Key findings

The various definitions of materiality in the sustainability reporting arena are linked to the standard setters' conceptions of the purpose and perceived users of sustainability reporting. The connectivity of social and environmental issues that are material from an impact perspective and a financial perspective remains unclear, as is the extent to which social and environmental impacts and dependencies affect financial reporting practices. In this context, we highlight some of the key findings of this project.

1. Materiality assessment: current practices

- Not all companies are transparent about their materiality assessment process, yet those that disclose it undertake different approaches in sustainability reporting: 83% of the 225 companies adopt a double materiality approach, 13% adopt an impact materiality approach, and the remaining 4% adopt a financial materiality approach.
- There is not overwhelming evidence of misalignment between which sustainability issues are deemed as most material across sustainability and financial reports, but we observe some misalignment for corporate governance and environmental issues.

2. Double materiality: current challenges

- Technical challenges mainly relate to determining materiality thresholds, considering time horizons and stakeholders' knowledge and expertise.
- Cultural challenges may arise where sustainability issues are not regarded as core to the business, and this is further exacerbated when sustainability reporting teams are not integrated with financial reporting units.
- Institutional challenges reflect the current fragmentation of sustainability reporting standard setting such that companies need to reconcile or at least navigate guidance from multiple sources.

3. Connectivity

Different factors undermine the adoption of the traditional conceptualisation of materiality in the sustainability reporting domain, with reference to multiple users' information needs, diverse time horizons and the inherent uncertainty and complexity of the sustainability issues that need to be accounted for.

- Double materiality implies that issues are deemed material when they are material from an impact or financial materiality perspectives, but connectivity is enhanced when the two materiality assessments build on each other. Specifically, the definition of material topics should start from an impact materiality perspective. Then, the list of identified topics should also be assessed from a financial materiality perspective to allow considering which sustainability impacts may have financial implications. However, the underlying processes for sustainability and financial reporting are often siloed and disconnected, suggesting a lack of connectivity between sustainability and financial reporting. Regulation is yet deemed a factor encouraging greater connectivity between the two reporting processes.

- The identification of material impacts is challenged by the lack of active engagement with stakeholders possessing the relevant expertise needed to identify key social and environmental impacts.
- The notions of risk and corporate governance are useful to connect impact and financial materiality.
    - Climate change as a financial risk is an example of a sustainability issue enhancing the connectivity between sustainability and financial reporting.
    - Companies that implement corporate governance processes, such as setting up board-level committees that directly engage in materiality assessments and discuss sustainability issues, foster an understanding of the strategic implications of material sustainability issues.

4. Implications

- Foster cooperation between corporate sustainability and financial reporting teams to enable connectivity between both reporting arenas. This collaborative work would not only improve materiality assessments but also contribute to increasing the awareness of the information produced by both teams.
- A broad stakeholder base should be consulted through active and bidirectional engagements to identify which sustainability topics are material from an impact or financial materiality perspective. Organisations should ensure a fair representative stakeholder base of knowledgeable external and internal stakeholders.
- Users of corporate reports need to be cognisant that sustainability information may be disclosed in different locations. Both corporate governance and risk are key elements through which organisations may navigate complex sustainability issues and so users need to pay particular attention to these within their considerations.
- Users need to engage with the materiality assessment process and bring an informed perspective to this process. This requires an undertaking to develop their understanding of the sustainability context and its complexity.
- Standard setters should continue to cooperate to ensure compatibility across reporting standards and provide clear guidance on how materiality is to be understood and the process that organisations should establish to carry out materiality assessments. Guidance is needed in the key challenges that currently affect practice, such as the determination of thresholds, or the quantification of impacts, to ensure the robustness and consistency of those processes.