Materiality in sustainability reporting: multiple standards and looking for common principles and measurement. The case of the seven biggest groups in Spain

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Received June 22, 2017; accepted October 16, 2017.

ABSTRACT

This article is an approach to new definitions of materiality as applied to corporate performance and disclosure practices. Over time, the materiality lens will have implications for multiple operating areas. They will range from; risk and compliance to strategy setting, corporate policy and governance, management practices including stakeholder engagement, and even human resource management. In the second part there is a presentation of the definitions, scope and perspectives of materiality according to six relevant standard-setters in the field of sustainability reporting. Finally there is the presentation of how materiality is reported according to the six biggest groups of quoted companies in Spain.

KEYWORDS

Materiality reporting, Sustainability reporting.

JEL Codes: M14, M41.

1. Introduction

How to respond to new definitions of materiality as applied to corporate performance and disclosure poses one of the biggest challenges facing boards and senior executives. Traditionally, materiality has been defined through the lens of financial reporting. Now, there's a powerful and growing movement to apply a more expansive definition that includes disclosure of the risks and opportunities posed by sustainability issues such as climate change, human rights, and board accountability. In addition to the substantive issues affecting Environmental, Social and Governance (ESG) domains, other features of this new materiality framework include: longer time horizons in which to gauge impacts on corporate performance, greater uncertainty concerning outcomes, and the views of a wider group of stakeholders who impact, and are impacted by corporate behavior.

New materiality management calls for a different outlook on reporting and valuation—one that needs to be effectively managed and wired into a firm's operating system. Over time, the materiality lens will have implications for multiple operating areas. They will range from; risk and compliance to strategy setting, corporate policy and governance, management practices including stakeholder engagement, and even human resource management.

Numerous external forces are converging to create increased awareness of ESG factors. These forces are challenging Chief Financial Officers (CFOs) to reconsider a traditional reporting model that may not effectively meet today's information needs. CFOs are becoming more involved in sustainability, with a total of 83 percent of respondents stating that they are always involved or frequently involved in setting sustainability strategy (up from 65 percent in 2012) and 80 percent stating that they are always involved or frequently involved in executing sustainability strategy (up from 66 percent in 2012) at their organizations.¹

¹ *CFOs and Sustainability: Shaping their roles in an evolving environment*. Deloitte Sustainability Global Enterprise Risk Services.

http://www2.deloitte.com/content/dam/Deloitte/global/Documents/Risk/dttl-risk-Deloitte-CFOs_and_Sustainability-2014.pdf

Of the 250 largest companies in the world (G250 companies), 95 percent now issue separate sustainability reports. Moving forward, there likely will be greater alignment of traditional financial reporting and reporting on ESG topics. The International Initiative for Integrated Reporting (IIRC) is proposing integrating the disclosure of standard financial information with ESG information to provide a more complete view of the commercial, social and environmental context within which a company operates. Importantly, integrated reporting likely will require reporters to make valuation impacts of ESG information more explicit.

Right now, a disconnect often exists between what ESG information companies disclose to their stakeholders and the data that actually drives management and investment decisions. Most agree that it is hard to know which information is business-critical for the long run.

For these reasons, focus is increasing in the sustainability world on the principle of materiality as the essential filter for determining which ESG information will be useful to key decision makers.

2. Financial materiality: the big bang of the concept

In accounting practice, materiality is a central tool. It entails many financial aspects of disclosure, among them income tax allocation, treatment of renegotiation refunds, and risk issues (Bernstein, 1967). In the 1930s, the Securities and Exchange Commission (SEC) in the USA was concerned with the possibility that readers of financial statements would be swamped with unimportant information indiscriminately commingled with significant information (Bernstein, 1967). These public concerns about materiality originated with the legislation creating the Securities and Exchange Commission (SEC) in 1934. It continued with subsequent interpretations of its mandate to require disclosure of information for the protection of investors and the public interest. The SEC has continued to rule that qualitative, as well as quantitative, data can be considered material for disclosure purposes, even though financial disclosure has dominated.

Core to the definition of materiality is the notion that corporate information is material if its omission or misstatement would influence decisions made by general users of the information.

Definition of materiality and related guidance for financial reporting have evolved over the years, as new interpretations of materiality principles were adopted by standard setters, regulators, and international organizations. Their interest in materiality is much bigger than the environment because other non-financial areas have financial implications across the sustainability spectrum.

At the Exposure Draft ED/2015/8 *IFRS Practice Statement: Application of Materiality to Financial Statements*, the International Accounting Standards Board framed materiality as a process that provides a threshold or cut-off point that determines what will be included in a financial statement and what will be left out. It elaborates as follows:

- a) “Materiality is a general concept that is widely used both in financial reporting and for other purposes. For example, it is common for legal agreements to refer to material information, usually within a specific context such as referring to ‘material changes to the terms of the offer’ which may or may not be financial in nature.
- b) Information is material if omitting it or misstating it could influence decisions that users make on the basis of financial information about a specific reporting entity. In other words, materiality is an entity-specific aspect of relevance based on the nature and magnitude, or both, of the items to which the information relates in the context of an individual entity’s financial report”

Materiality is a general and pervasive concept and is widely used in financial and non-financial reporting and for many other business purposes. For example, business contracts may include ‘material adverse change’ clauses, which may or may not be financial in nature. A material adverse change (also called a MAC) - also formulated as an Material adverse event or Material adverse effect (either, a MAE) - contingency is a legal provision often found in mergers and acquisitions contracts and venture financing agreements that

enables the acquirer (or funder) to refuse to complete the acquisition or merger or financing with the party being acquired (often termed, the "target") if the target suffers such a change.

In planning the audit of a corporation, an auditor will establish a materiality threshold for purposes of determining the scope of test procedures, which would be different from the materiality threshold the auditor will use for purposes of rendering the attest report on the fairness of the client's financial statements taken as a whole. Materiality is frequently a legal concept as well because some countries, by either statute, case law or regulation, have established a definition of materiality they require to be applied in their jurisdiction. As an obvious consequence, it is not possible to establish a 'one size fits all' quantified definition of materiality.

Various definitions of materiality and related guidance for financial reporting evolved over the years, as new interpretations of principles of materiality were adopted by standard setters, regulators, and international organisations (Murningham, 2013). It is clear that in accounting practice, materiality is measured as an expected change/loss in net income expressed in accepted monetary terms. Any material indicator can be quantified as a monetary value added up in the yearly balance. The question is how and to what extent sustainable issues can be measured, if at all, especially taking into account that their effect might be long-term rather than annually-based.

Many corporate leaders, including sustainability managers, are focused on materiality beyond the traditional and well-understood financial statement materiality concept. These leaders recognize that the traditional interpretation of financial statement materiality does not adequately capture non-financial business drivers. GRI guidance encourages companies to consider what is material to stakeholders, but the guidance does not provide enough information on what that could mean for a company. Is it a visit to the emergency room because a child has an asthma attack precipitated by air pollution? Is it five such visits in a week because the family lives next to a facility which emits particulate matter that causes chronic infection of the lungs? Is it a fire in a Bangladesh clothing factory? Is it rainforest destruction? If so, how many acres and in what timeframe?

For many companies, the problem is not a lack of ESG issues that are important to stakeholders, but when and why these issues might become financially material. This is particularly difficult for ESG issues because they are often related to externalities and are not properly priced in the marketplace. Thus, without a clear price signal, figuring out materiality is a more subjective, rather than objective, endeavor especially if you are only looking at it from a traditional financial statement standpoint. The costs of the externalities to others in the community, supply chain and the broader ecosystem are real and can be quantified via health economics and environmental economics. This is knowledge that needs to be more integrated into corporate decision-making on the trade-off between total (social and environmental) costs and benefits of every product and technology. Omitting this information means that it has zero value to the company.

That's what AccountAbility set out to do in 1998 with the AA1000 Series of Standards, and what the Global Reporting Initiative (GRI) continued with issuance and periodic update of its Sustainability Reporting Guidelines. (The GRI's most recent reporting guidelines were released last October, 2016).

<https://www.globalreporting.org/information/news-and-press-center/Pages/First-Global-Sustainability-Reporting-Standards-Set-to-Transform-Business.aspx>

More recently, several simultaneous global conversations about expanding and codifying materiality are underway. They push the boundary even further, and are evolving in different ways, depending on scale, scope, and geography. What they hold in common is a belief in new frameworks, timeframes, and metrics. Their focus: climate risk, political contributions, human rights, supply chain integrity, bribery and corruption, diversity, product quality and safety, and corporate governance.

Widening the focus of materiality is the means by which the basis of mainstream financial assurance and reporting can absorb, or be absorbed into, the sustainability agenda.

According to noted authors Robert G. Eccles, Michael P. Krzus, Jean Rogers, and George Serafeim, most definition and interpretations of materiality are “principles-based” and

fairly general. (AccountAbility's AA1000 Standards are principles-based.) In the U.S., materiality is rules-based.

General guidance for both approaches occur within clearly definition accounting standards—a Generally Accepted Accounting Principles (GAAP) in the U.S., the International Financial Reporting Standards (IFRS) everywhere else—promulgated by groups such as the Financial Accounting Standards Board (FASB) in the U.S. and the International Accounting Standards Board (IASB) throughout the rest of the world. The authors Eccles et al. (2012) argue for a way of definition materiality that accommodates both rules-based and principles-based approaches.

At a corporate level, the challenge is not only to stay abreast of these conversations, but also to apply a methodology that's robust enough to definition those issues in anticipation of new disclosure requirements, and embed them into business models and long-term strategy.

Key questions become: How will you know which are the most important environmental, social, and governance issues that affect competitive performance, including.

3. Sustainability reporting (major) standard-setters and definition of materiality

Over the last three years, the total number of instruments that require or encourage organizations to report information about their sustainability performance has grown rapidly and significantly worldwide.

As continued pressure to integrate ESG factors into business practice and disclosure matures, there is an equivalent push for greater focus and disclosure on their definition and impact. This means tying them to specific performance outcomes within the context of sustainability realities. The aim: to provide key stakeholders, including investors, with insight into the continuum of ESG factors and how they will shape institutional performance. Already, there are signs of a context-based approach springing up throughout the world.

If everything is material, it's not material. Everything cannot be top priority. Everything cannot be most important. The complexity of sustainability, especially for large, global businesses, is vast. A list of potential material issues can run into hundreds of issues.

Key questions become: How will you know which are the most important ESG issues that affect competitive performance, including brand, reputation, and customer base? Who are you going to ask to answer this question, and how will you prioritize the answers? Once you've done that, how will you weave these sustainability risks and opportunities into your business strategy?

Early attempts to do this often involved creation of a “materiality matrix”, which featured issues considered important to both companies (on one axis) and stakeholders (on the other axis). While useful as a preliminary map, the effectiveness of materiality matrices is somewhat limited. That's because they often don't show the priorities of different groups, or the industrial benchmarks used by peers and investors to compare performance, or characteristics such as “innovation” that represent resilience and adaptability to changing times. They also don't show key sustainability performance indicators within an industry, or provide for future disruptive events or changes in stakeholder priorities that may change the mix.

Just as AccountAbility did in 2006, a new approach to materiality needs to focus on what is important to the business. But it needs to do this with a wider focus, in order to capture:

A longer-term view of the issues that could affect the success of its strategy.

A wider view of the people whose actions influence performance and who therefore need sound information to guide their judgments.

A deeper view of the information necessary for sound decision making, including where necessary both financial and non-financial data, and forward as well as backward looking indications of performance.

New definitions and management of materiality will affect virtually every aspect of corporate operations, from the board room through the supply chain and extending

through the product life cycle. At a minimum, CEOs, boards, and senior executives will need to familiarize themselves with recent developments and begin to sort through how they will link material sustainability issues to their financial reporting, stakeholder engagement and, increasingly, assess the impact of their sustainability performance (externalities) on a wider context. That's a process of discernment and development, as mentioned earlier, that involves a wide variety of corporate personnel and stakeholders, across disciplines and departments.

More than that, CEOs, boards, and senior executives will need to understand the strategic importance of material sustainability issues, and make sure they are effectively managed. "Effective management" calls for a suite of new knowledge and skills, building on what already is there, and is necessary to reporting, stakeholder engagement, and determining sustainability impacts. This involves new partnerships with reputable policy institutes and analysts, so that the substantive issues of material importance—on climate, human rights, corporate governance, economic and political stability, employee health and safety, supply chain performance, and so on—are comprehended and continually updated.

Finally, CEOs, boards, and senior executives will need to adopt a new framework for excellence, one that puts dynamic, emergent learning at the center, rather than more static "knowledge transfer"—because new materiality management is about managing for the future, not just reiterating what has worked in the past.

It is about foresight, not hindsight. Approaching new materiality management this way creates a climate conducive to innovation and experimentation—and failure, because after all, who can fully predict what the future holds?—that, in turn, reignites an entrepreneurial spirit so vital to competitive advantage and continued business success. The bonus: it's also vital to wider community well-being and prosperity, particularly for future generations.

Leading companies will seize the opportunity posed by new materiality management, and put processes into place to manage both financial and sustainability issues. Other groups in the corporate reporting ecosystem, of course, are also affected by these new definitions and applications of material sustainability priorities.

Accountants and auditors, management consultants, securities lawyers, investors, and advocacy groups will need to make adjustments in their goals and tactics.

For the moment in the next table there is a presentation of the definitions, scope and perspectives of materiality according to six relevant standard-setters in the field of sustainability reporting.

This too,	Definitions / Principle	Scope / Boundaries	Comments / Discussion
FASB	<p>Current: ‘Information is material if omitting it or misstating it could influence decisions that users make on the basis of financial information of a specific reporting entity. ...’</p> <p>Status as of February 2016: There is an active FASB project reconsidering the definition of materiality which has the potential for changes in the scope and general application for entities which report in accordance with US GAAP. No financial decisions have been made and overall project direction remains to be determined.</p>	In process of being evaluated with potential for revision.	In process of being evaluated with potential for revision.

Definitions / Principle	Scope / Boundaries	Comments / Discussion
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GRI	<p>‘Material Aspects’ are those that reflect the organization’s significant economic, environmental and social impacts; or that substantively influence the assessments and decisions of stakeholders.</p>	<p>Stakeholders broadly defined as entities or individuals that can reasonably be expected to be significantly affected by the organization’s activities or products and services; and whose actions can reasonably be expected to affect the ability of the organization to successfully implement its strategies and achieve its objectives.</p> <p>‘Aspects’ refers to the list of subjects covered by GRI guidelines and cover a range of a reporting entity’s economic, environmental and societal activities and impacts.</p>	<p>Materiality is the threshold at which aspects become sufficiently important that they should be reported (i.e. they become ‘Material Aspects’).</p>
IASB	<p>Current: ‘Information is material if omitting or misstating it could influence decisions that users make on the basis of financial information about a specific reporting entity. ...’</p> <p>Proposed: Information is material if omitting it or misstating it could influence decisions that the primary users of general purpose financial reports make on the basis of financial information about a specific reporting entity.’</p>	<p>Scope is narrowly defined as any assessment of materiality would be limited to the reporting entity and more specifically its financial statements prepared in accordance with IFRS. Intended audience is primary users of financial statements (current/potential capital providers, lenders) in order to assist in making hold, buy, sell, lend and similar investment and credit decisions. Further, primary users are defined to be those users with a general knowledge of business and economics and the willingness to diligently study the financial information presented.</p>	<p>Scope/boundary discussion is focused on the IASB’s proposed definition of primary users, which is somewhat more restrictive than their current definition. The Current definition is in the existing Conceptual Framework and the proposed definition is an Exposure Draft on a revised Conceptual Framework, which should be finalized in 2016. Materiality is assessed/evaluated in the context of how the omission or misstatement could influence primary users especially regarding their assessments of future cash flows and stewardship.</p>

Definitions / Principle	Scope / Boundaries	Comments / Discussion
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IIRC	<p>A matter is material if it could substantively affect the organization's ability to create value in the short, medium or long term.</p>	<p>Scope of reporting is towards providers of financial capital with focus on what is material to an assessment of how an organization creates value over time.</p>	<p>Frame of reference for assessing materiality is the organization's value creation process. This process is influenced by a range of factors, including the organization's use of or effects on 'the capitals'. The International <IR> Framework categorizes these capitals as financial, manufactured, intellectual, human, social and relationship, and natural capital. The materiality determination process applies to both positive and negative matters, including risks and opportunities and favourable and unfavourable performance or prospects. It also applies to both financial and other information.</p>
ISO	<p>An organization should review all the core subjects to identify which issues are relevant. The identification of relevant issues should be followed by an assessment of the organization's impacts. The significance of an impact should be considered with reference both to the stakeholders concerned and to the way in which the impact affects sustainable development.</p>	<p>Broad, inclusive definition of stakeholder as 'an individual or group that has an interest in any decision or activity of an organization. 'Scope' of reporting extends to both those activities an organization has control over but may situationally extend to other organizations and activities that the reporting entity has the ability to influence (its 'sphere of influence')</p>	<p>Uses word 'significance' in lieu of 'materiality' in ISO 26000 (Social Responsibility) guidance. Intention appears to be the same. Therefore, materiality/ significance needs to be very broadly evaluated, as stakeholder group is diverse and the reporting obligation appears to include/extend to non-controlled organizations or activities the reporting entity can influence.</p>

	Definitions / Principle	Scope / Boundaries	Comments / Discussion
SASB	<p>SASB standards are developed using the definition of “materiality” applied under the U.S. federal securities laws. That definition set forth by the U.S. Supreme Court in <i>TSC Industries v. Northway</i>, 426 U.S. 438 (1976), is that a fact is material if “there is a substantial likelihood” that a “reasonable investor” would view its omission or misstatement as “having signification altered the total mix of information.”</p> <p>SASB identifies sustainability topics that are reasonably likely to be material for a specific industry and then develops corresponding metrics. A company’s management must determine whether the relevant SASB standard should be used to comply with the disclosure requirements of the federal securities laws.</p>	<p>SASB standards are developed for 79 industries in 10 sectors and can be used by all public companies. The standards apply to U.S. and non-U.S. companies that access capital in the U.S. markets and are subject to SEC reporting requirements.</p> <p>The SASB recommends that issuers follow the same boundaries and timing as they use for financial reporting to the S.E.C., thus ensuring that financial fundamentals and material sustainability fundamentals can be analyzed in a similar context and compared year on year.</p>	<p>SASB standards are designed to be integrated into the MD&A and other relevant sections of mandatory SEC filings such as the Form 10-K and 20-F, so that information is reliable and all investors have access to material, comparable information without the need to source it from questionnaires or purchase it from commercial vendors.</p> <p>SASB’s standards development process is evidence-based and market-informed in order to ensure the standards are focused on information that is material, are cost-effective for companies and are decision-useful for investors.</p>

Table 1. Source: Corporate Reporting Dialogue. *Statement of Common Principles of Materiality*.

Available at: <http://corporatereportingdialogue.com/wp-content/uploads/2016/03/Statement-of-Common-Principles-of-Materiality1.pdf>

4. The case of the seven biggest groups in Spain

I have chosen these companies as global ones and for this reason I expect that targeted to emerging forms of capitalism and especially more worried about how companies implement sustainability principles in their businesses.

The most immediate resource for this is the Financial Times Global 500 that ranks companies by market capitalization – the greater the stock market value of a company, the higher its ranking.

Below I paste the original ranking for the seven Spanish companies included (at the moment of writing this paper the last available ranking at the date of Marc, 31 2015).

FT Global 500 2015										
Market values and prices at 31 March 2015										
Global rank 2015	Global rank 2014	Company	Market value \$m	Sector	Turnover \$m	Net income \$m	Total assets \$m	Employees	Price \$	P/e ratio
71	58	Banco Santander	105,960.3	Banks	N/R	7,032.7	1,504,392.0	185,405	7.5	13.2
76	79	Inditex	100,013.2	General retailers	22,539.1	3,203.5	17,825.6	128,313	32.1	31.2
123	117	Telefonica	70,326.6	Fixed line telecommuni	60,915.4	3,402.7	139,579.2	123,700	14.2	19.2
138	121	BBVA	63,794.0	Banks	N/R	3,165.7	749,112.6	109,239	10.1	19.1
258	224	Iberdrola	41,179.6	Electricity	36,314.8	2,813.2	106,328.9	28,212	6.4	14.6
442	325	CaixaBank	27,350.6	Banks	N/R	749.7	398,105.5	31,210	4.7	36.5
481	305	Repsol	25,592.9	Oil & gas producers	57,104.0	1,949.2	57,946.8	24,289	18.6	13.1

Table 2. Seven biggest Spanish groups in Financial Times Global 500

4.1. Banco Santander

In the “Sustainability report 2015” the “materiality of the process of sustainability report” was outlined in two pages of presentation called “Identification of material concerns”, and with very general and not detailed contents:

“ External sources:

- Among other factors, the external quantitative analysis considers the issues assessed by socially responsible investors, the sustainability objectives set by companies in the sector, the United Nations' Sustainable Development Goals and topics dealt with in the media.

Internal sources:

- The internal quantitative assessment considers and evaluates the issues dealt with by the Bank's sustainability committees over the previous five years and in institutional communications, and the issues of the most concern in its internal communication channels, and its corporate intranet and Santander News platform.
- Analysis is also carried out to identify the main stakeholders and relevant issues throughout the Bank's value chain.

And the information is synthetized with this graphic:

New variables were introduced in 2015 to enhance this analysis.

Main material concerns identified:

Talent attraction and retention, respect for diversity and promotion of active listening.

Customer satisfaction, service quality and correct management of complaints and incidents.

Transparency of information about products and services, simplicity and trust.

Products and services with an environmental/ social focus to help the development of local communities and protect the environment.

Multichannel structure and digitalisation, innovation as a key, strategic factor.

Compliance, reputational, social and environmental risk control and management.

Reducing consumption and emissions.

Anti-fraud and corruption mechanisms.

Community investment.

Corporate governance and adaptation to regulatory changes.

Graphic 1. Banco Santander “Sustainability report 2015”

4.2. Inditex

Materiality analysis

In line with its sustainability policy, Inditex's stakeholder relations are based on ongoing dialogue and transparency. Inditex engages in dialogue to identify the most important issues for those parties linked with the Group. For example, the company uses the materiality analysis to ensure that her strategy is aligned with the concerns and expectations of those associated with the company or affected by her activities, as well as to decide on the content of Inditex's Annual Report. These concerns and expectations, along with sustainable value creation, give the programmes run by Inditex purpose and allow the company to deal with the challenges and opportunities it faces in the course of its activities.

This is the fifth consecutive year (2015) that Inditex has gone through the exercise of analysing and prioritizing issues relevant to the Group.

For this materiality analysis, Inditex followed the GRI - G4 guidelines and the Integrated Reporting Framework. Last year 2015, the Group also reviewed the list of relevant issues in light of the current state of the industry, and expanded the list of stakeholders consulted. Inditex also has at its disposal a Social Council that advises the Group on sustainability issues.

The Council's members are external individuals or institutions independent from the Group. Its purpose is to formalize and institutionalize dialogue with key actors in the civil society within which Inditex develops its business model. The Social Council played an active role in preparing the materiality matrix.

Process of preparing the Inditex materiality matrix

The material issues were categorized according to the five areas identified by the United Nations, which encompass the 17 Sustainable Development Goals, in order to align the strategies and programmes for addressing these issues with the SDGs and their targets

Graphic 2. Inditex Annual Report (2015)

Balance of material issues

Material issues	Related GRI indicator	Category	Coverage	Section of Annual Report 2015	Pages
1 Commitment to customers	G4-PRS			Innovation in customer services	94
2 Product quality, health and safety	G4-PR1 to G4-PR4			Integrity of the supply chain, The quality of our products	36, 58
3 Product information and labelling	G4-PRS			The quality of our products, Innovation in customer services	58, 94
4 Changes in consumption habits	Strategic business issue			Retail formats, Innovation in customer services	14, 94
5 New sales channels	Strategic business issue			Commercial presence, Retail formats	12, 14
6 Security and protection of data and information systems	G4-PRB			Innovation in customer services	94
7 Labour practices	G4-LA3, G4-LA4, G4-LA12, G4-LA13			Developing everybody's talent	80
8 Attracting and retaining talent	G4-LA1, G4-LA2, G4-EC3			Developing everybody's talent	80
9 Developing human capital	G4-LA9 to G4-LA11			Developing everybody's talent	80
10 Health and safety at suppliers and manufacturers	G4-LA5 to G4-LA9, G4-LA14, G4-LA15			The quality of our products, Sustainability balance sheet	36, 144
11 Eco-Design	G4-EN1 to G4-EN14, G4-EN27 to G4-EN29			The quality of our products, Sustainability balance sheet	58, 144
12 Volatility of raw material prices	Strategic business issue			The quality of our products, Efficient use of resources	58, 70
13 Energy consumption and GHGs	G4-EN3 to G4-EN7, G4-EN15 to G4-EN21, G4-EN30			Efficient use of resources, Sustainability balance sheet	70, 144
14 Water consumption and controlling discharges	G4-EN8 to G4-EN10, G4-EN22, G4-EN24, G4-EN26, G4-EN32 to G4-EN34			Integrity of the supply chain, Efficient use of resources, Sustainability balance sheet	36, 70, 144
15 Waste control and management	G4-EN22 to G4-EN26			Integrity of the supply chain, Efficient use of resources, Sustainability balance sheet	36, 70, 144
16 Management of product end of life and circular system	G4-EN23, G4-EN25, G4-EN27 to G4-EN29			Integrity of the supply chain, Efficient use of resources, Sustainability balance sheet	36, 70, 144
17 Protecting biodiversity	G4-EN11 to G4-EN14			Integrity of the supply chain, Efficient use of resources	36, 70
18 Animal welfare	G4-EN11 to G4-EN14			The quality of our products	58
19 Corporate governance	G4-S4 to G4-S5, G4-S06			Corporate governance	114
20 Transparency and tax contribution	G4-EC1, G4-S08, G4-PR9			Corporate governance, Tax contribution	114, 158
21 Compliance with regulations and responsible practices	G4-S6 to G4-S8, G4-S03 to G4-S05, G4-S08, G4-S011, G4-EN29, G4-PR9			Corporate governance	114
22 Socio-economic impact on the community	G4-EC1 to EC4, G4-EC7, G4-EC8, G4-S011			Contribution to community welfare, Sustainability balance sheet	98, 144
23 Human rights and industrial relations in the supply chain	G4-LA14 to G4-LA16, G4-HR1 to G4-HR6, G4-HR10 to G4-HR12, G4-S09 to G4-S011			Integrity of the supply chain, Sustainability balance sheet	36, 144
24 Traceability of the supply chain	G4-L2, G4-EN32, G4-EN33, G4-LA14, G4-LA15, G4-HR18, G4-HR11, G4-S09, G4-S018, G4-PR1, G4-PR2			Traceability of the supply chain	32
25 Responsible purchasing practices	G4-L2, G4-EN32, EN33, G4-LA14, LA15, G4-HR18, HR11, G4-S09, S010, G4-PR1, PR2			Integrity of the supply chain	36
26 Changes in regulation	Strategic business issue			Corporate governance	114
27 Logistics model	Strategic business issue			Efficient use of resources, Sustainability balance sheet	70, 144
28 Expansion in new markets	Strategic business issue			Commercial presence, Retail formats	12, 14
29 Exposure in mature markets	Strategic business issue			Commercial presence, Retail formats	12, 14
30 Risk management and control systems	Strategic business issue			Innovation in customer services, Systems for control of risks	94, 236
31 Investment in the community	G4-EC1 to G4-EC4, G4-EC7, G4-EC8, G4-S01, S02			Contribution to community welfare, Sustainability balance sheet	98, 144
32 Stakeholder engagement and dialogue	G4-24 to G4-27			Traceability of the supply chain, Integrity of the supply chain, The quality of our products, Efficient use of resources, Developing everybody's talent, Innovation in customer services, Contribution to community welfare, Corporate governance	32, 36, 58, 70, 88, 94, 98, 114

Sustainability

Business

Within the organization

Outside the organization

Within and outside the organization

Table 3. Inditex Annual Report (2015)

Graphic 3. Inditex's Annual Report (2015)

The following organizations, among others, have been consulted in the definition of material issues for 2015

Cáritas Española	Medicus Mundi
Spanish Committee for UNHCR	International Labour Organization
Cruz Roja	Textile Exchange
Entreculturas	The Humane Society of the US
Fundación SERES. Sociedad y Empresa Responsable	UN High Commission for Refugees
IndustriaALL Global Union	University of Santiago de Compostela
Médicos Sin Fronteras	Water.org

Table 4. Inditex Annual Report (2015)

4.3. Telefonica

Every year Telefónica carries out a materiality analysis process in order to identify those issues which require special attention for the sustainability of the Company.

Among other aspects, the Company have based her analysis on the materiality analysis designed by the Global e-Sustainability Initiative (GeSI) in November 2014, which is specifically for the whole value chain of the ICT hypersector. As can be seen via this link (http://gesi.org/news?news_id=73), the GeSI analysis preselects 55 potentially material issues, divided into eight categories: digital inclusion, employees, climate change, supply chain, customers, privacy, governance and impact on communities.

At Telefónica they called upon all the stakeholders related to the Company to help them preselect the 55 material issues which have a key impact on their activity. The stakeholders who have collaborated on the project are: Alcatel-Lucent, Amdocs, AT&T, Bell, Bkash, Bolo Phi, Bosch, BSR, BT, Calvert, Deutsche Telekom, Ericsson, ETNO, Everything Everywhere, Forum for the Future, GeSI, Green Electronics Council, Greenpeace, GSMA, HP, Huawei, Institute for Public and Environmental Affairs (IPE), Institute of Contemporary Observation (ICO), ITU, KPN, Nokia, OTE, SACOM, SAM Robeco, SASB, Seagate Technology, Skyworks Solutions Inc., Solving the e-Waste Problem (StEP), Sony Mobile, Sprint, Swisscom, TDC Group, Telecom Italia, Telefónica, Telenor, TeliaSonera, Telstra, The Consultative Group to Assist the Poor (CGAP), The Energy and Resources Institute (TERI), The Sustainability Consortium, United Nations University, Verizon, VimpelCom, Vodafone, World Resources Forum and WWF.

The results of the external and internal analysis enable the Company to establish the level of total importance of the material issues for Telefónica, as shown below, to group them according to field - financial, environmental or social - and present them graphically in the matrices which can be seen on next pages.

All these issues are material within the organisation. With regard to the scope of the information on external issues, please see the chapter on ‘Structure and scope of consolidation’ in the Integrated Report.

The materiality analysis process that the Company carries out annually enables them to identify issues of particular importance in terms of their impact on Company strategy and of their relevance to our stakeholders, which helps in the establishing of priorities and courses of action.

Main material issues for Telefónica

The thorough analysis revealed information which plays a key role for a company in which the interconnection between environmental, social and economic factors is increasingly intense, and concluded that the most important aspects are:

Graphic 4. Telefonica Annual Report (2015)

Three kinds of materiality matrix: Economic, Social Affairs and Environmental.

Economic Affairs Matrix

1. Quality of service
2. Data security
3. Ethical business practice
4. Transparency
5. Tax contributions
6. Public policy and relations with public bodies
7. Impact on communities
8. Impact on customers' lifestyles
9. Innovation
10. Corporate governance

Social Affairs Matrix

1. Privacy
2. Online cybersecurity
3. Occupational standards in the supply chain
4. Freedom of expression
5. Child protection
6. Health, safety and occupational well-being
7. Accessibility
8. Minerals in conflict
9. Talent acquisition and development
10. Diversity

Environmental Affairs Matrix

1. Energy consumption
2. Green and Smart services
3. Carbon emissions
4. Reuse and recycling of devices
5. Waste electrical and electronic equipment (WEEE)
6. Electromagnetic fields in networks
7. Responsible network roll-out
8. Infrastructure sharing
9. Environmental management systems
10. Environment and climate change
11. Electromagnetic fields in devices
12. Adaptation to climate change
13. Water
14. Fluorinated gases
15. Renewable energy
16. Paper

Graphic 5. Telefonica's Annual Report (2015)

4.4. BBVA

The process of defining material issues has been bottom-up: in other words, each of the countries has carried out its materiality exercise taking into account the local reality. All the exercises have then been consolidated to give a global vision of the Group. This methodology has been prepared following the recommendations on disclosure in the GRI G4 sustainability reporting guidelines.

The final result of the process is a materiality matrix in which each of the relevant issues identified is classified according to two variables: importance for stakeholders and importance for the BBVA business.

1. Process of defining material issues

a) Identification of material issues:

To draw up the final list of material issues, BBVA has used those issues that have been defined as reputational risks for the company and identified other material issues that do not represent a risk.

In both cases the sources used have been:

Research and contacts that provide information on stakeholder perceptions through the consultation tools described in the above section.

Analysis of information from expert observers (NGOs, sustainability analysts, labor unions and other civil associations) that assess company behavior.

Regulatory trends in the sector.

Analysis of competitors: the most relevant issues or controversial subjects that affect them and that may also affect us.

Analysis of the media and social networks: negative news, trending topics, social concerns, etc.

b) Prioritization of material issues:

c) BBVA have analyzed two aspects for prioritizing material issues: relevance for stakeholders and relevance for the BBVA business.

Relevance for stakeholders: To measure the relevance of these issues for stakeholders, the company have taken into account how important the issues are for these groups, as well as whether there are legal requirements or related commitments entered into by BBVA. Thus, an issue is more relevant:

The greater the number of stakeholders affected and the greater the importance of these stakeholders for BBVA.

The greater the impact of the issues for the stakeholders affected.

When there are legal requirements or commitments by BBVA related to the issue.

Relevance for the business: The relevance for the business involves determining the impact the issue has on BBVA's current and future business. The global Responsible Business Department identifies those responsible for managing each issue at global level and they then identify their local counterparties. These counterparties are those who have calculated the impact on the business of the issues within their area of management.

2. Materiality matrix

In accordance with this process, BBVA has built a materiality matrix for each country. This has then been used to obtain a global materiality matrix for the whole Group.

The consolidation process has been carried out by taking a weighted average of the relevance for the stakeholders and for the business in all the countries. The weighting used has been the gross income in each country.

The resulting global materiality matrix is as follows according to the next 25 items:

- 1) Products with good value for money (without abusive clauses).
- 2) Communication and commercialization practices: foster informed decisions.
- 3) Quality of customer care and service.
- 4) Response to the demand for credit in society.
- 5) Customer security, privacy and protection (including big data).
- 6) A solution for customers in a difficult situation.
- 7) Quality of employment (temporary, outsourcing, relocation, etc.).
- 8) Respect for employee rights.
- 9) Talent attraction, development and retention.
- 10) Remuneration policy for senior management and the Board of Directors.
- 11) Social and environmentally responsible finance.
- 12) Prevention of money laundering and terrorist financing.
- 13) Compliance with the tax code.
- 14) Ethical behavior.
- 15) Responsible procurement and outsourcing.
- 16) Good corporate governance.
- 17) Financial solvency and management.
- 18) Respect for human rights.
- 19) Contribution to the development of local communities (job creation, support for SMEs, etc.).
- 20) Financial inclusion.
- 21) Community involvement not linked to the business.

22) Diversity and work/life balance.

23) Eco-efficiency and the environment.

24) Digitalization: providing customers with the benefits of digitalization.

25) Financial literacy.

Graphic 6. BBVA Annual Report (2015)

4.5. Iberdrola

Iberdrola has been using GRI's Sustainability Reporting Guidelines as a model for preparing its annual sustainability report since 2003.

According to GRI, these guidelines are the result of a process in which various stakeholders throughout the world have participated, with representatives from business, unions, civil society, the financial markets, auditors, and specialists from various disciplines in the business area, regulators, and governmental bodies from various countries.

Iberdrola is, in turn, a multinational company with a presence in countries on various continents and with diverse economic and social models, and in recent years it has developed systems and processes to obtain the information needed to meet requests in this regard both by GRI, with its recommendations, and by other areas with heightened awareness on sustainability issues, such as the Dow Jones Sustainability Index and the Carbon Disclosure Project.

Iberdrola therefore believes that the issues identified in the GRI guidelines and in the Electric Utilities Sector Supplement are based on the broad participation of corporate stakeholders and sufficiently meet the requirements of materiality to be included in its sustainability report, with no exclusions.

The report for financial year 2014 also maintains the information on the issues identified in the GRI guidelines, providing continuity to the information from prior financial years. These issues are specifically identified in Annex 1 to this report.

Iberdrola has also performed its own Materiality Analysis in order to identify specific issues of interest relating to the Company's activities, which analysis was performed with the advice of an independent external firm.

In this analysis, carried out in financial year 2013 and considered valid for all purposes for financial year 2014, nine issues have been identified as "necessary" based on the levels

of maturity and significance of the issues of interest relating to the activities carried out by the Group, as shown in the graphic below:

Materiality Analysis of the IBERDROLA Group

Most significant material issues

Electricity generation
 Renewable energy development
 Price risk management
 Climate change strategy
 Business opportunities
 Government relations / public policy / lobbying
 Customer relations management
 Local community impacts and benefits
 Transmission and distribution

Graphic 7. Iberdrola Annual Report (2014)

4.6. Caixabank

MATERIALITY STUDY

The analysis is written in an appendix to the Integrated Corporate Report (2015). This appendix is a supplement to the 2015 CaixaBank Integrated Corporate Report, providing an overview of the bank's position, its management model and strategies.

The 2015 report aims to address those topics influencing CaixaBank's ability to create value in the short, medium and long term, which are also of interest to the bank's stakeholder groups.

Upon completion of the process and once the topics to be included and their degree of relevance were determined, the bank decided to report on all those topics that are highly relevant both for the entity and for its stakeholders.

Graphic 8. Caixabank Annual Report (2015)

4.7. Repsol

Repsol states that the sustainability report has been drawn up according the directives of the “Sustainability Reporting Guidelines” of the Global Reporting Initiative, in the G4 version thereof and the sector supplement for oil and gas businesses, in the exhaustive option. Moreover, the report has been completed with the basic principles governed by Standard AA 1000 2008 APS: inclusivity, materiality and accountability, and verified according to Standard AA 1000 2008 AS.

Repsol define materiality as the wide range of topics on which the company accounts on its performance in the economic, environmental and social issues and that substantially influence the evaluations and decisions of its stakeholders.

To determine materiality, Repsol have brought together internal factors such as the company’s mission, competitive strategies and its risk map, with external factors such as the concerns and expectations directly expressed by the stakeholders in the studies to identify expectations. Such studies, based on the recommendations in Standard AA 1000, are aimed at identifying and listing the concerns and expectations of Repsol’s stakeholders on a global and local level.

Repsol conducted in-depth interviews on a sample of around 100 representatives from the stakeholders identified, to which we have added an analysis of the media.

The process to define the content is made up of 3 phases:

- Phase 1: Identification of the relevant aspects and issues and the coverage thereof, starting from the principles within the context of sustainability and shareholder participation, as well is the impact on the business.
- Phase 2: Prioritization of the material aspects and issues identified by the stakeholders and the company.
- Phase 3: Validation of the material aspects and issues, applying the principles of exhaustiveness and stakeholder participation.

Repsol have identified 19 material issues with average and high priority related to the areas of governance, economics, security, environment and social matters, which are shown in the following figure.

1 Local communities	11 Governance, ethics and transparency
2 Economic development	12 Leaks
3 Safety	13 Water
4 Energy efficiency and climate change	14 Relationship between the business and the employees
5 Corruption	15 Compliance
6 Supply chain	16 Waste
7 Due diligence	17 Diversity and equal opportunities
8 Labour conditions, training and development	18 Emissions (not Greenhouse Gases)
9 Indigenous rights	19 Participation in public policy
10 Biodiversity	

Graphic 9. Repsol Annual Report (2015)

The most relevant stakeholders identified, whose concerns that Repsol have analyzed in the materiality study, are the following

- Employees
- Investors
- National public bodies and institutions
- International bodies
- Suppliers and contractors

– Civil society

5. Conclusions

Materiality determination is one of the most complicated ESG-related decisions for senior management, which faces considerable uncertainty related to ESG topics. With limited resources at hand, managers should choose a small set of material performance indicators that inform on valuation impacts and consistently report data, and they should focus less on trying to satisfy every one of the company's stakeholders. Furthermore, ESG materiality determination need not be a qualitative "finger to the wind" exercise. Decision science methods can help corporate leaders and CFOs effectively leverage the intelligence that is gained from all key stakeholders by applying a more structured approach to stakeholder engagement.

They can also help management make strategic choices, including capital budgeting decisions. More importantly, the result is quantitative and based upon fundamental insights into how complex decisions are made.

The level of detail covering the underlying process of materiality determination is very variable. Many companies simply refer to external guidance, whilst others offer substantially more information.

Based on published data we have reviewed the range of inputs used to evaluate the level of significance along both the stakeholder and company axes. We find that, in the main, companies disclose much more detail about the stakeholder aspect than the internal company process.

Generic, according to reporting (GRI in the majority of the cases) and not clear related with the strategy of the companies.

The Materiality Principle of the GRI Guidelines defines materiality in the context of a sustainability report:

"The report should cover Aspects that:

- Reflect the organization's significant economic, environmental and social impacts; or

- Substantively influence the assessments and decisions of stakeholders.”

Organizations are faced with a wide range of topics on which they could report. Relevant topics are those that may reasonably be considered important for reflecting the organization’s economic, environmental and social impacts, or influencing the decisions of stakeholders, and, therefore, potentially merit inclusion in the report. Materiality is the threshold at which Aspects become sufficiently important that they should be reported. Beyond this threshold, not all material Aspects are of equal importance and the emphasis within a report should reflect the relative priority of these material Aspects.

Many of the companies surveyed make it very clear that the results of their materiality determination process guide their sustainability strategy. Only a very small minority say that the materiality analysis impacts went beyond sustainability management and actually had a direct influence over their main business strategy.

However, many questions around strategic alignment are often left unanswered. In particular:

- ☐ should an issue deemed to be material in a sustainability matrix automatically be considered material under a more conventional accounting approach?
- ☐ if not immediately, over what frame might this be expected to happen, if at all
- ☐ should sustainability and traditional accounting and accountability remain separate or be combined into an integrated process?

The use of a materiality determination process has certainly brought a clearer focus to sustainability reporting, with leading reporters disclosing better linkages between sustainability indicators and their company’s primary business objectives. The underlying approach, first articulated by AccountAbility, is widely adopted and appears to be quite workable, although it does have inherent limitations.

In order to improve things still further the following recommendations are made. Companies should be encouraged to:

- ☐ adopt a materiality process, if one is not already in place;

- publish a quantified and populated materiality matrix;
- disclose the underlying process and scoring mechanisms;
- review results against peers to avoid inexplicable anomalies;
- provide much more detail on how company impacts are assessed;
- converge sustainability and business materiality assessments;
- investigate supplementary data feeds;
- consider full life cycle impacts; and
- work towards an integrated reporting platform

Materiality of ESG topics needs to be tied to potential valuation impacts on the business, even over the long term and when these impacts are uncertain. Otherwise, much of the ESG information that is disclosed will likely remain marginal to business and investment decisions. The selection of ESG metrics needs to be tied to corporate strategy, value drivers, organizational objectives, and the competitive environment—using a combination of quantitative and qualitative information. The challenge faced by companies that disclose ESG information is that in many cases the valuation impact of ESG topics is not well understood and there are far too many ESG topics to choose from. The question we have raised here is: With so much uncertainty and complexity, can companies successfully prioritize ESG topics to disclose only those that are material?

Certainly, the process would be much easier if we had a single scale to effectively balance a company's needs with those of its stakeholders, and to prioritize ESG topics by their relative likelihood to be material. Managers need a quantifiable manner in which to balance these needs and calibrate whether their company is fully achieving its potential to create value. That scale is not yet in dollars and cents, so we have to look elsewhere. Given today's immature state of knowledge on ESG valuation impacts, decision science methods are a powerful tool that can help managers develop a single scale and structure some of the complexity involved in ESG topics, including the subjective biases of multiple stakeholders. Using these methods can augment the credibility of ESG materiality determination and can allow business leaders to better defend their decisions about ESG management, investment, and disclosure on matters of value to their myriad stakeholders. With these decision tools in hand, business leaders can shed more light on

how superior performers create long-term business value and sustain the underlying asset base—financial, human, manufactured, social, and natural.

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