GreymatterFinch

UNPACKING MATERIALITY

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WHY IS IT KEY TO EFFECTIVE REPORTING?

> *"Things which matter most must never be at the mercy of things which matter least."*
> *— Johann Wolfgang von Goethe*

DEAR JOHN

German writer Von Goethe's wisdom reminds us not to let minor issues overshadow what truly matters. In the business world, it's easy to get sidetracked by trivial problems like a broken printer or desk placement, while more significant concerns – for example, data security – should demand our attention.

This is how the concept of materiality works; it acts as a lens through which to focus on what's truly essential.

> *"Materiality is like packing a backpack for a hike: you can only bring the supplies that are absolutely critical. Otherwise, the weight will slow you down and eventually bring you to your knees."*
> *- Gary Niekerk, former Director of Global Citizenship at Intel*

MAKING SENSE OF MATERIALITY

Materiality has long been a cornerstone of financial reporting, referring to information that can significantly influence investor decisions or a company's financial outcomes. By pinpointing material aspects, companies can ensure stakeholders receive vital, consistent, reliable data. While the term is well-defined in accounting, its application in sustainability reporting is more complex and often sparks debate. Questions frequently arise: What environmental, social, and governance issues are financially material? How are these determined?

This newsletter will illuminate some of the complexities of materiality. For those looking for further clarity, GreymatterFinch has done the heavy lifting and can assist you in navigating these intricacies.

WHO DECIDES WHAT IS MATERIAL?

In financial accounting, materiality is determined by the report preparer and auditor. In the realm of non-financial reporting, however, it involves considering the reasonable expectations of all stakeholders. The concept is highly context-specific, varying significantly across companies depending on their industry, business model and stakeholder priorities.

The board is the gatekeeper, steering the materiality process and giving the final nod on what really matters.

MATERIAL MATTERS VS RISKS

At GMF, we find that it is common for companies to conflate material matters with key risks. While there is some overlap, material matters encompass a broader scope, including opportunities and challenges that impact a company's value creation. In contrast, key risks specifically focus on potential threats.

DIVERSE DEFINITIONS AND PROCESSES

Determining what's material for the different elements of a reporting suite is no easy task, with various standard setters trying to bring clarity. Here are how different frameworks define materiality:

INTEGRATED REPORTING (Now part of IFRS Foundation): "A matter is material if it could substantively affect the company's ability to create value in the short, medium, or long term."

KING IV™: "Materiality is judged in terms of its inherent nature, impact, value, and the context in which it occurs."

GRI: "Reports should cover aspects that reflect significant economic, environmental, and social impacts or substantively influence stakeholder decisions."

IASB: "Information is material if omitting, misstating, or obscuring it could reasonably be expected to influence the decisions of primary users of general-purpose financial statements."

EFRAG: "Double materiality is a concept which provides criteria for determining whether a sustainability topic or information has to be included in the undertaking's sustainability report."

In addition, each framework has its own requirements for materiality determination. Financial accounting often uses quantitative thresholds, whereas sustainability reporting considers broader factors, including stakeholder engagement and risk assessments. The concept of "double materiality" combines financial and non-financial perspectives and is especially prevalent in European frameworks.

Most frameworks also require that reports include a description of the process followed – and these also differ! For instance, the Integrated Reporting Framework suggests summarising the process, while the GRI and European Sustainability Reporting Standards specify more detailed steps.

While not all the frameworks mandate disclosing a specific list of material matters, providing one can enhance understanding and facilitate better decision-making.

ASSURANCE AND MATERIALITY

With increasing regulatory requirements, particularly in Europe, the assurance of materiality processes is becoming more critical. Companies must ensure their materiality assessments are robust and capable of withstanding external scrutiny.

SO, WHY DOES MATERIALITY MATTER?

Materiality is not just about compliance; it's about understanding and communicating what truly matters. Companies can better align their strategies with stakeholder expectations, enhance transparency, and ultimately create long-term value by focusing on material issues.

Everything we've shared can be a bit overwhelming, especially given it is a dynamic and evolving landscape.

Effective communication, clarity and transparency are paramount, whether through an integrated report, sustainability report or other disclosures.

GMF can help your company determine what is material and communicate it effectively.

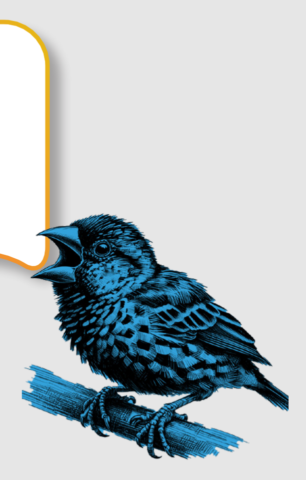
Email us today!

FORWARD TO FRIEND

GMF publishes a "Do you know" series that provides insight into the reporting value chain in bite-size chunks. These provide practical considerations for enhancing any company's reporting processes and outcomes.

Do you know the five steps to writing a concise report?

READ MORE



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