

FEBRUARY 2024

Consultation input: Draft materiality assessment implementation guidance

The European Financial Reporting Advisory Group (EFRAG) in December 2023 launched a 30 day public consultation on key draft implementation guidance documents including the [Draft Materiality Assessment Implementation Guidance](#) (MAIG).

The MAIG sets out to describe reporting requirements on the materiality assessment including the illustration of possible steps of the process. It also contains FAQs on the double materiality assessment to provide implementation guidance from a practical perspective.

The Danish Institute for Human Rights (DIHR) has provided input to this consultation in addition to the input given through participation in [EFRAG Sustainability Reporting Technical Expert Group](#) (SRTEG), which advises the EFRAG Sustainability Reporting Board on among other things, implementation guidance in support of the [European Sustainability Reporting Standards](#).

The DIHR's consultation input was delivered by way of an online survey and is made publicly available below.

Consultation survey questions and input

Chapter 1: Introduction

Clarification needs: In paragraph (hereafter: para) 20 the guide reads 'for example, the due diligence aspects related to the materiality assessment (and VC aspects) are covered in that guidance rather than here'. However elsewhere in the guide MAIG there is reference to the relevance of due diligence (e.g. para 75 or chapter 4.3) and in the same section (para 18) it is highlighted that key standards on due diligence have been used as a basis for the preparation of the MAIG. This leaves preparers with unclarity on where best to find such information. We suggest deleting the above sentence in para 20 and instead amend

para 18 to direct readers to where guidance related to due diligence can be found specifically.

Chapter 2: The ESRS approach to materiality

Substantive points:

In para 31 the MAIG clarifies that the undertaking may explain the reasoning behind omitted topics and shall explain if reporting on ESRS E1 climate change is omitted. In the same way that ESRS E1 on climate change is likely to be material for all companies the same can be argued for ESRS S1 covering own workers. As all undertakings covered by CSRD will have a significant number of own workers, they will also have potential negative impacts on the rights of such workers, as reflected in ESRS S1. We suggest that messaging around the likely materiality of ESRS S1 is brought through more clearly either as an example in para 31 itself and/or in paragraphs covering the exercise of judgement, application of thresholds or consideration of severity (e.g. paras 27 or 84)

The draft MAIG currently fails to convey the potential usefulness of DRs and associated ARs to identifying material impacts. The chapter explains the interaction between materiality assessment and assessing material information. It conveys that consideration of the materiality of information, including by applying DRs, is a step that follows the materiality assessment process in a linear fashion (see para 49). However, topical DRs and associated datapoints and AR methodologies can also be instructive for the identification of material impacts. Identifying whether an impact is material or not may necessitate gathering some of the data that is required by a given DR, irrespective of whether that data will subsequently be reported on. For example, assessing whether workers are paid adequately (ESRS S1-10) is not common practice by covered undertakings. However, collecting and analyzing related data such as that detailed under S1-10 can be key to determining whether or not adequate wages is a material matter. We suggest that a paragraph is added to clarify such nuanced interrelations and explain how preparers can make use of datapoints and methodologies included in topical DRs when identifying impacts and assessing their materiality. Once implemented this messaging should be repeated at relevant stages of chapter 3.

Figure 1c can be improved by adding further illustration on the analysis needed to be able to arrive at a yes or no on the question of whether a matter is material. The figure currently overly simplifies this as a quick yes/no consideration and fails to convey that a conclusion on whether a matter is material or not should be based on robust assessment. In addition, to adequately convey important messaging from ESRS 1 para 45 and 60 and MAIG para 75 about the relevance of due diligence to materiality assessment, we suggest that the text box in the top right corner is revised to read: 'list of matters identified by the

undertaking from existing materiality assessment' and/or its potential sustainability due diligence or risk management processes (new text suggestion underlined). This is also to offer helpful clarity to preparers with limited resources that indeed they can and should rely on existing sustainability assessments and processes to inform materiality assessments.

Clarification needs:

The use of different arrow types in figure 1 b page 12 is not clear and needs to be double checked. For example, one arrow in the arrow overview (single dotted line arrow) is not included in the figure. Further, the use of 'dependencies' in the figure and in para 35 is not explained and its meaning remains unclear to the reader at the risk of diluting the main messages of the figure. Although more content is included on dependencies in para 36 and 38, further clarification in the Figure would assist readers.

Para 36(a) should include a reference to where the reader can understand more about how to identify impacts (chapter 3)

Correction needs:

in para 37 please change from "indigenous' people" to "indigenous peoples" which is the correct term for the group.

Chapter 3: How is the materiality assessment performed ?

Affected stakeholders: Although the chapter helpfully includes guidance related to engaging with affected stakeholders several improvements are needed including to align the guidance more closely with ESRS 1 24 and provide sufficient clarity to preparers and their advisers including those new to engaging with affected stakeholders. Concretely we suggest:

in para 69 (b) adding 'geographical location' to the list of where separate groups may be identified. Indeed identifying affected stakeholders is a contextual exercise and not something that can be robustly performed at an aggregate or group level.

In para 85 first sentence: change 'key stakeholders' to 'key affected stakeholders and their legitimate representatives'. If it is not clarified that the importance is to consult potentially affected people then the distinction between the new ESRS element around consulting affected stakeholders and existing consultation practices via internal processes or external engagement with users or other experts is lost. This change would also bring about consistency with para 99.

103 last sentence: change stakeholders to 'affected stakeholders'

105: reads 'the mapping of affected stakeholders and, where possible, prioritizing them could be the first step'. The part about prioritization should be adjusted to align with para 69 that highlights that the prioritization has to do with their relevance to specific business activities etc, not, for example, their perceived importance to the company or their potential power. This is important to avoid the possibility that certain affected groups perceived to be less important are deprioritized in consultations despite potentially being affected by severe impacts.

Precision in the use of severity terminology: In line with ESRS 1 the MAIG helpfully includes guidance on assessing severity including as it relates to the three severity criteria. However more precision is needed to align with guidance with OECD MNE Guidelines and UNGPs from which the concept of impact severity stems. Concretely:

In para 113 (a) the parenthesis should be adjusted to provide more meaningful explanation of gravity. Suggestion: (i.e. the extent or seriousness of infringements e.g. in the context of S impacts on rights to life, health, liberty, security or in the context of E e.g, threats of extinction etc)

In para 116: note gravity and scale are synonymous concepts. Consider changing to 'scale or scope'.

Examples underused: Chapter three could be improved by including more examples and cases to illustrate the steps and their underlying components vis-à-vis different types of companies, impacts, sectors, and affected stakeholders. As a guidance document, examples would greatly benefit the preparers and other users in putting the theoretical instruction to practice.

Chapter 4: How to leverage other sources?

134: the para reads: 'the general criterion for assessing the materiality of information ... (ESRS 1 paragraph 31) is expected in most cases to rely on decision usefulness'. While this might be the case with regards to financial materiality it is not the case in relation to impact materiality where significance is the other criteria. The paragraph should be revised to better reflect this duality or make explicit that this is true in the context of financial materiality only.

139: the para reads: 'through this due diligence process the undertaking can also identify affected stakeholders, whose engagement informs the materiality assessment of IRO'. This is not correct as engaging with affected stakeholders is absolutely central to due diligence and hence not only something the undertaking 'can do'. Suggested alternative: 'through this due diligence process the undertaking should identify and engage with affected stakeholders. Such efforts can inform the materiality assessment of IRO'

Chapter 5.1: FAQs on impact materiality

Para 149 reads: “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.”

First, the term ‘directly caused’ is not consistent terminology with international due diligence guidelines. To align delete ‘directly’. Second, the sentence leaves open what difference in assessment or categorization that the three types of impact involvement would imply. This comes with the risk of implying that lower involvement (e.g. directly linked) would typically be less material, whereas ESRS make clear that this should be considered by assessing severity criteria. To avoid misinterpretations of para 149, we suggest adding this sentence at the end of the above sentence: ‘However, this does not imply that impacts that are directly linked are necessarily less material than those caused. As illustrated in section 3.6. the materiality of impacts is to be assessed by a consideration of their severity.’

Chapter 5.3: FAQs on Materiality Assessment Process

FAQ 7. In point 160 (c) the draft combines outbreak of a pandemic with entering into a new business relationship. It is not clear why these two are combined. Suggest moving the ‘new business relationship’ element under point (a) where it fits better. In addition suggest adding as a new (e) ‘entering into a new geographical context with significant contextual risks (e.g. conflict zone, indigenous peoples’ land etc). This is to highlight that some impacts are bound to geographical context.

Chapter 5.4: FAQs on stakeholder engagement

The term “stakeholders” can be interpreted differently to different readers. Throughout 5.4. the guidance should specify where relevant that you are talking about ‘affected stakeholders’, for example, in para 186, 187 (last sentence), 188, heading FAQ 16. Without this, the guidance is unclear on the difference between consulting affected stakeholders and engagement with investors and other users as part of ‘traditional’ stakeholder engagement in past materiality assessment practices.

Chapter 5.6: FAQs on reporting

Para 197: Suggest to add to the list of disaggregation categories in the first sentence: 'activities or value chain step'. These categories are relevant for many companies, in that their impacts differ widely across own operation, upstream and downstream as well as in the case of large companies, will differ significantly across different business activities / lines. Hence from an impact perspective such disaggregation can bring about needed clarity.