IFRS Sustainability

Staff paper

Agenda reference:2A

Sustainability Standards Advisory Forum meeting

Date	**February 2025**
Project	**Supporting the implementation of IFRS S1 and IFRS S2**
Topic	**Overview of the educational material 'Sustainability-related risks and opportunities and the disclosure of material information' published in November 2024**
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Purpose of this session

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- To provide an overview to the SSAF about the ISSB's educational material 'Sustainability-related risks and opportunities and the disclosure of material information' published in November 2024.

Questions for SSAF members

- Do you have any questions or comments on the materials presented in this paper?
- Do you have any suggestions for sharing or making this material more accessible, beyond the published document and the forthcoming webinar?

Reminders

- Educational material is not part of ISSB Standards and cannot add or change requirements in the Standards.
- This educational material:
  - explains *what* to provide information about (sustainability-related risks and opportunities that could reasonably be expected to affect an entity's prospects) and *how* to assess whether that information is material; and
  - uses concepts that are aligned with concepts used by the IASB—including as set out in IFRS Practice Statement 2.

IFRS Sustainability

Agenda

1. Introduction and overview
2. Definition of material information and its application in ISSB Standards
3. Sustainability-related risks and opportunities that could reasonably be expected to affect an entity’s prospects and its application in ISSB Standards
4. Identifying and disclosing material information
5. Q&A discussion

Overview and main messages

Chapter 1

Examines main components of the **definition of 'material information'** to enable an understanding of the use of this term in ISSB Standards and how to make materiality judgements.

1. ISSB Standards are designed to result in the provision of information that is useful to **primary users** of general purpose financial reports.
2. Materiality is an entity-specific characteristic of **information**.
3. When making materiality judgements, an entity assesses whether **omitting, misstating or obscuring information** could reasonably be expected to influence the decisions primary users make about providing resources to the entity.

Overview and main messages

Chapter 2

Explains what **sustainability-related risks and opportunities** are and how to identify them.

4 IFRS S1 describes the concept of **sustainability-related risks and opportunities.**

5 An entity **identifies** sustainability-related risks and opportunities that could reasonably be expected to affect its prospects.

6 A specific approach or method to identify sustainability-related risks and opportunities is not required; but the Standards require entities to consider specific **sources of guidance** to identify such risks and opportunities (eg SASB Standards).

Overview and main messages

Chapter 3

Explains how to apply the requirements in ISSB Standards to **identify and disclose material information** about sustainability-related risks and opportunities.

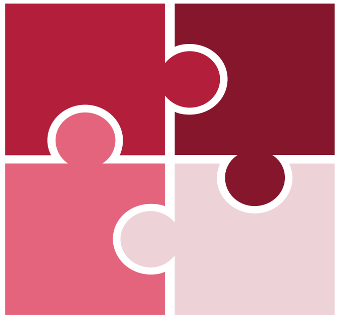
7 An entity might follow a **process** to identify and disclose material information about the sustainability-related risks and opportunities it has identified.

8 ISSB Standards require the disclosure of information about how an entity's activities **impact** people and the environment when those impacts give rise to sustainability-related risks or opportunities that could reasonably be expected to affect the entity's prospects, and the related information about those impacts is material to primary users.

Connectivity and interoperability considerations

Connectivity considerations

An entity applying ISSB Standards is required to provide information in a manner that enables primary users to understand the connections between disclosures provided in its sustainability-related financial disclosures and its related financial statements. Connectivity is also a particular focus in the work of the ISSB and IASB. These considerations are included in boxes labelled ‘connectivity considerations’.



Interoperability considerations

Interoperability considerations might be helpful to preparers who are applying ISSB Standards alongside the European Sustainability Reporting Standards (ESRS) and Global Reporting Initiative (GRI) Standards. Considerations related to this are included in boxes labelled ‘interoperability considerations’.

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The definition of material information and its application in ISSB Standards

Chapter one

The definition of material information

In the **context of sustainability-related financial disclosures**, information is material if **omitting, misstating or obscuring** that information could reasonably be expected to influence **decisions that primary users** of general purpose financial reports make on the basis of those reports, which include financial statements and sustainability-related financial disclosures and which provide information about a specific reporting entity.

Connectivity considerations
ISSB Standards and IFRS Accounting Standards use aligned definitions of 'material information'. This facilitates: • connectivity in an entity's general purpose financial reports; and • a closer connection than if the entity's sustainability-related information were provided using another definition of material information.

The ISSB Standards refer to ‘materiality of information’

Materiality is an entity-specific characteristic of *information*, consistent with IASB’s use of the term.

- ISSB Standards set out requirements that an entity applies in preparing sustainability-related financial disclosures.
- Materiality is used to assess whether *information* required by ISSB Standards would need to be disclosed by a particular entity.
- In other words, the definition of ‘material information’ is used as a **filter to assess whether** *information* **about a sustainability-related risk or opportunity would need to be provided by an entity** to **meet the requirements set out in ISSB Standards**.

Interoperability considerations

- ISSB Standards refer to ‘material information’ about sustainability-related risks and opportunities, whereas other standards use the term material/materiality differently:
  - ESRS refer to ‘material matters’, GRI Standards refer to ‘material topics’.
  - Commonly used in the context of a ‘materiality assessment’.
- Despite these differences, the definition of ‘material information’ in ISSB Standards is aligned with the corresponding definition used in ESRS related to ‘financial materiality’.

Primary users of general purpose financial reports

- ISSB Standards are designed to result in the provision of information that is useful to primary users.
- **Primary users are existing and potential investors, lenders and other creditors – this is the same audience that IFRS Accounting Standards focus on.**
- Primary users and their information needs:
  - Information they are assumed to know.
  - Common information needs.
  - Consideration of both 'existing' and 'potential'.

Could reasonably be expected to….

- An entity assesses whether information is material based on **whether that information** could reasonably be expected to **influence decisions of primary users**.
- Although **the entity itself makes this assessment**, it is **based on the perspective of primary users** and their information needs.

Interoperability considerations
This focus on the information needs of primary users distinguishes sustainability-related financial information under ISSB Standards from broader, multi-stakeholder sustainability reporting.

In the context of sustainability-related financial disclosures

- Sustainability-related financial disclosures serve a **specified objective**:

  Provide information about an entity's sustainability-related risks and opportunities that is useful to primary users of general purpose financial reports in making decisions about providing resources to the entity.

In applying ISSB Standards, and the definition of material information, an entity considers whether information is material in the context of this objective.

Connectivity considerations

- Although the definition of 'material information' is aligned with the definition of the same term in IFRS Accounting Standards, the information required to meet the objective of the respective general purpose financial reports is distinct.
- Sustainability-related financial disclosures:
  - complement information in an entity's financial statements;
  - likely include more qualitative and forward-looking information than financial statements;
  - provide information about sustainability-related risks and opportunities that could reasonably be expected to affect an entity's prospects, whereas financial statements provide information about an entity's assets, liabilities, equity, income and expenses; and
  - will more often require consideration of longer time periods and information throughout the value chain.

Omitting, misstating or obscuring information

In assessing whether information is material, an entity considers the effect of **omitting, misstating or obscuring that information** on primary users' decisions.

An entity is required to identify its **sustainability-related financial disclosures clearly and distinguish** them from other information the entity provides. This is important in the context of sustainability-related financial disclosures because:

The location of sustainability-related financial disclosures within general purpose financial reports might vary between entities. There are various possible locations in general purpose financial reports in which to disclose sustainability-related financial information, for example management commentary or a similar report. These reports might also provide information to meet other requirements.

Information might be provided alongside information to meet the needs of other stakeholders in addition to primary users. An entity's sustainability reporting might include information intended for a broader range of stakeholders beyond primary users or to meet particular needs of primary users that are not common information needs.

In both cases, sustainability-related financial disclosures are required to be clearly identifiable and not obscured by additional information.

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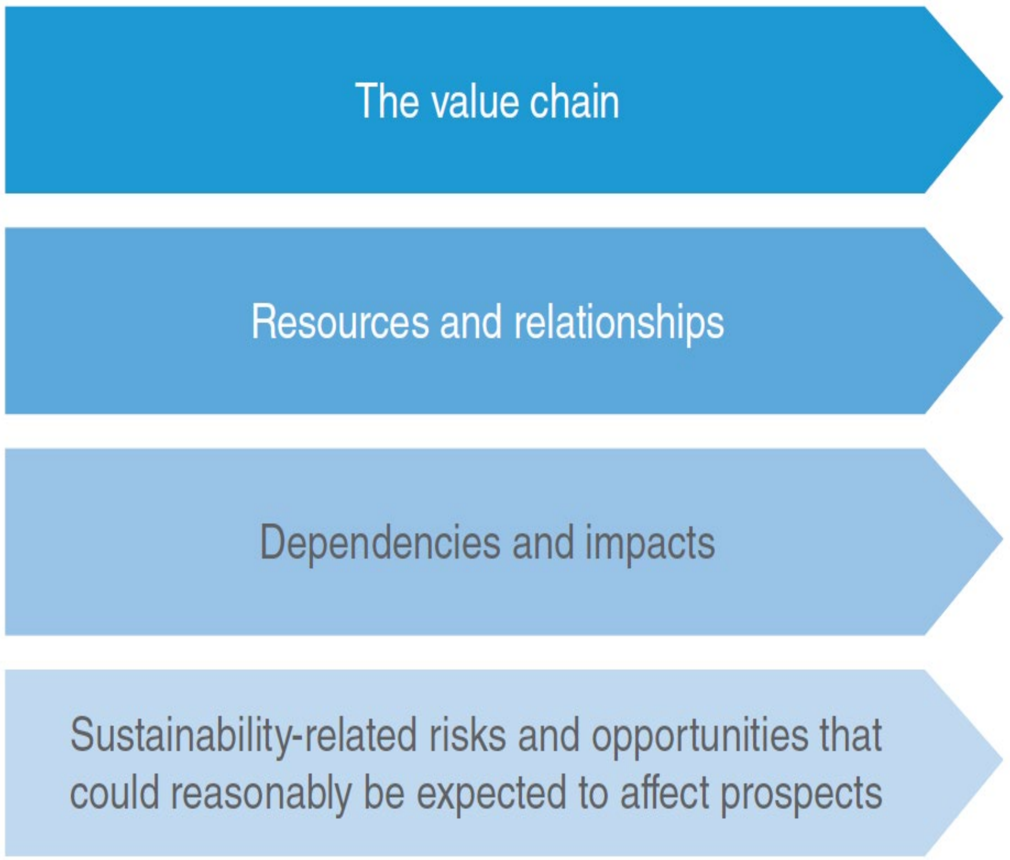
Sustainability-related risks and opportunities that could reasonably be expected to affect an entity's prospects and its application in ISSB Standards

Chapter two

The concepts underlying ‘sustainability risks and opportunities’



- Arise out of the interactions between an entity and its stakeholders, society, the economy and the natural environment throughout the entity’s **value chain**.
- An entity both depends on and affects **resources and relationships** throughout its value chain, which can contribute to their preservation, regeneration and development, or to their degradation and depletion.
- These **dependencies and impacts** might give rise to **sustainability-related risks and opportunities that could reasonably be expected to affect the entity’s prospects**.

The ‘value chain’ and interactions throughout the value chain

The full range of interactions, resources and relationships related to a reporting entity’s **business model** and the **external environment** in which it operates.

Interactions with stakeholders, society, the economy and the natural environment throughout an entity’s **value chain.**

Example—The entity, its business model, the external environment and distribution channels

In assessing its value chain, and specifically its distribution channels, an electronic device manufacturer considers:

- **business model:** third-party vendors that the entity depends on to sell its products to customers.
- **external environment:** a regulation that effects the devices permitted to be manufactured, in an effort to reduce electronic waste.

Example—Interactions with stakeholders, society, the economy and the natural environment

An entity considers its dependency on suppliers in three jurisdictions for raw materials:

- Jurisdiction A’s **local communities** are protesting against the entity’s deforestation practices.
- Jurisdiction B’s **government** introduces a tax incentive for sustainable operations.
- Jurisdiction C is experiencing a **drought**.

In identifying the scope of an entity’s value chain, an entity is required to use ‘all reasonable and supportable information that is available to the entity at the reporting date without undue cost or effort’.

The resources and relationships an entity depends on and affects exist throughout its value chain

Forms and examples of resources and relationships

Human	Intellectual	Financial	Natural	Manufactured	Social
• Entity's workforce • Workers in supply chains	• Patents • Copyrights • Trademarks	• Cash • Investments • Access to financial resources	• Land • Water • Minerals • Raw materials	• Machinery • Equipment • Buildings • Infrastructure	• Stakeholder relationships • Customers • Indigenous communities

Resources and relationships can:

- be **internal**, such as the entity's workforce, its know-how or its organisational processes;
- be **external**, such as the materials and services the entity needs to access or the relationships it has with suppliers, distributors and customers; and
- include (but are not limited to) the resources and relationships recognised as assets in the entity's financial statements.

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Dependencies and impacts

An entity considers how it—directly and indirectly—depends on and affects resources and relationships. IFRS S1 explains that an entity:

- **depends** on resources and relationships to **generate cash flows**; and
- **affects** resources and relationships through its **activities and outputs**.

These dependencies and impacts contribute to the preservation, regeneration and development of resources and relationships, or to their degradation and depletion.

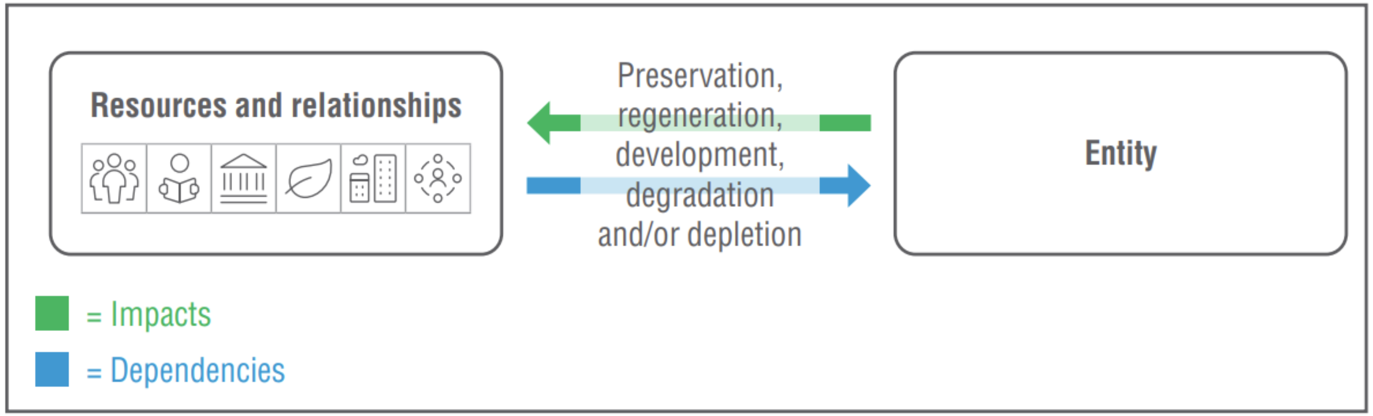
An entity's dependencies and impacts on resources and relationships as a result of the entity's activities and outputs

Entity's activities and outputs	Entity's **dependency** on a resource and relationship to generate cash flows	Entity's **impact** on a resource and relationship through its activities and outputs
The entity **extracts** groundwater for irrigation.	The entity depends on **water** to operate its business model.	The entity's activities might **deplete** the water source because of its dependency on water and its activities impacting the water.
The entity **invests** in employee training.	The entity operates in a highly competitive market and depends on a **highly specialised workforce** to operate its business model.	The entity's investment in training can help to **develop** its workforce because of its dependency on a highly specialised workforce and its activities which impact the workforce.

The ‘interdependent system’

- An entity’s **activities and outputs** can affect **resources and relationships** on which it **depends.**
- In such circumstances, the entity is **affected by its own impact** on the resource or relationship.

This **interdependent system**, in which the entity both depends on and affects its resources and relationships, is depicted below:



An entity’s dependencies and impacts might not always be closely related. An entity can:

- depend on something it does not impact; and
- impact something it does not depend on.

Yet, in both cases—the dependency and impact—might give rise to sustainability-related risks and opportunities that could reasonably be expected to affect an entity’s prospects.

Sustainability-related risks and opportunities that *could reasonably be expected* to affect an entity's prospects

- An entity identifies sustainability-related risks or opportunities considering an external perspective. This means a sustainability-related risk or opportunity could be identified even if the entity itself does not have an expectation that the sustainability-related risk or opportunity could reasonably be expected to affect its prospects.
- In such circumstances, an entity discloses associated material information.

Example—Entity determines it could reasonably be expected to be affected by a sustainability-related risk to which it does not believe itself to be exposed

- Clothing manufacturer sources supplies from a jurisdiction known for effective human rights protections.
- Peers have disclosed risks of human rights violations throughout supply chains—but these peers source supplies from jurisdictions in which the entity does not.
- In assessing its sustainability-related risks, entity considers that:
  - it does not expect the risk of human rights violations throughout its supply chain to affect its prospects (entity-specific factor); and
  - that the industry in which the entity operates is known to be exposed to such risks (external factor).
- The entity determines that *it could reasonably be expected* that it is exposed to the risk of human rights violations in its supply chain, because primary users expect this to be a risk for an entity in this industry.

Sustainability-related risks and opportunities that could reasonably be expected to affect *an entity's prospects*

An entity's prospects refers to the entity's **cash flows**, its **access to finance** or **cost of capital** over the **short, medium or long term**.

The effects of sustainability-related risks and opportunities on an entity's cash flows, its access to finance or cost of capital include:

- the amount, timing and uncertainty of the entity's incoming and outgoing cash flows;
- the entity's ability to obtain funding; and
- the cost incurred by the entity to secure funding for its operations and investments.

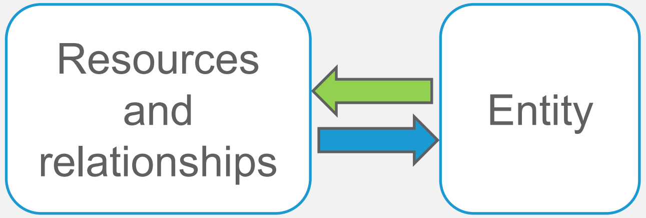
- The effect of a sustainability-related risk or opportunity on an entity's **access to finance** and **cost of capital** brings in an **assessment of how other market participants might interact with the entity**.
- The effects are assessed over the short-, medium- and long-term time horizons and the time horizons can vary among entities and depend on many factors.

Examples

An entity considers the **resources and relationships** throughout its **value chain** on which it **depends** and which it **affects**, and whether they give rise to **sustainability-related risks and opportunities** that **could reasonably be expected** to affect the **entity's prospects.**

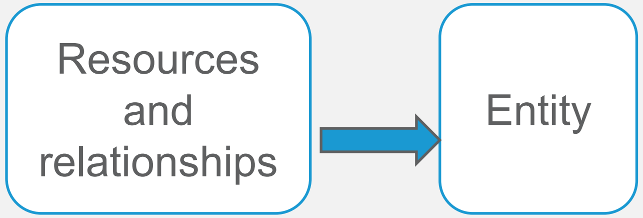
Example 1: highly specialised workforce

Relationship that the entity is *dependent on that it also affects.*



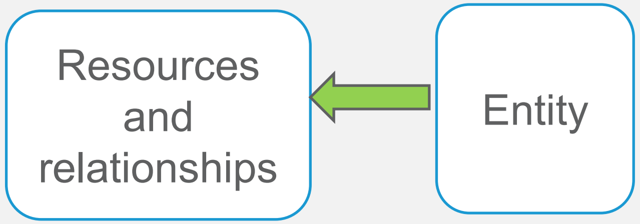
Example 2: access to finance

Resource that the entity is *dependent on that it does not affect.*



Example 3: local marine species

Resource that the entity *affects* that it *does not depend on.*



Key

dependencies impacts

How to identify sustainability-related risks and opportunities

- Entities often have well-established processes for identifying sustainability-related risks and opportunities.
- ISSB Standards **do not require that an entity use a specific approach or method to identify** sustainability-related risks and opportunities; however, the Standards **do require entities to consider specific sources of guidance**.

Sources of guidance

Required to

- Apply ISSB Standards
- Refer to and consider applicability of the SASB Standards

May consider

- CDSB Framework Application Guidance
- Work of other standard setters focused on investor information needs
- Industry or regional practice

Use all reasonable and supportable information that is available to the entity at the reporting date without undue cost or effort

If there is a significant event or significant change in circumstances, reassess the scope of sustainability-related risks and opportunities throughout the value chain

Output

List of sustainability-related risks and opportunities that could reasonably be expected to affect an entity's prospects

Identifying and disclosing material information

Chapter three

A four-step process to identify and disclose material information

- An entity might find it helpful to follow a process to identify and disclose material information about its sustainability-related risks and opportunities.
- The four-step process described in the educational material is an example of such a process.

	Step	Output
1	**Identify** information about sustainability-related risks and opportunities that has the potential to be material	A set of potentially material information
2	**Assess** whether the potentially material information identified in Step One is, in fact, material	A preliminary set of material information
3	**Organise** the information within the draft sustainability-related financial disclosures	Draft sustainability-related financial disclosures
4	**Review** the draft sustainability-related financial disclosures	Final sustainability-related financial disclosures

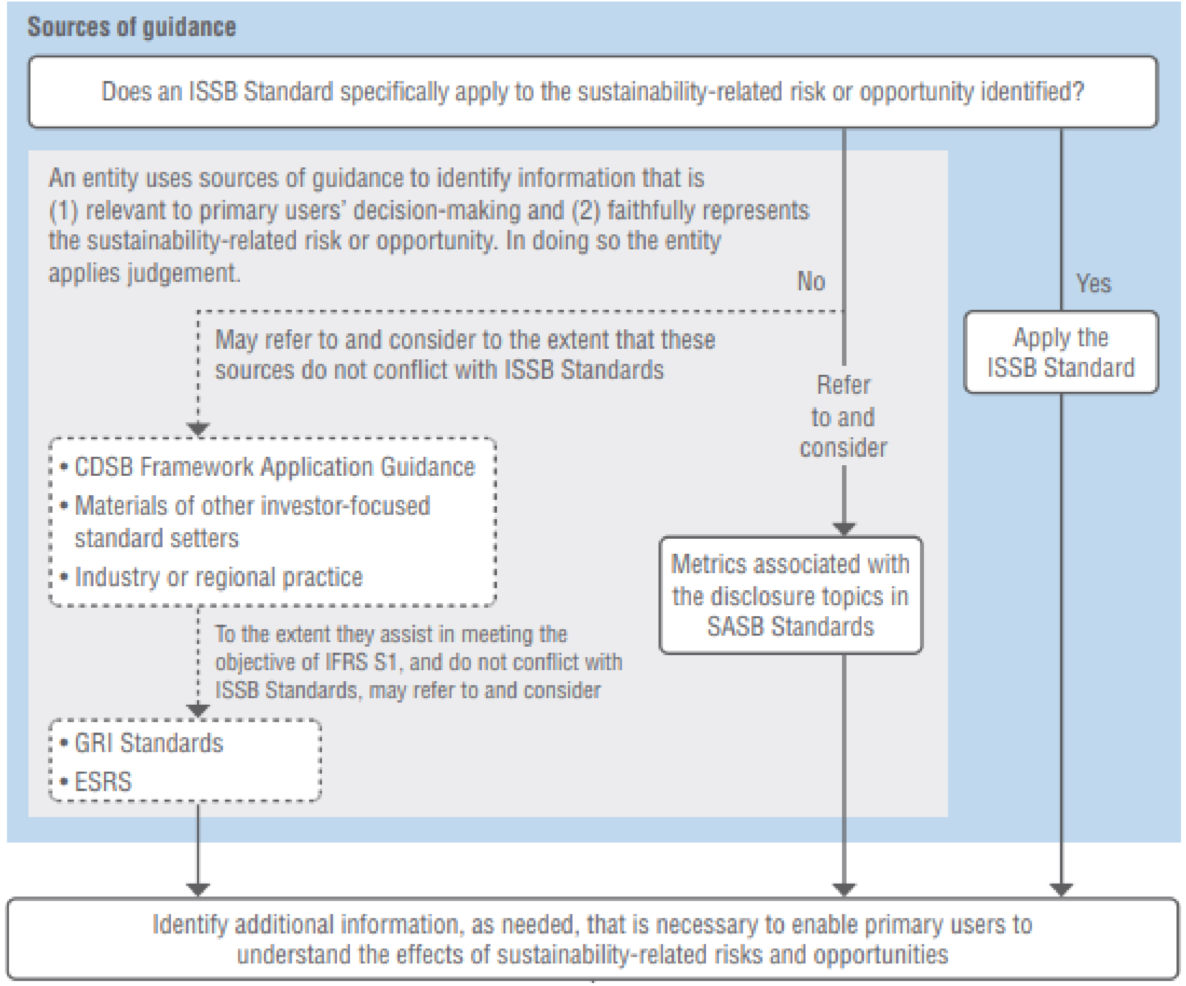
As needed

Connectivity considerations

This four-step process is similar to the 'four-step materiality process' illustrated in IFRS Practice Statement 2 *Making Materiality Judgements*.

Step One: Identify information about sustainability-related risks and opportunities that has the potential to be material

- An entity applies the requirements in ISSB Standards, including related to the use of sources of guidance.
- Additional information is required when that information is necessary to enable primary users to understand the effects of sustainability-related risks and opportunities on the entity's prospects.



The output of Step One is a set of potentially material information.

Step Two: Assess whether the potentially material information identified in Step One is, in fact, material

- This assessment requires the entity to **apply judgement**, taking into consideration its facts and circumstances.
- This step explains what an entity considers as it makes **materiality judgements**, including questions an entity might encounter when making materiality judgements, such as how to consider:

Qualitative and quantitative factors	Possible future events with uncertain outcomes	Changed circumstances and assumptions

The output of Step Two is a preliminary set of material information.

Step Three: Organise the information within the draft sustainability-related financial disclosures

- Organise preliminary set of material information in a way that **communicates information clearly and concisely** to primary users.

- Requirements related to the **judgements an entity will make** while organising material information include those related to:

Aggregating and disaggregating information	Obscuring information	Disclosing material information *See next slide*

- This step also explains other requirements in ISSB Standards related to the interaction of ISSB Standards and laws or regulations and to the disclosure of commercially sensitive information about opportunities.

The output of Step Three is draft sustainability-related financial disclosures.

Disclosing material information—dependencies and impacts

Additional information is required when that information is necessary to enable primary users to understand the effects of sustainability-related risks and opportunities on the entity's prospects.

Example:

- The objective of IFRS S1 is to **disclose information about sustainability-related risks and opportunities** that is useful to primary users (Chapter One).
- An entity's **dependencies and impacts** on resources and relationships **give rise to sustainability-related risks and opportunities** (Chapter Two).
- **Information about both dependencies and impacts could therefore be necessary** to enable a primary user's understanding of the effects of sustainability-related risks and opportunities that could reasonably be expected to affect the entity's prospects.

Interoperability considerations

- In ESRS, impact materiality assessments consider how an entity impacts people or the environment. GRI Standards consider how an entity impacts the economy, environment, and people, including impacts on their human rights. This is sometimes referred to as an 'inside-out perspective'.
- Describing ISSB Standards as 'outside-in' is an incomplete, and therefore incorrect, description. The effect of an entity's activities on resources and relationships—including on people and the environment—might give rise to sustainability-related risks and opportunities that could reasonably be expected to affect the entity's prospects and thus are relevant when applying ISSB Standards.

Step Four: Review the draft sustainability-related financial disclosures

- In this step, the entity 'steps back' and considers its sustainability-related financial disclosures as a whole.
- An entity assesses whether information is material both individually and in combination with other information in the context of its whole sustainability-related financial disclosures.
- This review might lead an entity to reconsider its assessment in Step Two, and reassess some information presented in its draft sustainability-related financial disclosures.

Example considerations when determining whether all material information has been identified.

In performing this review, the entity considers whether:

- relevant relationships between different items of information have been identified.
- items of information that are individually immaterial are also immaterial in the aggregate.
- information is communicated in an effective and understandable way.
- the sustainability-related financial disclosures provide a fair presentation of an entity's sustainability-related risks and opportunities.

The output of Step Four is the final sustainability-related financial disclosures

Questions

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