Common categories of stakeholders are: employees and other workers, suppliers, consumers, customers, end- users, local communities and persons in vulnerable situations, and public authorities, including regulators, supervisors and central banks.
- **Nature may be considered as a silent stakeholder.** In this case, ecological data and data on the conservation of species may support the undertaking's materiality assessment.
- **Materiality assessment is informed by dialogue with affected stakeholders.** The undertaking may engage with affected stakeholders or their representatives (such as employees or trade unions), along with users of sustainability reporting and other experts, to provide inputs or **feedback on its conclusions regarding its material impacts, risks and opportunities.**



Step B: Identification of actual & potential impacts, risks and opportunities



Step B: Identification of the actual and potential impacts, risks and opportunities related to sustainability matters

In this step, the undertaking identifies the material IROs relating to environmental, social and governance matters across its own operations and in its 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.

Approaches:

1. Identification of the potential matters may start from screening the list of matters summarized in **ESRS 1 paragraph AR 16** and then be completed by additional entity-specific matters. These may follow from either internal processes, (e.g., due diligence, risk management or grievance mechanisms) or external sources such as those described in paragraph 69 above and stakeholder engagement.
2. The undertaking may also develop a 'long' list of impacts, risks and opportunities relevant to its business model and upstream/downstream value chain and aggregate them following the structure of ESRS 1 paragraph AR 16. The approach detailed in paragraph 75 above could be effective for undertakings new to preparing the sustainability statement. Alternatively, an undertaking could start from the matters as informed by existing processes (e.g., GRI reporting or internal processes such as due diligence and risk management). Then the undertaking could compare the matters identified with the list in ESRS 1 AR16 for completeness.

→ The two approaches may be combined.

ESRS AR - 16

Topical ESRS	Sustainability matters covered in topical ESRS		
	Topic	Sub-topic	Sub-sub-topics
ESRS E1	Climate change	<ul style="list-style-type: none"> Climate change adaptation Climate change mitigation Energy 	
ESRS E2	Pollution	<ul style="list-style-type: none"> Pollution of air Pollution of water Pollution of soil Pollution of living organisms and food resources Substances of concern Substances of very high concern Microplastics 	
ESRS E3	Water and marine resources	<ul style="list-style-type: none"> Water Marine resources 	<ul style="list-style-type: none"> Water consumption Water withdrawals Water discharges Water discharges in the oceans Extraction and use of marine resources
ESRS E4	Biodiversity and ecosystems	<ul style="list-style-type: none"> Direct impact drivers of biodiversity loss 	<ul style="list-style-type: none"> Climate Change Land-use change, fresh water-use change and sea-use change Direct exploitation Invasive alien species Pollution Others
		<ul style="list-style-type: none"> Impacts on the state of species 	Examples: <ul style="list-style-type: none"> Species population size Species global extinction risk
		<ul style="list-style-type: none"> Impacts on the extent and condition of ecosystems 	Examples: <ul style="list-style-type: none"> Land degradation Desertification Soil sealing
		<ul style="list-style-type: none"> Impacts and dependencies on ecosystem services 	


Topical ESRS	Sustainability matters covered in topical ESRS			
	Topic	Sub-topic	Sub-sub-topics	
ESRS E5	Circular economy	<ul style="list-style-type: none"> Resources inflows, including resource use Resource outflows related to products and services Waste 		
ESRS S1	Own workforce	<ul style="list-style-type: none"> Working conditions 	<ul style="list-style-type: none"> Secure employment Working time Adequate wages Social dialogue Freedom of association, the existence of works councils and the information, consultation and participation rights of workers Collective bargaining, including rate of workers covered by collective agreements Work-life balance Health and safety 	
			<ul style="list-style-type: none"> Equal treatment and opportunities for all 	<ul style="list-style-type: none"> Gender equality and equal pay for work of equal value Training and skills development Employment and inclusion of persons with disabilities Measures against violence and harassment in the workplace Diversity
			<ul style="list-style-type: none"> Other work-related rights 	<ul style="list-style-type: none"> Child labour Forced labour Adequate housing Privacy
ESRS S2	Workers in the value chain	<ul style="list-style-type: none"> Working conditions 	<ul style="list-style-type: none"> Secure employment Working time Adequate wages Social dialogue Freedom of association, including the existence of work councils Collective bargaining Work-life balance Health and safety 	
			<ul style="list-style-type: none"> Equal treatment and opportunities for all 	<ul style="list-style-type: none"> Gender equality and equal pay for work of equal value Training and skills development The employment and inclusion of persons with disabilities Measures against violence and harassment in the workplace Diversity
			<ul style="list-style-type: none"> Other work-related rights 	<ul style="list-style-type: none"> Child labour Forced labour Adequate housing Water and sanitation Privacy

Topical ESRS	Sustainability matters covered in topical ESRS			
	Topic	Sub-topic	Sub-sub-topics	
ESRS S3	Affected communities	<ul style="list-style-type: none"> Communities' economic, social and cultural rights 	<ul style="list-style-type: none"> Adequate housing Adequate food Water and sanitation Land-related impacts Security-related impacts 	
			<ul style="list-style-type: none"> Communities' civil and political rights 	<ul style="list-style-type: none"> Freedom of expression Freedom of assembly Impacts on human rights defenders
			<ul style="list-style-type: none"> Rights of indigenous peoples 	<ul style="list-style-type: none"> Free, prior and informed consent Self-determination Cultural rights
ESRS S4	Consumers and end-users	<ul style="list-style-type: none"> Information-related impacts for consumers and/or end-users 	<ul style="list-style-type: none"> Privacy Freedom of expression Access to (quality) information 	
			<ul style="list-style-type: none"> Personal safety of consumers and/or end-users 	<ul style="list-style-type: none"> Health and safety Security of a person Protection of children
			<ul style="list-style-type: none"> Social inclusion of consumers and/or end-users 	<ul style="list-style-type: none"> Non-discrimination Access to products and services Responsible marketing practices
ESRS G1	Business conduct	<ul style="list-style-type: none"> Corporate culture Protection of whistle-blowers Animal welfare Political engagement Management of relationships with suppliers including payment practices 		
			<ul style="list-style-type: none"> Corruption and bribery 	<ul style="list-style-type: none"> Prevention and detection including training Incidents


ESRS – Data points overview



List of ESRS Data Points
Standards:
ESRS 2 - General Disclosures
ESRS 2 - Minimum Disclosure Requirements (MDR)
E1 - Climate Change
E2 - Pollution
E3 - Water and Marine Resources
E4 - Biodiversity and Ecosystems
E5 - Resource Use and Circular Economy
S1 - Own Workforce
S2 - Workers in the Value Chain
S3 - Affected Communities
S4 - Consumers and End-users
G1 - Business Conduct



Step C: Assessment and determination material impacts, risks and opportunities



Step C: Assessment and determination of the material impacts, risks and opportunities related to sustainability matters

In this step, the undertaking applies criteria for assessing impact and financial materiality, in order to determine the material actual and potential impacts, and material risks and opportunities. This then forms the basis for determining material information, based on the ESRS topical disclosure requirements.

→ Setting thresholds

Setting thresholds – Impact materiality

For **negative impacts**, materiality is based on the **severity of the impact**:

- a) Scale: how grave the negative impact is or how beneficial the positive impact is for people or the environment
- b) Scope: how widespread the negative or positive impacts are. For environmental impacts, e.g.: the extent of environmental damage or a geographical perimeter. In the case of impacts on people, the scope may be understood as the number of people adversely affected
- c) Irremediable character: hether and to what extent the negative impacts could be remediated, i.e., restoring the environment or affected people to their prior state.

For **positive impacts**, materiality is based on the **severity and likelihood** of the impact:

- a) the scale and scope of the impact for actual impacts; and
- b) the scale, scope and likelihood of the impact for potential impacts.

Setting thresholds – Actual impacts

Figure 4: Graphical representation of impact severity for actual impacts in columnar format

Please note that that the graphical representation in this figure serves only as illustration of a possible approach to visualisation of the conclusions of assessment of impact materiality criteria. ESRS 2 IRO-1 also requires the undertaking to explain how it determined the materiality of the impact, including the qualitative and quantitative thresholds used.

Negative impact	Severity assessment			Is the impact assessed as material?
	Scale	Scope	Irremediability	
Impact 1	Medium	Medium	Low	No
Impact 2	Medium	High	Low	Yes
Impact 3	High	High	Medium	Yes
...				
Impact N	High	Low	Medium	Yes

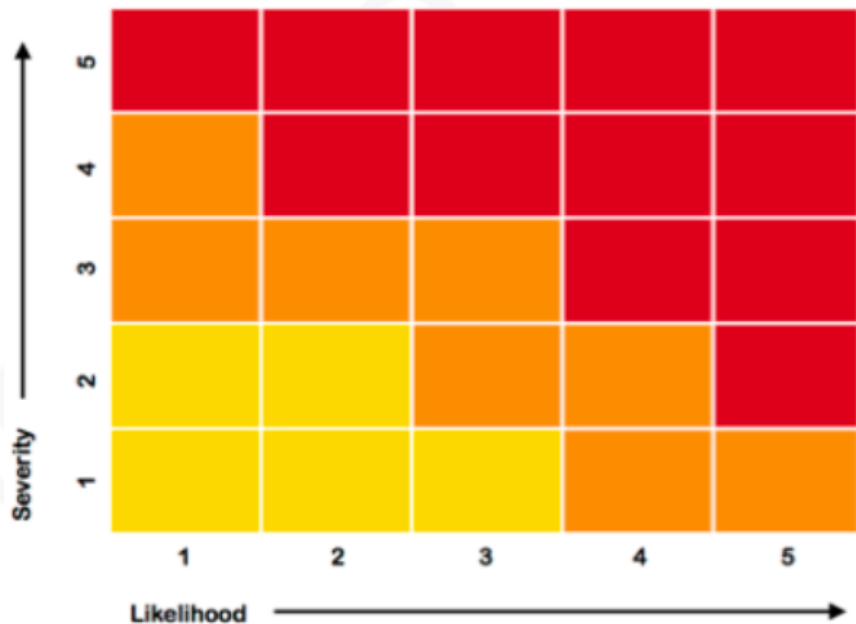
Colour coding:



Setting thresholds – Potential impacts

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

Please note that that the graphical representation in this figure serves only as illustration of a possible approach to visualisation of the conclusions of assessment of impact materiality criteria. ESRS 2 IRO-1 also requires the undertaking to explain how it determined the materiality of the impact, including the qualitative and quantitative thresholds used.



Setting thresholds – Actual impacts

Kwantitatieve toetsing voor zowel voor de impact als de financiële materialiteit.

Er kan voor gekozen worden om de kwalitatieve risico's kwantitatief te maken, zodat de risico's gemakkelijker kunnen worden weergegeven in een visuele scatterplot. Het is niet verplicht om dit te doen. Echter voor het nauwkeurig kunnen weergegeven van de risico's kan het gemakkelijker zijn om dit te doen aan de hand van kwantitatieve data.

Tijdens deze stap worden de kwalitatieve risico's omgezet naar kwantitatieve eenheden. Hierbij kunnen de elementen schaal, scope, herstelbaarheid, omvang en waarschijnlijk worden geplot als laag, middel en hoog. Voor de kwantificering kan dan gerekend worden met de volgende getallen:

Laag = 0,15

Middel = 0,50

Hoog = 0,90

Voor de impact materialiteit wordt de volgende formule gehanteerd om de risico's kwantitatief te maken:
 $((\text{schaal} + \text{scope} + \text{herstelbaarheid})/3) * \text{waarschijnlijkheid} / 0,81$.

Voor de financiële materialiteit wordt de volgende formule gehanteerd om de risico's kwantitatief te maken:

$(\text{omvang} * \text{waarschijnlijkheid}) / 0,81$

Setting thresholds – Financial materiality

The ESRS do not prescribe the use of specific thresholds definition for financial materiality.

However, ESRS 1 paragraph AR 15 states: “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

- a) the **likelihood of occurrence** and
- b) 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.

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.

Step D: Reporting

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Following the materiality assessment process, the undertaking shall report the assessment process and its 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 statement. The undertaking shall also disclose how it has determined the material information to be disclosed, including thresholds and criteria used to assess such information (ESRS 2 paragraph 59).

Example structure of ESRS sustainability statement



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