

## IFRS Sustainability Developments

# ISSB issues educational material on materiality

### What you need to know

- The educational material covers the identification of sustainability-related risks and opportunities and the disclosure of material information under ISSB Standards. The content does not override or adjust the requirements of ISSB Standards.
- There is no requirement to use a specific approach to identify sustainability-related risks and opportunities, but sources of guidance are provided to help entities.
- Only material information is required to be disclosed to ensure information is relevant to primary users. This requires judgement and is specific to an entity's facts and circumstances.
- The entity's impact on the environment and society should not be ignored, as information may be material to primary users if its impacts could reasonably be expected to affect the entity's prospects.

### Background

On 19 November 2024, the International Sustainability Standards Board (the ISSB or Board) published educational material on sustainability-related risks and opportunities and the disclosure of material information when reporting under IFRS Sustainability Disclosure Standards (ISSB Standards).

The educational material has been developed as part of the ISSB's commitment to supporting the implementation of ISSB Standards, *IFRS S1 General requirements for Disclosure of Sustainability-related Financial Information (IFRS S1)* and *IFRS S2 Climate-related Disclosures (IFRS S2)* that were released in June 2023.

Note that the content of the educational material is educational in nature and does not override or adjust the requirements of the ISSB Standards.

### What does the educational material cover?

The educational material centres around the IFRS S1 requirement that an entity must disclose material information about the sustainability-related risks and opportunities that could reasonably be expected to affect the entity's prospects, i.e., its cash flows, access to finance or cost of capital over the short, medium or long term.

The educational material defines material information and sustainability-related risks and opportunities and explains the associated requirements of the ISSB Standards in simple terms to help entities ultimately identify material information about their sustainability-related risks and opportunities to disclose in the entity's general purpose financial reports.

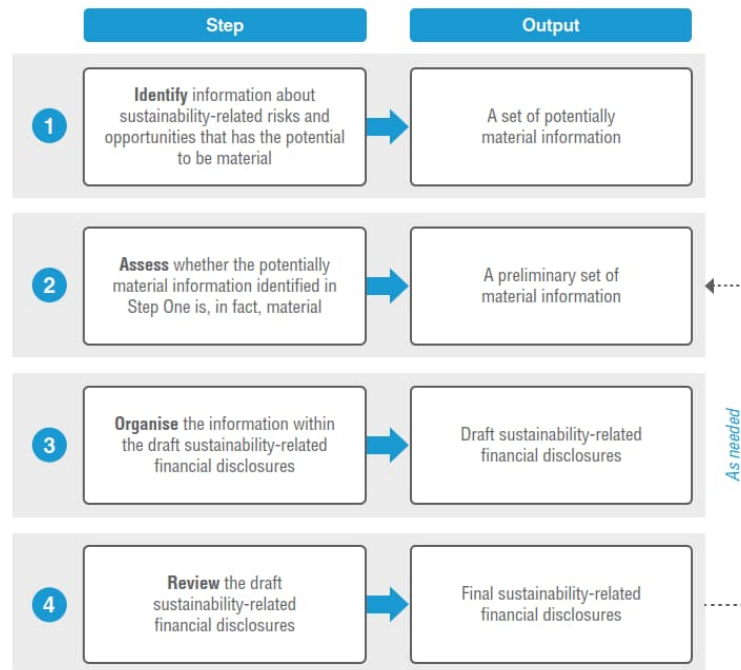
Connectivity and interoperability considerations are included throughout the educational material. Connectivity considerations highlight where sustainability-related financial disclosures may be connected to the financial statements. Interoperability considerations highlight relevant matters for entities applying ISSB Standards alongside other sustainability-related standards such as the European Sustainability Reporting Standards (ESRS) or Global Reporting Initiative (GRI) Standards.



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Practical examples are used to illustrate how to meet the relevant requirements for materiality in ISSB Standards. An example four-step process that entities could follow to identify and disclose material information is provided in the educational material (see figure 1 below) which is similar to the ‘four-step materiality process’ from the IFRS Practice Statement 2 *Making Materiality Judgements*.

*Figure 1 (extract from educational material): Identifying and disclosing material information about sustainability-related risks and opportunities that could reasonably be expected to affect an entity’s prospects*



## Key messages in the educational material

### The meaning of materiality under ISSB Standards

The term materiality is not used in ISSB Standards in relation to the significance or importance of a sustainability-related risk or opportunity, rather materiality is used to determine what information should be disclosed about those risks or opportunities.

Information is material if it could reasonably be expected to affect an entity’s prospects by influencing the decisions that primary users (being investors, lenders or other creditors) make relating to providing resources to the entity.

In other sustainability standards such as ESRS and GRI, ‘materiality’ as a term is used more broadly as they refer to material matters or topics as well as the material information about those topics. The educational material explains that, “*despite these differences in the application of the word ‘material’, when applying the concept of ‘materiality’ in ISSB Standards and ‘financial materiality’ in ESRS ... this difference is not in itself expected to result in different outcomes of the information reported.*” Hence, the ISSB Standards are interoperable with ESRS in relation to what information is considered material for primary users.

In addition to financial materiality, ESRS requires an assessment on impact materiality, which considers how an entity’s activities impact people and the environment. This means that ESRS considers the information needs of other stakeholders beyond just primary users, unlike ISSB Standards.

However, the educational material makes clear that the entity’s impact on people and the environment should not be ignored when applying ISSB Standards, as information may be material to primary users if its impacts could reasonably be expected to affect the entity’s prospects.

## How to approach materiality under ISSB Standards

### Identify all sustainability-related risks and opportunities

There is no requirement to use a specific approach to identify sustainability-related risks and opportunities when applying ISSB Standards.

Entities often already have established processes for identifying sustainability-related risks and opportunities as part of the management of their business. This would be a good starting point, particularly, because matters that are important to an entity's board or management may also be important to primary users.

To help entities identify the sustainability-related risks and opportunities that are relevant based on their facts and circumstances, sources of guidance are provided in IFRS S1. These include the SASB Standards' industry-specific disclosure topics that entities must refer to and consider, and other sources such as the CDSB Framework that may be considered.

The entity's process in identifying sustainability-related risks and opportunities does not need to be exhaustive because the breadth of information available can be wide ranging. However, entities are required to *"use all reasonable and supportable information that is available to the entity at the reporting date without undue cost or effort."*

In its initial assessment, an entity needs to identify the sustainability-related risks and opportunities throughout its entire value chain. However, its value chain may be subject to change often, so whilst an entity may choose to reassess the scope of sustainability-related risks or opportunities throughout its value chain more frequently, it is only required to do so if a significant event or significant change in circumstance occurs [IFRS S1.B11].

### Assess what information would be material to primary users

Having identified all sustainability-related risks and opportunities, entities should then determine what information to disclose about them, as not all information identified will be material to the primary users. Only the disclosure of material information is required when applying ISSB Standards. This aims to ensure that the information disclosed in the general purpose financial reports is the most relevant to the primary users and that material information does not get obscured by other, less important, information.

An example might be a brewery business that depends on having access to clean water to operate and identifies this as a sustainability-related risk to business continuity, such that poor water quality would prevent it from producing its product, which would negatively affect its revenue. However, for other entities, although access to clean water may be identified as a risk, information about the risk may not be material to that entity, depending on its specific facts and circumstances, hence, would not require disclosure.

Identifying material information requires judgement. Entities will need to make these materiality judgements based on the primary users' information needs at each reporting date. Entities should consider the information needs of all primary users equally and focus on common information needs. This means not singling out information needs of, for example, current investors, future investors or investors that have particular interests such as 'impact investors' who may have social and environmental goals.

### Consider qualitative and quantitative factors

Because materiality judgements are specific to an entity's facts and circumstances, IFRS S1 does not specify any thresholds for materiality, nor does it predetermine what would be material in a particular situation.

An entity could determine this based on any number of quantitative or qualitative factors, i.e., the magnitude and nature of the effect of a sustainability-related risk or opportunity on the entity. The educational material states that, *“in general, the more factors that apply to a particular sustainability-related risk or opportunity, or the more significant the possible effect of those factors, the more likely it is that information about that risk or opportunity is material.”*

Information may be quantitatively material based on the magnitude of the sustainability-related risk or opportunity. For example, when assessing investment in employee health and safety measures related to a specific sustainability-related risk, the entity may consider the value of the investment made over time, relative to its total number of employees. The magnitude could also be compared to other measures commonly used in the financial statements, such as the impact on cash flows or the return on investment.

Qualitative factors can include entity-specific factors (such as the involvement of a related party of the entity) and external factors (such as the geography, industry sector and markets in which the entity operates). The presence of a qualitative factor is more likely to mean that the information is of interest to the primary users, but this alone does not necessarily mean it is material, so entities need to apply judgement.

Nevertheless, the educational material explains that, *“by its nature, some information required by ISSB Standards is likely to be material because of the presence of a qualitative factor. For example, information about how an entity structures its governance function to manage the topic of climate risk is, by its nature, likely to be material for all entities exposed to a climate-related risk that could reasonably be expected to affect their prospects.”*

#### Disclose material information

Entities assess whether the information identified individually or in combination with other information is material in the context of the entity's sustainability-related financial disclosures taken as a whole. If an entity concludes that information is material, ISSB Standards require that it be disclosed in the entity's general purpose financial report.

#### How we see it

Applying the materiality concept in the context of sustainability-related financial disclosures prepared in accordance with ISSB Standards is expected to be dynamic over time as adoption of the Standards becomes widespread. Although it can be informed by the assessment of materiality in financial statements, entities need to establish an appropriate approach as materiality judgements will be required based on the primary users' information needs and an entity's specific circumstances.

The educational material will be useful for entities that want to understand more detail on the requirements for identifying and ultimately disclosing material information about their sustainability-related risks and opportunities. This is a judgemental area and the ISSB Standards require entities to disclose information about the judgements they have made to prepare their sustainability-related financial disclosures.

The interoperability considerations are also helpful for those entities that need to consider materiality under ISSB Standards alongside other sustainability-related standards.

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EYG No. 010145-24GbI  
ED None

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