Te Kāwai Ārahi Pūrongo Mōwaho
EXTERNAL REPORTING BOARD

Materiality Questions and Answers

Assurance over Greenhouse Gas disclosures

Contents

What do these Questions and Answers cover?

These Questions and Answers (Q&As) focus on key questions about materiality that practitioners may face when applying ISSA (NZ) 5000, *General Requirements for Sustainability Assurance Engagements*. They can be read in two ways: as general guidance for sustainability assurance engagements, and as New Zealand-specific guidance for assurance over greenhouse gas (GHG) disclosures in climate statements.

The Q&As highlight questions from the IAASB's publication ISSA 5000 Frequently Asked Questions: The Application of Materiality ("FAQs") and International Standard on Sustainability Assurance (ISSA) 5000 Implementation Guide ("The Guide"). The IAASB's publications address assurance over sustainability information generally. Shaded New Zealand specific material highlights relevant considerations given the New Zealand statutory scope for mandatory assurance over GHG disclosures.

These Q&As address three main areas:

- the distinction between entity materiality and practitioner materiality
- how the scope of the mandatory assurance engagement affects materiality
- how practitioners may apply different materiality judgements.

Section 1: Entity materiality and practitioner materiality

Question 1. What is the concept of materiality related to sustainability information?

Materiality is a concept relating to the information needs of the intended users and what may reasonably be expected to influence their decisions based on the information reported and subject to assurance. For this reason, materiality is often referred to as a "user-driven concept".

The sustainability reporting framework or criteria may define or describe materiality and provide the context for users whose needs are being addressed.[1]

Information required by Aotearoa New Zealand Climate Standards must be disclosed if it is material. Information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that primary users make on the basis of an entity's climate-related disclosures[2].

Question 2: Who are the intended users and how are they and their information needs identified?

For purposes of ISSA (NZ) 5000, the standard defines "intended users" in paragraph 18 as the individual(s) or organisation(s), or group(s) thereof, that the practitioner expects will use the sustainability assurance report. In some cases, there may be intended users other than those to whom the assurance report is addressed.[3]

The practitioner may not be able to identify all those who will read the assurance report, particularly when a large number of people have access to it. In such cases, particularly when possible users are likely to have a broad range of interests in the sustainability matters, intended users may be limited to major stakeholders with significant and common interests. Intended users may be identified in different ways, for example, by agreement between the practitioner and management or those charged with governance, or by law or regulation.[4]

The information needs of the intended users may be specified. For example, in some cases, certain users (for example, lenders) may request that an assurance engagement be performed on sustainability information that has been prepared using criteria that are designed for a specific purpose. In other cases,

[1] FAQs, Question 1
[2] NZ CS 3, General Requirements for Climate-related Disclosures, paragraph 28
[3] FAQs, Question 5
[4] The Guide, paragraph 123

the entity may have gone through a process to test the topics they have identified with relevant stakeholders such as through a survey or consultation mechanism. The practitioner may consider the process the entity followed to inform them of what may influence the information needs of the intended users.[5]

Identifying intended users and their information needs may be challenging for sustainability reporting, at least for initial engagements, as there may be a diverse range of users with broad and disparate interests. Those interests may focus on financial materiality, impact materiality or double materiality. However, intended users do not need to encompass every possible user or group of users, but instead will usually include the major stakeholders with significant and common interests.[6]

The reporting framework may provide a description of the intended users for which the framework has been developed.

The ultimate aim of Aotearoa New Zealand Climate Standards is to support the allocation of capital towards activities that are consistent with a transition to a low-emissions, climate resilient future.

NZ CS 1 defines primary users as existing and potential investors, lenders and other creditors.[7]

Question 3: What is the difference between the entity's process to identify sustainability information to be reported (sometimes referred to as the entity's "materiality process") and the practitioner's application of materiality in planning and performing the engagement?[8]

The concept of materiality is the same for the entity and the practitioner (i.e., it is a user-driven concept, that is, it is affected by perceptions of the information needs of intended users of the sustainability information). Both the entity and the assurance practitioner make judgements about materiality in the context of the information needs of intended users, and requirements of the reporting framework may provide a frame of reference for the entity's and assurance practitioner's judgments about materiality (e.g., financial materiality, impact materiality or both).

The entity's process to identify sustainability information to be reported is focused on identifying the sustainability topics or aspects of topics relevant to users and then applying materiality to determine which information about relevant topics or aspects of topics is material and therefore needs to be reported. In applying materiality, the entity also considers the level of detail in the disclosures to meet the information needs of intended users. The practitioner considers the entity's process at various times throughout the engagement (refer Appendix 2 of ISSA (NZ) 5000).

The practitioner considers (for qualitative disclosures) or determines (for quantitative disclosures) materiality when identifying and assessing the risks of material misstatement, designing and performing further procedures in response to assessed risks, and in evaluating identified misstatements of the sustainability information.

In the context of evaluating identified misstatements, both management and the practitioner share a similar objective, i.e., evaluating whether identified misstatements, individually or in the aggregate, would cause the sustainability information to be materially misstated. Management's perspective on what is deemed to be a material misstatement may differ from the practitioner's view, but ultimately any difference in views about whether the sustainability information is materially misstated would need to be resolved, or it may lead to a modified assurance conclusion.[9]

[5] The Guide, paragraph 124
[6] FAQs, Question 5
[7] NZ CS 1, *Climate-related Disclosures*
[8] The Guide, paragraphs 117 -120
[9] The Guide, paragraphs 117 -120

Materiality applies to all the disclosure requirements in Aotearoa New Zealand Climate Standards.[10]

The application of the disclosure requirements in Aotearoa New Zealand Climate Standards are presumed to result in material information in most cases. However, if when applying the disclosure requirements to its own specific facts and circumstances, an entity determines that the resulting information is not material, it need not disclose it.[11]

Materiality is entity-specific, based on the nature, magnitude, or both, of the items to which the information relates.[12]

The assurance practitioner considers materiality in relation to the GHG disclosures that are within the scope of the assurance engagement. (Refer question 5 below)

Question 4: For what purpose does the practitioner apply materiality in a sustainability assurance engagement?[13]

Materiality is applied by the practitioner in planning and performing a sustainability assurance engagement, including when performing risk assessment procedures to identify and assess the risks of material misstatement and determining the nature, timing and extent of further procedures in response to the assessed risks of material misstatement. In addition, the practitioner applies materiality in evaluating whether the sustainability information is free from material misstatement. Relevant requirements and guidance are:

- ISSA (NZ) 5000, paragraph 95 addresses the practitioner's responsibility to develop an overall strategy and engagement plan. The application material explains, among other matters, that understanding how the entity disaggregates or aggregates the sustainability information for purposes of reporting may assist the practitioner in planning the engagement[14]. How the practitioner decides to group disclosures, whether in the same way as management or using another logical way, will affect the level at which the practitioner considers or determines materiality and designs and performs risk assessment procedures.[15]
- ISSA (NZ) 5000, paragraph 98 requires the practitioner to consider materiality for qualitative disclosures, and to determine materiality for quantitative disclosures, and paragraph 100 requires the practitioner to determine performance materiality for quantitative disclosures.[16]
- If both financial materiality and impact materiality ("double materiality") are required to be applied by the reporting framework or criteria, paragraph 99 of ISSA (NZ) 5000 requires that the practitioner "takes into account" both perspectives in considering or determining materiality. Where the applicable framework applies double materiality, the practitioner may use the entity's double materiality assessment as part of obtaining an understanding of the information needs of intended users and identifying and assessing risks of material misstatement. This does not imply that the practitioner re-performs the entity's double materiality assessment. This is further explained in the Guide, paragraphs 312-314, *What does it mean to "take into account both perspectives" of double materiality when considering or determining materiality?*
- During the engagement, the practitioner may identify misstatements of the sustainability information and if management does not correct such misstatements, the practitioner is required

[10] NZ CS 3, *General Requirements for Climate-related Disclosures*, paragraph 27
[11] NZ CS 3, *General Requirements for Climate-related Disclosures*, paragraph 31
[12] NZ CS 3, *General Requirements for Climate-related Disclosures,* paragraph 30
[13] FAQs, Question 9
[14] ISSA (NZ) 5000, paragraph A284
[15] See FAQs, Question 10 for further discussion of group disclosures
[16] See FAQs Questions 13 -19 for further discussion

to determine whether uncorrected misstatements are material, individually or in the aggregate (i.e., determine whether the sustainability information is materially misstated).[17]

Section 2: How the scope of assurance is considered when applying materiality

Question 5: Does the practitioner consider the scope of the assurance engagement in applying materiality?[18]

The practitioner makes judgements about materiality in the context of the information needs of the intended users related to the sustainability information that is subject to assurance - actual or potential misstatements of the sustainability information that may reasonably be expected to influence the decisions of users taken on the basis of that information. The scope of the assurance engagement may extend to all the sustainability information to be reported by the entity or only part of that information.[19]

Paragraph A298 of ISSA (NZ) 5000 explains that materiality relates to the sustainability information within the scope of the assurance engagement. When the assurance engagement covers some, but not all, of the sustainability information, materiality is considered in relation to only the sustainability information that is within the scope of the assurance engagement.

The above concept is not unique to sustainability assurance but is fundamental to assurance engagements generally. Assurance standards contemplate that assurance work is performed over subject matter information within the scope of the engagement (e.g., whether financial statements as a whole or elements thereof, or all the sustainability information being reported or specific sustainability disclosures).

The following information required by Aotearoa New Zealand Climate Standards is subject to an assurance engagement:

- gross GHG emissions in metric tonnes of CO_2e classified as scope 1, scope 2, and scope 3
- additional requirements for the disclosure of GHG emissions and
- GHG emissions methods, assumptions and estimation uncertainty.

The assurance practitioner considers materiality in relation to only the GHG disclosures that are within the scope of the assurance engagement.

The practitioner plans and performs procedures to obtain sufficient appropriate evidence to obtain limited assurance or reasonable assurance, as applicable, that *the sustainability information that is subject to assurance* is free from material misstatement. The practitioner's assurance conclusion communicated in the assurance report is designed to enhance the degree of confidence of the intended users about *that information* (i.e., the information within the scope of the assurance engagement).

In applying materiality, the practitioner recognises that different disclosures may give rise to different information needs and tolerances for misstatement among intended users. This means that ordinarily the practitioner considers or determines materiality for different disclosures or groups of disclosures. Therefore, the practitioner's consideration or determination of materiality in relation to a specific disclosure or grouping of disclosures may not necessarily be different based on whether the scope of the assurance engagement is the entire sustainability information or only part of the sustainability information reported by the entity.

There are various factors that may affect the practitioner's consideration of qualitative materiality and determination of quantitative materiality. Some factors may have greater prominence when the scope of the

[17] ISSA (NZ) 5000, paragraphs 153-161 and related application material (paragraphs A470-A498), as well as paragraphs 482-490 in the Guide
[18] FAQs, Question 12
[19] ISSA (NZ) 5000, paragraph 5

assurance engagement covers some, but not all, of the sustainability information as contemplated in ISSA (NZ) 5000, paragraph A298. The following are examples of such factors (none of which are necessarily determinative on their own):

- sensitivity of the information to stakeholders, including the number of persons or entities affected by, and the severity of the effect, of the sustainability matter.
- The relative importance of the disclosure in the context of the entity's industry or the geographic locations of its operations (e.g., sustainability information about the same topic or aspects of a topic may be of greater or lesser interest to intended users, depending on the entity's industry or geographic locations).
- The determination of the scope of the engagement by law or regulation, including the reasons why specific or only certain sustainability information is required to be assured relative to those matters that are relevant to the information needs of intended users. This also may include recognising that users' attention would be drawn to those disclosures that have been assured.

The mandatory assurance engagement in New Zealand is not over the climate statements as a whole but is restricted to the GHG disclosures within these statements[20]. The user's attention or focus may be drawn to the GHG disclosures that have been assured.

- Whether a potential misstatement of the disclosure could affect compliance with law or regulation, including whether there is an incentive or pressure on management to achieve an expected target or outcome in relation to the topic or aspects of the topic.
- Whether or the extent to which the disclosure addresses matter(s) that are part of the entity's sustainability strategy.
- The attention placed on the disclosure or aspects of the disclosure in the entity's reporting (e.g. included in the foreword of the CEO, discussed as part of key results) or with respect to known previous communications to the intended users on matters relevant to their information needs.

[20] Section 461ZH of the Financial Markets Conduct Act, 2013

Example: Contrasting how certain factors may affect the practitioner's consideration or determination of materiality for disclosures subject to assurance

	Steel Manufacturer – Integrated steel producer with blast furnace operations	**Retail Bank – Regional retail bank with office-based operations**
Disclosures within the scope of the assurance engagement	Scope 1 and 2 emissions only	Scope 1 and 2 emissions only
Scope 1 and 2 emissions profile	Very high Scope 1 emissions from production processes and significant Scope 2 electricity consumption	Low Scope 1 emissions and moderate Scope 2 emissions from offices and data centres
Relevant factors in the circumstances		
Stakeholder sensitivity	Investors, customers, regulators and communities closely monitor decarbonisation performance due to transition risk and environmental impacts	Investors and regulators are more focused on financed emissions and climate risk management than operational emissions
Industry/ geographic relevance	Operational GHG emissions are a central industry metric and subject to significant scrutiny in the country's industrial transition	Operational GHG emissions are generally of lower significance within the sector compared with financed emissions
Law or regulation	Material Scope 1 and Scope 2 disclosures are within the scope of mandatory reporting/assurance requirements	Material Scope 1 and Scope 2 disclosures are within the scope of mandatory reporting/assurance requirements
Compliance pressures	Significant pressure to meet public emissions reduction commitments and regulatory expectations	Limited direct pressure relating to operational emissions targets
Link to sustainability strategy	Reduction of operational emissions forms a key pillar of the entity's sustainability strategy	Sustainability strategy focuses primarily on financing activities and portfolio transition
Prominence in reporting	Emissions data highlighted in CEO messaging and key performance indicators	Operational emissions disclosed primarily to satisfy reporting requirements

The factors above suggest that users of the greenhouse gas disclosures within the scope of the assurance engagement for the steel manufacturer relative to those of the retail bank may be more sensitive to or have a lower tolerance for misstatement in the reported Scope 1 and Scope 2 emissions. For example, in the case of the steel manufacturer, relatively smaller misstatements in Scope 1 and Scope 2 emissions may be significant to users.

The notion of using multiple materialities also implies that for either of the entities above, the practitioner's consideration or determination of materiality related to Scope 1 and Scope 2 emissions information may not necessarily be different if the scope of the sustainability assurance engagement were to be broader (i.e., if

Scope 3 emissions, other disclosures or grouping of disclosures, or the entire sustainability information of the entity, were subject to assurance).

Section 3: Different materiality judgements

Question 6: Is the practitioner required to determine materiality for the sustainability information or greenhouse gas disclosures as a whole?[21]

No. A sustainability assurance engagement ordinarily involves the application of multiple materialities. This means that materiality is considered or determined for different disclosures.

Not all disclosures involve the same materiality considerations. Given the nature of greenhouse gas disclosures, i.e., qualitative and quantitative disclosures about three different scopes of direct and indirect emissions, it may be impracticable for practitioners to determine materiality for the disclosures as a whole. For different scopes of emissions, the same intended users may have different information needs, or a different tolerance for misstatement.

ISSA (NZ) 5000 is an overarching standard for the assurance of all sustainability information. ISAE (NZ) 3410, *Assurance over Greenhouse Gas Statements* A49 is specific to the application of materiality for greenhouse gas emissions assurance. Extracts from ISAE (NZ) 3410 below may be tailored further for the assurance of greenhouse gas disclosures.

A percentage is often applied to a chosen benchmark as a starting point in determining materiality. Factors that may affect the identification of an appropriate benchmark and percentage include:

- The elements included in the GHG disclosures (for example, Scope 1, Scope 2 and Scope 3 emissions). A benchmark that may be appropriate, depending on the circumstances, is gross reported emissions, (as required to be disclosed under NZ CS 1) that is, the aggregate of reported Scope 1, Scope 2 and Scope 3 GHG emissions before subtracting any emissions deductions or removals. Materiality relates to the GHG emissions covered by the assurance practitioner's conclusion. Therefore, when the assurance practitioner's conclusion does not cover the entire GHG disclosures, (e.g. if an entity chooses to apply an adoption provision that exempts their reported scope 3 GHG emissions disclosures from the scope of the assurance)[22] materiality is set in relation to only that portion of the GHG disclosures that is covered by the assurance practitioner's conclusion as if it were the GHG disclosures.

- The quantity of a particular type of emission or the nature of a particular disclosure. In some cases, there are particular types of emissions or disclosures for which misstatements of lesser or greater amounts than materiality for the GHG disclosures in its entirety are acceptable. For example, the assurance practitioner may consider it appropriate to set a lower or greater materiality for emissions from a particular jurisdiction, or for a particular gas, scope or facility.

- How the GHG disclosures present relevant information, for example, whether it includes a comparison of emissions with a prior period(s), a base year, or a "cap," in which case determining materiality in relation to the comparative information may be a relevant consideration. Where a "cap" is relevant, materiality may be set in relation to the entity's allocation of the cap if it is lower than reported emissions.

- The relative volatility of emissions. For example, if emissions vary significantly from period to period, it may be appropriate to set materiality relative to the lower end of the fluctuation range even if the current period is higher.

[21] FAQs, Question 11
[22] NZ CS 2, adoption of Aotearoa New Zealand Climate Standards, paragraph 24

- The requirements of the applicable criteria. In some cases, the applicable criteria may set a threshold for accuracy and may refer to this as materiality. For example, the criteria may state an expectation that emissions are measured using a stipulated percentage as the "materiality threshold." Where this is the case, the threshold set by the criteria provides a frame of reference to the assurance practitioner in determining materiality for the engagement.

Question 7: How does the practitioner determine materiality if the quantitative disclosure is very small or near zero?

If the quantitative disclosure is very small or near zero, an understatement of the disclosure may be material. The practitioner therefore applies professional judgement in determining what is material in the circumstances.[23]

[23] The Guide, paragraph 305

Sources

ISSA (NZ) 5000, *General requirements for Sustainability Assurance Engagements*

NZ CS 1, *Climate-related Disclosures*

NZ CS 2, *Adoption of Aotearoa New Zealand Climate Standards*

NZ CS 3, *General requirements for Climate-related Disclosures*

International Standard on Sustainability Assurance (ISSA) 5000 Implementation Guide ("The Guide")

ISSA 5000 Frequently Asked Questions: The Application of Materiality (FAQs)