

This paper has been prepared by the EFRAG Secretariat for discussion at a public meeting of EFRAG SR TEG. The paper forms part of an early stage of the development of a potential EFRAG position. Consequently, the paper does not represent the official views of EFRAG or any individual member of the EFRAG SRB or EFRAG SR TEG. The paper is made available to enable the public to follow the discussions in the meeting. Tentative decisions are made in public and reported in the EFRAG Update. EFRAG positions, as approved by the EFRAG SRB, are published as comment letters, discussion or position papers, or in any other form considered appropriate in the circumstances.

## **Possible way forward on approach to materiality**

### **Previous meetings**

- 1 Refer to the discussions in the following meetings:
  - (a) 15 August 2022 SR TEG
  - (b) 24 August SRB
  - (c) 2 September SR TEG
  - (d) 13 September SRB.

### **Objectives of this session**

- 2 To consider a possible way forward for the materiality approach in ESRS 1.

### **Assumptions and background**

- 3 All the SFDR should be mandatory and, upon clarification by the ESMA representative, they agreed that also the additional SFDR indicators should be mandatory, in order to create the data infrastructure for financial market participants to report.
- 4 A strong polarization that exists on this topic: there are two fronts (as it was in the PTF, in the outcome of the consultation and in the previous SR TEG discussions), between those that support materiality assessment (Approach 5 in the 15 August paper) and those that support a mandatory list (Approach 1). Members were split between scenario 1.2 above and scenario 3 or even 3+ (longer lists of mandatory KPIs). Approach 3 in the paper discussed on the 15 August (combination of a list of mandatory items and mandatory assessment for other items) was confirmed as the common ground/compromise solution.

### **Last SR TEG discussion (20/23 September)**

- 5 The discussion in the meetings from 20 to 23 September led to define a list of 'mandatory' items per each standards.
- 6 In addition, it confirmed that the area of materiality assessment would include the PTAPR DRs (45% of the total DRs), plus few specific cases for environmental KPIs (e.g. substance of concern), as 'indirectly' subject to materiality, as they are required only 'where applicable', i.e. when the undertaking doesn't have a policy/target/action it complies with the DR stating this fact and, when it has a plan to implement a policy/target/action, disclose such plan.
- 7 The following comments were made by individual members:
  - (a) The PTAPR DRs of social standards is built embedding a materiality assessment at level of standard, they present a list of sub-sub-topics to be considered and require

to report the datapoints listed in the DRs only for the sub-sub-topics that are material for the undertaking.

- (b) There should be one sub-sub-topic only covered by a given DR (avoid mixing sub-sub-topics for KPIs) and it should not be possible to omit a datapoint below the DR level.
- (c) Differently from the point above, if the approach to materiality would not allow to omit an individual datapoint of a mandatory DR (the EDs had this possibility with implicit approach), the approval of the ESRS text would require a very detailed decision making at individual datapoint level, before members would be able to agree on the standard.

#### **SFDR indicators mandatory (outside the scope of materiality assessment)**

- 8 SFDR should be mandatory, including the additional SFDR indicators, in order to create the data infrastructure for financial market participants to report.
- 9 EFRAG published an Appendix to the consultation Cover Note that maps the DRs in the EDs with the SFDR PAI.

[https://www.efrag.org/Assets/Download?assetUrl=%2Fsites%2Fwebpublishing%2FSiteAssets%2FED\\_ESRS\\_AP3.pdf](https://www.efrag.org/Assets/Download?assetUrl=%2Fsites%2Fwebpublishing%2FSiteAssets%2FED_ESRS_AP3.pdf)

#### **Proposed way forward and materiality applied to KPIs**

- 10 This paper assumes that the simplifications agreed upon in the week 19/23 September are finally implemented in the standards. As such, the DRs that have tentatively been identified in that week as 'to be deleted' are not considered in this paper.
- 11 The area of materiality assessment as resulting from the SR TEG detailed analysis of the DRs includes the following: KPIs only (as ESRS 2 – incl. IROs – and PTAPR in topical standards are mandatory always), other than the SFDR that are always mandatory. This area correspond to 28% of the total number of DRs.
- 12 Refer to Agenda Paper 06-02 for the detail of these KPIs.
- 13 The EFRAG Secretariat proposes to make these KPIs mandatory if the undertaking's materiality assessment has confirmed that the relevant matter (sub-sub topic) is material to the undertaking. In order to implement this approach, a list of sustainability matters (sub-sub-topics) per topical standard would be included in the Application Guidance of ESRS 1.
- 14 Refer to the Appendix below for a possible re-drafting of the relevant paraps of ESRS 1.

#### **Do we need an additional list of mandatory KPIs?**

- 15 This approach would leave under the scope of materiality assessment the following KPIs (in grey those that relate to financial effects):

(a) Climate:

- (i) E1-15 Potential financial effects from material physical risks;
- (ii) E1-16 Potential financial effects from material transition risks;
- (iii) E1-17 Potential financial effects from climate-related opportunities;

(b) Pollution:

- (i) E2-6 Pollution-related incidents and deposits impacts and risks, and financial exposure to the undertaking;

(ii) E2-7 Financial effects from pollution-related impacts, risks and opportunities;

(c) Water:

(i) E3-7 Potential financial effects from water and marine resources-related impacts, risks and opportunities;

(d) Biodiversity:

(i) E4-5 and E4-6 Pressure metrics and Impact metrics;

(ii) E4-10 Potential financial effects from biodiversity-related impacts, risks and opportunities;

(e) Own workforce:

(i) S1-9 Training and Skills Development indicators;

(ii) S1-10 Coverage of the health and safety management system;

(iii) S1-13 Work Life Balance indicators;

(iv) S1-14 Fair remuneration;

(v) S1-15 Social security eligibility coverage;

(vi) S1-17 Annual total compensation ratio;

(vii) S1-19 Employment of persons with disabilities;

(viii) S1-20 Differences in the provision of benefits to employees with different employment contract types;

(ix) S1-21 Grievances and complaints related to other work-related rights;

(x) S1-22 Collective bargaining coverage;

(xi) S1-23 Work stoppages;

(xii) S1-24 Social dialogue;

(xiii) S1-26 Privacy at work;

(f) Governance

(i) G2-7 Anti-competitive behavior events;

(ii) Political engagement and lobbying activities

(iii) Payment practices.

16 A key open question is therefore whether some of these KPIs should be mandatory in all cases, i.e. outside the scope of materiality assessment and included in a list of mandatory items, and which criterion should be used to identify them.

**Questions to SR TEG**

- 17 Do EFRAG SR TEG members agree with the proposed way forward?
- 18 Do EFRAG SR TEG members agrees with the proposed re-drafting?
- 19 Do EFRAG SR TEG members support the proposed list of sustainability matters?
- 20 Considering the resulting overall area of materiality assessment (25% of the KPIs), would a light explicit approach (no justifications but a list of omitted information) be acceptable?
- 21 Do you think that some of the KPIs in the scope of materiality assessment should be mandatory (paragraph 18 above)? Which criterion should be used to identify them?
- 22 Do you consider that the proposed list of sustainability matters could also serve as list of the omitted DRs? What alternative should be considered for the content index/list of omitted DRs? (refer to the link below - Appendices)  
  
<https://efrag.sharepoint.com/Meetings/2208261335242821/Meeting%20Documents/04%20-%2001%20-%20ESRS%20Approach%20to%20materiality%20-%20EFRAG%20SR%20TEG%206%20September%202022.pdf>
- 23 Do you have other comments on this topic?

## **APPENDIX**

### **Proposed amendment to ESRS 1**

#### *Relationship between double materiality and mandatory disclosure requirements*

57. Sector-agnostic and sector-specific ESRS mandate disclosure requirements for all undertakings or all undertakings in a particular sector reflecting double materiality.

All the disclosure requirements in ESRS 2 are assumed to be material for all undertakings, therefore they cannot be omitted as assessed to be not-material by the undertaking.

The undertaking shall conduct a materiality assessment that leads to the identification to its material impacts, risks and opportunities that will be included in the sustainability statements. The undertaking shall report on its material impacts, risks and opportunities either following the disclosure requirements mandated in a topical ESRS, when the specific matter or information related to a matter is covered by a topical ESRS, or on an entity-specific basis, when the specific matter or information related to a matter is not covered by a topical ESRS.

When a sustainability matter is assessed to be material for the undertaking, the undertaking shall apply the disclosure requirements related to that specific matter in a topical ESRS.

58. The undertaking shall establish explicit thresholds and/or criteria to determine when a sustainability matter is material, as well as when a specific information to be disclosed under a disclosure requirement for a matter that has been assessed to be material is assessed to be 'not material for the undertaking' and, as such, omitted.

The disclosure requirements in the topical standards that relate to policies, targets, actions and resources are mandatory where applicable. This means that when an undertaking doesn't have in place a given policy, target or action it complies with the respective disclosure requirement stating this fact or reporting any plan to implement the policy, target or action, if it exists.

62. When information to be disclosed under a disclosure requirement (under a specific datapoint or under an entire disclosure requirement) that is omitted by the undertaking is considered implicitly disclosed as 'not material for the undertaking'.

## Appendix B: Application provisions – new – to be added

1. When performing its materiality assessment, the undertaking shall consider the following list of sustainability matters covered in the topical standards. When, as a result of the undertaking's materiality assessment (ref. to DR ESRS 2 IRO 1), a given sustainability matter in this list is assessed to be material, the undertaking shall report according to the corresponding DRs in the performance measures chapter of the relevant topical standard.
2. As the disclosure requirements in ESRS S2, S3 and S4 relate only to policies, targets, actions and resources (there are no performance measures in these standards), they are not included in this list.
3. As described in ESRS 1 par. 19, in addition to complying with the DRs in the topical ESRS, the undertaking shall develop disclosures (entity-specific disclosures) on material impacts, risks and opportunities not covered by topical ESRS.

**[FOR HIGHER CLARITY THE CORRESPONDING DR CAN BE ADDED NEXT TO THE MATTER]**

TOPICAL STANDARD	SUSTAINABILITY MATTERS TO BE COVERED IN MATERIALITY ASSESSMENT FOR PERFORMANCE MEASURES IN TOPICAL ESRS
ESRS E1	<ul style="list-style-type: none"> <li>- Energy</li> <li>- GhG Emissions</li> <li>- Climate-related financial effects</li> </ul>
ESRS E2	<ul style="list-style-type: none"> <li>- Pollution of air (both indoor and outdoor)</li> <li>- Pollution of water (including groundwater)</li> <li>- Pollution of soil</li> <li>- Pollution of living organisms and food resources</li> <li>- Substances of concern</li> </ul>
ESRS E3	<ul style="list-style-type: none"> <li>- Water withdrawals</li> <li>- Water consumption</li> <li>- Water use</li> <li>- Water discharges in water bodies and in the oceans</li> <li>- Habitat degradation and intensity of pressure on marine resources</li> </ul>
ESRS E4	<b>- [TO BE COMPLETED]</b>
ESRS E5	<ul style="list-style-type: none"> <li>- Depletion of non-renewable resources</li> <li>- Regeneration of renewable resources</li> <li>- Decoupling growth from extraction of natural resources</li> </ul>
ESRS S1	<ul style="list-style-type: none"> <li>- Training &amp; Development</li> <li>- Health &amp; Safety</li> <li>- Working hours</li> <li>- Work-life balance</li> <li>- Fair remuneration</li> <li>- Social security</li> <li>- Non-Discrimination</li> <li>- Equality in pay</li> <li>- Access to secure employment</li> <li>- Equal treatment regarding working conditions, access to social protection and training</li> <li>- Inclusion of persons with disabilities</li> <li>- Freedom of Association &amp; Collective Bargaining</li> <li>- Social Dialogue</li> <li>- Child labour</li> <li>- Forced labour</li> <li>- Privacy at work</li> <li>- Adequate housing</li> </ul>
ESRS G1	<ul style="list-style-type: none"> <li>- Corruption and bribery</li> <li>- Anti-competitive behaviour</li> <li>- Political engagement and lobbying activities</li> </ul>

