Material or Not: That is the Question in ESG Reporting



In This Thought Piece

In this thought piece we explore the evolving concept of materiality within the world of corporate environmental, social and governance (ESG) reporting and four "types" of materiality that have emerged: financial materiality, impact materiality, double materiality and dynamic materiality.

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Introduction: Material or Not, That is the Question

"To be or not to be," one of Shakespeare's most iconic questions, also belongs center stage in corporate environmental, social and governance (ESG) reporting – namely, whether ESG information is material and worthy of public disclosure.

From a corporate reporting standpoint, the concept of materiality is grounded in the idea that companies should disclose to investors information they need to make decisions. Through regulations, guidance and case law, U.S. securities law has defined what constitutes materiality for the purpose of filing documents with the Securities and Exchange Commission (SEC). Information is deemed "financially material" if there is a substantial likelihood that a "reasonable investor" would consider it important to their decision-making around buying or selling securities or issuing shareholder votes.¹ As the Sustainability Standards Accounting Board (SASB) explains, "...in many jurisdictions, [materiality] is the basis for determining whether a company may be exposed to fines or lawsuits for making a false or misleading statement about a material matter or for omitting information about a material matter."²

For decades, however, a growing number of investors, asset managers, employees, non-governmental organizations, and other stakeholders have been asking companies to go beyond SEC-mandated financial materiality in their reporting. They recognize that managing ESG risks poorly around issues like climate change, human capital and business ethics could lead to increased costs and liabilities – and that managing such risks well and innovating around them could lead to positive returns. This movement, which has gained significant momentum in recent years, has expanded the realm of what companies are considering material, especially as they strategize on long-term value creation and risk management.

¹ Handy, Allison C. and Feldis, Kevin R. (July 13, 2021). Sustainability Disclosures: What Is Material?

 ² Sustainability Accounting Standards Board (SASB). Fundamentals of Sustainability Accounting Level I Study Guide. (March 2021).
 p. 66.

Originally defined by the Global Reporting Initiative (GRI) in 2011, "impact materiality" (or "environmental and social materiality") reflects an organization's significant economic, environmental, and social impacts – even if such impacts are not (yet) financially material. In 2019, the European Commission began requiring companies to report disclosures that are doubly material in order to understand both a company's "development, performance and position" (financial materiality) and its "external impacts" (impact materiality).³ By the end of 2020, 96% of the 250 largest companies globally (the G250) were reporting on their sustainability performance, with 73% of the G250 and 67% of the N100 (5,200 companies comprising the largest 100 firms in 52 countries) using the GRI framework and its definition of impact materiality.⁴



In the United States, debate continues in some circles around what ESG topics might be material for public disclosure and if such disclosures should be regulated. In 2021, the SEC announced it would begin analyzing the accuracy, gaps and misstatements in public company disclosures around climate risks and other ESG factors, and is set to propose rulemaking on climate risk and human capital management disclosures sometime this year.

⁴ KPMG. (December 2020). The Time Has Come: 2020 KPMG Survey of Sustainability Reporting.

³ European Commission. (2019). *Guidelines on reporting climate-related information*.

Conceptions of Materiality within the SEC

Not all SEC Commissioners agree on whether ESG information is financially material to investor decisions – or if the SEC should specify such disclosures.⁵

On the one hand, Commissioners Hester Peirce and Elad Roisman have stated that they do not think that ESG issues are financially material, nor should they be part of securities laws – unless Congress mandates their disclosure and until one set of investor ESG expectations and comparable metrics exists (as they do in financial reporting).

On the other hand, former Acting Chair Allison Herron Lee has stated that "the idea that the SEC must establish the materiality of each specific piece of information required to be disclosed in our rules is legally incorrect, historically unsupported, and inconsistent with the needs of modern investors, especially when it comes to climate and ESG."⁶

And, without using the exact term, SEC Chairman Gary Gensler explained the concept of dynamic materiality at the Principles for Responsible Investment's "Climate and Global Financial Markets" webinar in July 2021:⁷

"Over the decades, there's been debate about disclosure on things that, today, we consider pretty essential for shareholders. The first disclosures revolved around companies' financial performance. Then, there was investor demand for information about who runs the company. Later, investors wanted more information on how much a company's resources were dedicated to paying those executives... Of course, there was opposition to many disclosure requirements that have become so integral to our regime that it's hard to imagine investors making a decision without them. So why am I talking about climate risk? Simple: because investors are. Today, investors increasingly want to understand the climate risks of the companies whose stock they own or might buy. Large and small investors, representing literally tens of trillions of dollars, are looking for this information to determine whether to invest, sell, or make a voting decision one way or another."

⁵ Handy, Allison C. and Feldis, Kevin R. (July 13, 2021). *Sustainability Disclosures: What Is Material?*

⁶ Lee, Allison Herren, U.S. Securities Exchange Commissioner and former Acting Chair. (May 24, 2021.) *Living in a Material World: Myths and Misconceptions About "Materiality.*"

⁷ Gensler, Gary, U.S. Securities Exchange Commissioner and Chair. (July 28, 2021.) Prepared Remarks Before the Principles for Responsible Investment "Climate and Global Financial Markets" Webinar. Washington, D.C.

Examples of Materiality in ESG Reports

Given the evolving nature of ESG and materiality, how have U.S. companies been disclosing ESG information that they determine is material to their business?

Some use tables, Venn diagrams, or other infographics to list material ESG topics grouped under the headings of environmental, social or governance and/or under the types of stakeholder groups that identified the issues as impactful.

Left to right, top to bottom: Citigroup Inc., Healthpeak Properties and Broadcom use tables or Venn diagrams in their latest ESG annual reports to show ESG issues material to their businesses and stakeholders.

Material ESG Topics*			Key Stake	eholders		
	Clients and Customers	Employees	Suppliers	Communities and NGOs	Shareholders	Governmen and Regulato
Environmental						
Biodiversity	•			•	•	
Climate Change	•	•	•	•	•	•
Environmental Justice	•		•	•		
Operational Footprint		•	•			•
Products and Services with Environmental or Social Benefits	•		•	•	•	
Social						
Community Investment		•		•		
COVID-19	•	•	•	•	•	•
Employee Health and Well-being		•	•			•
inancial Inclusion	•			•	•	E
luman Rights	•	•	•	•	•	Ву
tacial Equity/Racial Justice	•	•	•	•		bu all
alent Attraction, Retention and Development		•			•	S1 EV
Workforce Diversity, Inclusion and Equal Opportunity		•		•	•	an toj wł
Sovernance						ea loc
Business Ethics	•	•	•	•	•	
Susiness Model Resilience	•				•	s 0
Pata Security/ inancial Product Safety	•	•	•	•	•	E
SG Governancee	•	•			•	
nnovation and Digitization	•	•				s
Public Policy and Regulation Reform	•			•	•	d
itakeholder Engagement	•	•	•	•	•	· ·
iystemic Risk Management	•				•	P
ransparency and Trust	•			•	•	Ę
or issue definitions, see next page.						

ESG Materiality Assessment

By conducting a regular ESG materiality assessment, we maintain focus on the ESG issues that are most important to our business and key stakeholders. Our materiality assessment, which is informed by stakeholder engagement and analysis, ako allows us to continually refine our ESG initiatives to ensure they are meaningful and impactful. Stakeholder Engagement

Every year, we engage formally, and informally with our stakeholders to determine the material economic, environmental, social and governance area of focus for our concomposity. We use regular tracholder engagement rais and redback to isolarity material topics and ESS initiatives. This process allows us to identify and refine the issues that are nost important to our stakeholder, which is critical to our science. The table that follows simulatizes one of our ley stabiliseder engagement practications for each of identified material stakeholder groups: employees; stochholders; terrants and operators ("partners"); and our local communities.

STAKEHOLDER GROUP	ENGAGEMENT	DESCRIPTION			
	Annual Satisfaction Survey	Engagement tool for our employees to review performance, submit ideas, and relay concerns			
ä	Regular Town Hall Meetings	Platform to engage directly with employees and provide a Q&A forum with our CEO and executive leadership team			
Stockholders	Ongoing Outreach	Direct engagement with our investors to address ESG matters			
စို့စို့	Industry Events, Investor Conferences and Meetings	Opportunity to engage directly with investors and industry peers at conferences and events, as well as one-on-one investor meetings			
Partners	Annual Tenant Satisfaction Survey	Engagement tool for our tenants to review performance, submit ideas, and relay concerns			
	Healthpeak-Sponsored Sector Conferences	Forums to share operational and ESG best practices with our partners across all business segments for implementation at our properties			
Communities	Social Responsibility Committee	Committee comprised of employees from all levels and locations to partm with national and local charitable organizations to support advancing healthcare, senior communities, and emergency disaster relief, especially the local communities in which our employees work and live			
	Volunteering and Giving	Support local community needs through volunteering and charitable donations, including matching employee contributions, as well as paid time off for employee volunteering activities			

Framework Alignment

Dur ESG Committee conducts an annual analy he feedback from our ESG engagement with inder GRI, SASB and TCFD. This analysis helps intervies introitize initiatives and enhance o

Environment				
Climate Risk				
GHG Emissions Reduct	ion			
Energy Savings				
Waste & Landfill Reduc	tion:			
Water Savings				
Surtainable Buildings				

Social

Diversity, Equity & Inclusion alent Attraction & Retention

Our ESG Priorities

During our fiscal year ended November 1, 2020 (FY20), we conducted our inaugural ESG materiality assessment, to help us understand the ESG issues that are most significant to the any and our stakeholders, and to guide us develop our ESG program and initiatives. as, risks and opp y. These inputs included the following

- vs of leading global repo no the Global Reporting ding the Global Reporting Initiativ Sustainability Accounting Standar Id (SASB), and market trends and rds in the semiconductor and softwa ies, including the focus areas set fort Responsible Business Alliance (RBA) ectives and feedback re vestors and our custom
- al subject matter experts, ze the ESG issues with the

inificant potential impact on our business ulting issues were evaluated, rar ad by our ESG Steering Commit ad by our Board of Directors (Be eviewed by our Board of Directors (Board, ISG topics presented below were determin o be the most significant and will guide ou sustainability programs and initiatives. We in



A growing number of companies use materiality matrices to show how ESG topics identified by the business as material compare to those identified by stakeholders. Companies then prioritize those issues that are most important to both.

Left to right, top to bottom: HPE, Walgreens Boots Alliance and ADM use matrices in their latest ESG annual reports to show ESG issues material to their businesses and stakeholders.

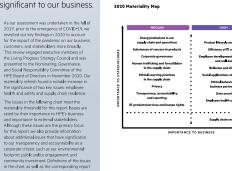
OUR APPROACH

Our fifth annual Living Progress Report offers an overview of our approach, our programs, and our progress on the environmental, social, and governance issues most significant to our business.

hity investment, or hart, as well as the corre

MATERIALITY

eqularly u nt to ensure we are addressing the ental social and governance (ESG) greatest significance to our business eted our lates ing Index (GRI) and



HPE LIVING PROGRESS RI

Responsible and ethical supply chains O Prescription drug abuse Employee health, safety and well-being Product labeling and transparency 2 Data privacy and securit Environmental impacts of materials O Corporate governance Employee wages
 and hiring practices
 Packaging 1 Diversity and inclus Cancer cure and prevention 15 Chemical use Community engager and partnerships 1 Animal testing 16 Waste management Dimete Impacts 20 Product end-of-life 2 Tobacco sales Sustainable Markete 22 Supplier diversity Healthy an

23 Water consumption and use

2 Deforestation

Significance of Walgreens Boots Alliance's Impacts

• Governance

CSR Materiality Matrix

a CSR wer priority topics, an icates how each topic 2 Product safety

Access to affordable and quality healthcare

Consumer health education and ma

Materiality Assessment and

Stakeholder Engagement

According to the Global Reporting Innitiative (GRI), materiality is a way to assess the topics that have a dire or indirect impact on an organization's ability to create, reserve or erode economic, environmental and social value for itself, its stakeholders and society at large. e or itself, its stakeholders and society at large. rraility is a crucial step in defining our sustainability rain. Withs on many topics that could be covered, ucting a materiality assessment allows us to focus aporting on topics that reflect the economic, onmental and social impacts that are the most icant to our strategy and business operations, and akeholders.

Au submittioners. ADM engaged a reputable professional services firm to andertake an updated formal materiality assessment to guide our sustainability strategy in the coming years. Hohough this year's Corporate Sustainability Report and priorities are based on the previous materiality we are presenting the refreshed matrix rm all stakeholders of where we are go ess applied this year was similar to that used for the teriality assessment. The assessment team applied edge of the GRI methodology and our industry to keholders for engagement based on the selection f responsibility, influence, proximity, dependency, ntation. Working with ADM, the firm in

ing stakeholder groups were included as part of

 ADM leadership Employees
Civil society/r Customers organizations (NGOs) e outset of the assessment, informed by the current scape and with a forward-looking lens, the firm ADM revised previous topic names and definitions. equently, some topics were disaggregated or At the outset of the ass urity," "Tax Strategy," and "Alter

Int results indicate several key topics stent across all stakeholder groups a tance: "GHG Emissions," "Deforestat "Governance," and "Water Managen se are critical to manage, the other to rix are also important to ADM and ou

stakeholders. We recognite that these priorities can change rapidly, so we will continue to monitor and adjust our focus as informed by ongoing stakeholder engagement via customer feedback, KOG inquiries, and dialogue with stakeholders. Any interested party can reach out to us sustainability game .com. All of these touchpoints help direct our sustainability programs.



Some also include a brief statement to note that the term "materiality" used within the context of their ESG reporting is not the same as the concept of financial materiality used for SEC reporting purposes, while some avoid using the term altogether, especially if they have not yet conducted a materiality assessment grounded in investor and other stakeholder input.

To Thy Own Self Be True

Regardless of how companies are disclosing what they determine are their material ESG issues, what's clear is that the concept of materiality is not static. Dynamic materiality captures the idea that as external and internal factors impacting companies and their investors change over time, so too does what is material:⁸

"Due to factors such as emerging technologies, new knowledge, and new regulations companies adapt their products and services and entire industries evolve. These factors taken together with changing social expectations mean that what is material for an industry will change. There can also be differences at the company level within an industry due to different strategies."

While research has shown that greenhouse gas emissions, labor practices and business ethics have constituted a steady 25% of all ESG disclosures from companies in the Russell 3000 since 2009⁹, issues like employee engagement, health and safety – alongside diversity, equity and inclusion – have risen quickly in importance due to the global COVID-19 pandemic and racial justice movements. It remains key, then, for companies to stay on top of what issues are of most concern to their investors and broader stakeholders. And until securities exchange commissions like the SEC specify ESG disclosures in their financial reporting requirements, the materiality of ESG topics will continue to be up to each company individually to determine, using GRI, SASB and others for guidance.

Or, in the words of Shakespeare, when it comes to determining the materiality of ESG topics, "to thy own self be true."

⁸ Eccles, Robert G. (January 17, 2020). Dynamic Materiality And Core Materiality: A Primer For Companies And Investors. Forbes.com.

⁹ Eccles, Robert G. (January 17, 2020). Dynamic Materiality And Core Materiality: A Primer For Companies And Investors. Forbes.com.

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