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The contest for materiality. What counts as CSR?

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Abstract

Purpose – The paper aims to show that materiality in the EU's non-financial reporting directive (NFRD) is an ambiguous concept, that its meaning is contested and that this contest for materiality is a contest for the meaning of Corporate Social Responsibility (CSR). Thus, the paper shall highlight a new aspect of materiality as a core principle in non-financial reporting.

Design/methodology/approach – The paper combines a historical analysis of the EU's CSR policies, an in-depth textual analysis of the EU's 2014 NFRD and associated documents, of non-financial reporting frameworks and exemplary adoptions of the NFRD in national laws.

Findings – The paper identifies two conflicting views of materiality in the NFRD. It shows that these "additive" and "cumulative" views correspond to the approaches taken by the Global Reporting Initiative (GRI) and International Integrated Reporting Council (IIRC) frameworks and by different national adoptions of the NFRD. The paper concludes that this contest for materiality is a contest for CSR – focusing either on business risks or impacts, shareholders or stakeholders, the business case or the social case for such a responsibility.

Research limitations/implications – The paper is mainly based on an in-depth analysis of the European debate on materiality in non-financial reporting. Some of the paper's descriptive results are thus limited to this particular case. However, the main conceptual findings are backed up by an analysis of internationally established reporting frameworks and scholarly debates on the issue.

Practical implications – The paper reveals the practical implications of the contesting "additive" and "cumulative" understandings of materiality present in the NFRD. The paper thus further underpins the preference for a "double materiality" perspective in the revision of the NFRD and the EC's 2021 CSRD proposal.

Originality/value – The paper makes an original contribution in its explication of different understandings of materiality in non-financial reporting and how these eventually represent different, competing perspectives on the nature of the NFRD and of CSR.

Keywords CSR, Discourse analysis, Social and environmental reporting, Double materiality, European green deal

Paper type Conceptual paper

1. Introduction

The *European Union's Directive 2014/95/EU*, for the first time, had large public-interest companies report on social and ecological business risks and impacts linked to their activities. The *Non-Financial Reporting Directive* (below "*the NFRD*") is principles-based, i.e. it does not exact from them any particular information. Yet, at its core is the *principle of materiality*, a principle that's supposed to curtail some of the downsides of such an approach, while at the same time allowing for flexibility, innovation and excellence in reporting.

The *NFRD* does share that focus and intent with what are currently the most prominent frameworks for non-financial reporting: the *GRI Standards* for sustainability reporting and the *IIRC's <IR> Framework* for integrated reporting. Yet, the *NFRD* also does contain both their conflicting notions of materiality, focusing either on business risks or impacts, shareholders or

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stakeholders, the "business case" or the "social case" for *CSR* – indeed two conflicting notions of *CSR* that the *NFRD* did inherit from the *EU*'s own conflicting history on the issue.

The paper starts with a brief account of this history of *CSR* in Europe. It then sketches the two distinctive interpretations of materiality present in the *GRI Standards* and the *IIRC's <IR> Framework*. Against this background, the paper conducts an in-depth analysis of the materiality principle in the *EU's* 2014 *NFRD* and 2017 *guidelines* for implementation, including a programmatic 2019 *supplement* on climate issues. Eventually, the paper is to show that the *NFRD*'s fundamental ambiguity regarding the materiality principle allowed academics, accountancy professionals and *EU* member states to draw very different implications about what's supposed to be material in non-financial reporting. At the end of the day, we see an old, unresolved question bubbling up again in that contest for materiality: *What is the social responsibility of business?* In other words, it is a *contest by proxy* for that much more fundamental debate.

Against that background, materiality could be referred to as an "essentially contested concept" (cf. Gallie, 1955). Being "essentially contested" means that there's no true or fixed meaning to it. If this is true for materiality in general, given that its actual meaning "is in the eye of the beholder" (Hicks, 1964, p. 159) or subject to "discursive truth games" (Edgley, 2014, p. 262), this is *a fortiori* the case in non-financial reporting, where it's about normative issues of social responsibility and sustainability (cf. Christensen *et al.*, 2021, p. 1222; Mosca and Picciau, 2020, p. 28). The debate about these issues will never be settled for good.

At the same time, the very contest itself – even if arguments may never suffice to convince the other side – might eventually improve the overall quality and clarity of the concept at stake (cf. Collier *et al.*, 2006, pp. 216–217). It is that "progressive competition", albeit power-ridden, crabwise and lengthy, that marked and shaped the EU's debates on *CSR* – until, in 2011, they ended up with a "new definition of *CSR*" that set the stage for the development of the *NFRD* (see section 2 below). That same "progressive competition", albeit equally power-ridden, crabwise and lengthy, has been at work ever since when it comes to the very meaning of materiality in non-financial reporting – until, in early 2021, it ended up with a clear preference for a "double materiality" perspective, as expressed in the *European Commission's* proposal for a *Corporate Sustainability Reporting Directive (CSRD)*.

In the course of that paper, I argue for this "double materiality" perspective. Still, the main contribution of this article probably lies in its effort to reconstruct this process and provide some historical and conceptual context, from a meta-perspective. Other scholars have recently made similar efforts and corroborate the main finding of a contest for materiality – even if they disagree about whether these contesting approaches to materiality be only "slightly different" (Mosca and Picciau, 2020, p. 27), "significantly different" (Mio *et al.*, 2020, p. 306), even "incommensurable" (Biondi *et al.*, 2020, p. 901) or indeed "two extremes" (Christensen *et al.*, 2021, p. 1182). At any rate, they also relate these notions of materiality to different ideas of social responsibility and, above all, a corporation's purpose (cf. Particularly Christensen *et al.*, 2021, p. 1222; Mio *et al.*, 2020, p. 306; Mosca and Picciau, 2020, p. 28).

The present article provides an in-depth analysis of these historical and conceptual backgrounds (sections 2 and 3, 3.3) as well as of the contesting takes on materiality in three different contexts: private standard-setters (sections 3.1–3.2), different national adoptions of the *NFRD* (section 3.4) and the academic debate surrounding them (3.5).

2. A brief history of CSR and non-financial reporting in the EU

In late 2014, the *European Union* issued its long-awaited new *Directive* "as regards disclosure of non-financial and diversity information by certain large undertakings and groups" (2014/95/*EU*, amending 2013/34/*EU*). In its central amendment on the "non-financial statement", the *NFRD* exacts the following:

> Large undertakings which are public-interest entities exceeding on their balance sheet dates the criterion of the average number of 500 employees during the financial year shall include in the management report a non-financial statement containing information to the extent necessary for an understanding of the undertaking's development, performance, position and impact of its activity, relating to, as a minimum, environmental, social and employee matters, respect for human rights, anti-corruption and bribery matters. (European Union, 2014 Article 1(1))

In a nutshell, the above passage provides a snapshot of the *EU*'s then understanding of the issue: what non-financial statements are supposed to cover, why, and in what form reporting by whom should help to secure it. As we shall see, the actual meaning and implications of the *NFRD*, indeed the very "spirit" it entails have been subject to interpretation and contest ever since it was enacted. In that, it has been a true heir to the controversial European debate on *CSR* that had preceded it, for more than 10 years – a controversy that, quite obviously, the *NFRD* could not end but only translate into more legal and technical terms. The issues, however, are still the same, and unsettled. A brief review of the *NFRD's* historical background may help to understand why it just achieved what it did – and why even that is still being contested.

The *EU*'s active politics on *CSR* dates back to the turn of the millennium. The *Commission's* 2001 *Green Paper*, with its definition of *CSR* "as a concept whereby companies integrate social and environmental concerns in their business operations and in their interaction with their stakeholders on a voluntary basis", both reflected and triggered off the debate on the issue for the coming years (European Commission, 2001, p. 6). Despite harsh criticism of this strictly voluntary approach by the *European Parliament* and *NGOs*, from the very outset (cf. European Parliament *et al.*, 2002), another *Communication* on the issue in 2002 practically codified this definition (cf. European Commission, 2002, p. 5) and the "voluntary nature of *CSR*" (p. 8). That same *Communication*, in its very title, also framed *CSR* as the "business contribution to Sustainable Development", and it kicked off the *European Multi-Stakeholder Forum on Corporate Social Responsibility*. That forum, however, broke up in 2006, as a result of *NGO* protest against massive corporate interference, and it gave way to the business-led *European Alliance for CSR*. In the official announcement of this *Alliance*, *CSR* was also officially re-framed as a contribution, no longer to sustainable development, but to "sustainable growth" (European Commission, 2006, p. 5).

To be sure, *CSR* had never and nowhere, originally, been meant as an alternative draft to neoliberal globalization. Rather, "CSR has co-evolved with neo-liberalism and was distinctly shaped by its emergence: it compensates for some of the latter's deficits in the areas of moral legitimation and social compensation, while maintaining the emphasis on voluntarism." (Kinderman, 2012, p. 42). Still, what was characteristic for this first phase of the European debate was the advance of the "business case" for *CSR*: a proposition that was to re-frame the issue in strategic terms, around the notion of "shared value" (cf. Porter and Kramer, 2002, 2006, 2011) – indeed in the very language of business – which at that time proved particularly attractive to the corporate world and its following (cf. Blowfield and Murray, 2008; Vogel, 2005)

The *post-2007 crisis*, the catastrophic *Deepwater Horizon* oil spill in 2010 and the later factory fires at *Ali Enterprises* and *Rana Plaza,* to name but a few of the most prominent global issues of corporate *irresponsibility*, at that time, eventually did have an effect on the *EU*'s politics on *CSR*. After months of consultation, in late 2011, the *European Commission* launched its "renewed EU strategy 2011–14 for Corporate Social Responsibility" (cf. European Commission, 2011). The *Communication* still did underline the voluntary nature of *CSR*, the need for a strategic approach, the potential benefits for corporations, and the ultimate goal to create "shared value" (pp. 5–6). Yet, it also identified "important challenges" that would call, among other things, for a "multistakeholder approach", "greater attention to human rights" and "complementary regulation" (pp. 5–6). Above all, in an effort to clarify expectations and catch up with "international principles and guidelines", it provided "a new definition of *CSR* as »the responsibility of enterprises for their impacts on society«." (p. 6)

In its "*Agenda for Action 2011–2014*", this *Communication* also promised "a legislative proposal" on non-financial reporting (p. 11). In a memo on this future *directive*, in 2013, the *Commission* finally left no doubt about the reasons for such a regulatory move: "Over the years, we have seen the limits of a voluntary approach . . .. Regulating the disclosure of some minimum requirements, whilst avoiding an undue administrative burden, in particular for the smallest companies, is the right decision at this time." (European Commission, 2013, p. 2)

This was the background, then, against which the 2014 *NFRD* finally took shape. There had already been one earlier move to implement non-financial reporting, in 2003, with the *EU's Accounts Modernization Directive (2003/51/EC)*. Yet, while this had been no more than the proverbial first step, no further steps were to be expected, politically, in the shown context (cf. Kinderman, 2015, p. 614). The eventual *NFRD*, too, met with massive resistance from big business lobby groups, such as *CSR Europe*, then *BusinessEurope* and *EuroChambres*, the British *Tories* (cf. Howitt, 2014) and particularly Germany (cf. Kinderman, 2015, p. 617; Schweren and Brink, 2016, p. 180).

All this may explain why not more was possible, in that particular historical situation. Still, even longtime critics of the *EU*'s *CSR* policies did consider the *NFRD* a milestone in that development: Richard Howitt, who, as British *Labour MEP* and untiring *Rapporteur* on *CSR* in the *EP*, had initiated efforts for non-financial reporting at *EU* level in 1999, hailed it "a landmark decision" and "historic date in the transition to business sustainability for all" (Howitt, 2014). Daniel Kinderman, among the most knowledgeable and critical chroniclers of *CSR* in the *EU*, openly acclaimed it "a breakthrough" (Kinderman, 2015, p. 614). A comparative study on *CSR* reporting in the *EU* and the *USA* called it a "paradigm shift" (Spießhofer and Eccles, 2014, p. 27), another study on the evolution of *European CSR* reporting a "turning point" (Schweren and Brink, 2016, p. 179).

Certainly, much of that praise for the *NFRD* has to be judged against its difficult delivery. Certainly, the *NFRD* does carry the marks of this history. Just like the new definition and strategy on *CSR* on which it is based, it reveals a compromise of two opposing views. So, in absolute terms, the progress manifest in the *NFRD* has still been pretty moderate – and again: *contested*. This is where the issue of "materiality" comes in. As a principle, it promises a solution to that contest. When it comes to its very meaning, however, materiality has itself become the subject of contest – *the contest for CSR*. That's what this paper is to show, with a discussion of materiality in the *NFRD*, and how very differently it is being interpreted, based on two contesting takes on the issue.

3. The contest for materiality

"Materiality" is really a *Janus*-headed concept. What looks like a straightforward *principle* from one angle takes the shape of a *petitio principii* from another: Claiming to focus on what matters, that is, actually *begs the question* what it is that matters. Consequently, there's general *consent about materiality*, as a formal principle – at the same time, there's a *contest for materiality* when it comes to what it actually means.

Before I explicate that *contest for materiality* in non-financial reporting (cf. The following sections), let me explain what I mean by that *consent about materiality* – and where non-financial reporting departs from it. Let's first focus on continuity: The *NFRD* does legally amend *Directive 2013/34/EU* on financial reporting, adopting thereby its generic definition of materiality:

> "»material« means the status of information where its omission or misstatement could reasonably be expected to influence decisions that users make on the basis of the financial statements of the undertaking." (European Union, 2013, Article 2(16))

So, material information is defined here in terms of what could influence a person's decisions. Tellingly, while the actual origin of the term remains obscure, this generic definition – in one wording or another – has remained pretty much the same since the first formal definitions of "material fact" in late 19th century law debates (cf. Edgley, 2014, pp. 256–257). Certainly, many an effort has been made along this way to methodologically or by definition nail down or at least determine thresholds for what's material information and what not (cf. also Brennan and Gray, 2005). At the same time, both in corporate law and in the adoption of the term to accounting and auditing, there was a telling – and decisive – change of addressees: The original model of "reasonable man" gave way to the image of the "typical" or "prudent investor" (cf. Edgley, 2014, p. 256) – and with it changed the notion of what was typically *material* for these model men, based on their particular kind of rationality.

As Ernest L. Hicks had it, in an early thoughtful analysis of the matter: "Materiality, like beauty, is in the eye of the beholder" – adding that "*our materiality decisions ultimately depend upon how we perceive him*." (Hicks, 1964, p. 159) What's material, in other words, depends "on the needs of the mysterious, mythical man" (Edgley, 2014, p. 262) that have been the subject of "discursive truth games" between practitioners, guidance setters and regulatory bodies ever since (p. 262).

These "truth games", indeed, are still going on – and even more so with the advent of non-financial reporting, in the wake of stakeholder management, and calls for corporate social responsibility and sustainability. Indeed, what the *contest for materiality* is all about, eventually, is a conflict between what's been dubbed "shareholder governance" and "stakeholder governance", and their corresponding notions of what a business, and thus the economy, is supposed to be – and good for: i.e. what its *social responsibility* is.

The traditional view – also in accounting and auditing – has been focusing on monetary or financial issues alone: the issue of "moral hazard" in managerial capitalism, the protection of investors' property rights, and the ultimate aim to secure trust and the constant supply of capital. The notion of "social responsibility" implicit here – in terms of a deep belief in the positive externalities of amoral utility maximization, in a free market economy – was probably never better summed up than in Milton Friedman's notorious dictum: "The social responsibility of business is to increase its profits." (Friedman, 1970) Materiality, traditionally, has thus been "a concept for shareholders as a group, for the purpose of financial decision-making. It has been shaped by a market logic (a shareholder focus) and a professional logic (as a practitioner responsibility) to protect investors." (Edgley *et al.*, 2015, p. 5) Some practitioners, guidance setters and regulatory bodies, as we shall see, see no need to change this – even if based on a more sophisticated "business case" argument for corporate social responsibility. This is particularly evident in the *IIRC*'s approach to "integrated reporting", as we shall see.

The other party in that contest does roughly correspond to the "stakeholder governance" model, with a focus on the very negative externalities linked to profit maximization, but also on the potential benefits of active and serious stakeholder management (cf. Freeman, 1984, 2004). It is in this context that the notion of materiality is currently being redefined – both in terms of information about impacts, in their own right, and in terms of a "materiality process" that defines the very procedures for such a definition.

The *contest for materiality*, therefore, is basically about how a business is to fulfill its social responsibility. In the following sections, I will set out in detail what that means. To that end, I will compare the different notions of materiality present in the respective reporting frameworks of the *IIRC* and the *GRI* – as exemplars of integrated reporting and sustainability reporting, resp. Their takes on materiality have been duly recognized recently as being "slightly different" (Mosca and Picciau, 2020, p. 27), "significantly different" (Mio *et al.*, 2020, p. 306) or indeed "incommensurable" (Biondi *et al.*, 2020, p. 901). In the preceding sections, I linked these different takes to different understandings of *CSR* and, ultimately, a corporation's purpose. In the following sections, I will explicate in-depth how this resounds in their resp. Definitions of materiality.

3.1 Materiality in the GRI standards

The *Standards* – until 2016 the "*Guidelines*" – issued by the *Global Reporting Initiative (GRI)* since 1997, today, are being applied by thousands of reporting organizations worldwide (cf. Global Reporting Initiative, 2015, p. 7). According to the most recent biennial *KPMG* survey on global *CSR* and sustainability reporting, 63% of reports done by *N100* companies (the 100 largest companies in 41 countries) and 75% of reports by *G250* companies (the top 250 companies listed in the *Fortune Global 500* ranking) were using the *GRI* framework in 2017 (KPMG International, 2017, p. 28). As for Germany, practically all large companies and close to 80% of *SMEs* do currently apply the framework in their reporting (cf. Dietsche *et al.*, 2019, p. 15). The situation in Austria and Switzerland is fairly similar, according to recent surveys done by *Ernst & Young* for those two countries (cf. Ernst and Young, 2016a, b). I do provide specific data for the German-speaking world, because part of my later analysis will deal with the different interpretations of materiality and corresponding implementations of the *NFRD* there. At any rate, based on these data, it is justified to say that the *GRI Standards* today present a global *de facto* standard for sustainability reporting.

The *Standards* that were issued in late 2016 meant the fifth major revision of the framework, after *G1* in 2000, *G2* in 2002, *G3* in 2006 and *G4* in 2013. The most important thing that this fifth generation introduced was the new modular design, rendering future updates of the whole framework obsolete – and with that also the version numbers. So, the major overhaul, here, was rather about formal issues. The more fundamental revision in terms of contents and rationale of sustainability reporting had already been introduced with the earlier transition from *G3* to *G4*.

This was *the shift to materiality as a core principle*, in an effort to curb a problematic trend in sustainability reporting. *GRI* had been criticized for losing focus and valuing breadth over depth (cf. Global Reporting Initiative, 2015, p. 7). The introduction, with *G3,* of so-called "application levels", in particular, had provided an adverse incentive for companies to disclose high levels of indiscriminate information: information of questionable relevance and quality whose mere quantity – awarded with an "A" for high levels of disclosure – had been too easily mistaken for good sustainability performance. Thus, *G4* had to put the brakes on these developments, signaling that less is sometimes more, also in sustainability reporting.

So, *G4* was to provide more focus on aspects that really matter, which was supposed to benefit both a company's strategy and its credibility with stakeholders. "Materiality" was the new watchword – and it still is. That's what *GRI* also made clear in a more recent document discussing the relationship of the *Standards* and the *NFRD*: "Both the GRI Standards and the European Directive place a strong emphasis on materiality in order to help organizations determine which economic, environmental, and social impacts to report on". (Global Reporting Initiative, 2017, p. 3)

So, there's a clear commitment to materiality, in principle. When it comes to its actual meaning, the *GRI Standards* immediately tie in with *G4* and more systematically introduce it as a central "principle of reporting". The key *chapter 1.3* on materiality in *GRI 101: Foundation* exacts that reports "shall cover topics that 1.3.1 reflect the reporting organization's significant economic, environmental, and social impacts; or 1.3.2 substantively influence the assessments and decisions of stakeholders." (Global Reporting Initiative, 2018, p. 10) In the *Guidance* section on that principle, *GRI* makes clear what's special about that two-dimensional definition. First, it is different from materiality in financial reporting, since "it is concerned with two dimensions, i.e., a wider range of impacts and stakeholders." (p. 10) Second, *GRI* sets out "that a topic can be material based on only one of these dimensions" (p. 10) – that's why, obviously, they are *linked with an "or", instead of an "and"*. As we shall see in our discussion of the *NFRD*, the use – and interpretation – of such a conjunction can make all the difference in how "materiality" is being understood.

The *GRI Standards* make many additional remarks on materiality. Indeed, materiality is a true *leitmotif* in that prominent framework, and its focus both on objective consequences and subjective stakeholder claims, including the "process" in which these are being heard, mirrors what's been identified by some commentators as the distinctive feature of non-financial reporting. As we shall see, they also argue that this is what the *EU*'s new strategy and definition of *CSR,* and thus the *NFRD* is all about. However, there's also another take on what "materiality" could mean in non-financial reporting.

3.2 Materiality in the IIRC's <IR> framework

The branded "*<IR> Framework*" for integrated reporting was introduced in late 2013 by the *International Integrated Reporting Council (IIRC)*, until 2011 *Committee*, a global coalition of regulators, investors, companies, standard setters, the accounting profession and *NGOs*. The *IIRC's* plans for its framework are quite ambitious: "It is anticipated that, over time, <IR> will become the corporate reporting norm." (IIRC, 2013, p. 2) – an ambition that has recently been renewed, with the renewal of the IIRC's Framework in early 2021 (International Integrated Reporting Council (IIRC, 2021, p. 2) Despite these high aspirations and a general trend towards integrated reporting (in small letters), *<IR>* has not yet nearly matched the *GRI Standards*, in practice.

What marks out *<IR>* and what's supposed to back up its ambitions, however, is the importance it gives to "integrated thinking", i.e. "the active consideration by an organization of the relationships between its various operating and functional units and the capitals that the organization uses or affects. Integrated thinking leads to integrated decision-making and actions that consider the creation, preservation or erosion of value over the short, medium and long term." (p. 3, again p. 53). That entails a similarly integrated understanding of "value", based on an "integrated model" of six "capitals": financial, manufactured, human, social and relationship, intellectual and natural (cf. pp. 18–20). These "capitals" are understood both as inputs and outputs – "resources" and "stocks of value" – that an organization both utilizes and affects in its process of value creation, a process that "manifests itself in increases, decreases or transformations of the capitals caused by the organization's business activities or outputs." (p. 16)

Based on such an integrated understanding, the *IIRC* arrives at what's been dubbed a "business case" proposition of corporate sustainability or social responsibility, i.e. an understanding that doing good and well, as an organization, would certainly merge, at least in the long run (cf. Flower, 2015, pp. 13–14). From that perspective, value "is unlikely to be created through the maximization of one capital while disregarding the others." (IIRC, 2021, p. 17)

This also impacts on the particular notion of "materiality" the *IIRC* champions. The official *<IR>* Framework (2021) – the *IIRC's* core document – features "materiality" as one of the "guiding principles" of integrated reporting (cf. p. 7, pp. 29–31). To emphasize that importance, the *IIRC* and the *International Federation of Accountants (IFAC)* also issued a paper that specifically deals with materiality (cf. International Federation of Accountants (IFAC), 2015).

On several occasions, the *Framework* exacts that "[a]n integrated report should disclose information about matters that substantively affect the organization's ability to create value over the short, medium and long term" (IIRC, 2021, pp. 29, 53, 56 – cf. also IFAC, 2015, p. 4). Additionally, it underlines the need for information on the "materiality determination process" (cf. IIRC, 2021, pp. 29–30, pp. 47–48 – also IFAC, 2015, pp. 12–14, 23) and provides some guidance on how to identify, evaluate, prioritize and determine material information in that process (cf. IIRC, 2021, pp. 30–31). In that context, "[a]n understanding of the perspectives of key stakeholders is critical to identifying relevant matters." (p. 30) Yet, these are not material *per se*, but only if "these interactions, activities and relationships are material to the organization's ability to create value for itself" (p. 16).

The "primary purpose" of integrated reporting, therefore, "is to explain to providers of financial capital how an organization creates, preserves o erodes value over time" (pp. 5, 11, 30 – also IFAC, 2015, p. 25). These are the actual addressees, because they are supposed to have an immediate interest in the good management of all capitals. Therefore, the *IIRC's* take on materiality boils down to the view that it is sufficient to report on those issues that, eventually, will have an impact on how the organization creates value for itself – i.e. *on the organization itself*: "Providers of financial capital are interested in the value an organization creates for itself. They are also interested in the value an organization creates for others when it affects the ability of the organization to create value for itself" (IIRC, 2021, p. 16).

Despite the integrated understanding of "value" the *IIRC* seems to promote, it is "the value created for the organization itself" that, at the end of the day, defines what's material – and what not. Against that background, *<IR>* represents an understanding of materiality that focuses on the business case for CSR, on shareholder interests and on the impact on the business itself. This, quite clearly, distinguishes *Integrated Reporting* (in capital letters) as proposed by the *IIRC* from *Sustainability Reporting* as proposed by the *GRI*.

In the remainder of that article, I'd like to argue that actually both these notions of materiality seem to be present in the *EU*'s *directive 2014/95/EU*, and there's currently a debate over what interpretation should prevail: *a contest for materiality*.

3.3 Materiality in the EU's directive 2014/95/EU

The 2014 *directive* does not make any concrete, binding, material prescriptions – in a word, it is "principles-based" (cf. European Union, 2014). That's one of the things the *Guidelines* on non-financial reporting (2017/C 215/01 – below "the guidelines") that the *European Commission* later provided, to support implementation of the *NFRD*, make unmistakably clear (cf. European Union, 2017). Another thing that these explicitly "non-binding guidelines" (cf. p. 2) explicate is the principle of materiality and its significance, in that context (cf. pp. 5–7).

Indeed, materiality had nowhere actually been mentioned in the *NFRD*. Still, it is more than obvious just how central the principle is, implicitly (cf. also Baumüller and Schaffhauser-Linzatti, 2018, p. 106). Actually, materiality in the *NFRD*, *avant la lettre*, does apply to different things: issues, risks, key performance indicators and also to the right to omit information (cf. pp. 108–110). However, it is the first, "general provision" on material information, as it is expressed in *Article 1(1)* of the *NFRD*, that's at stake here: It is the one that defines *for what and to whom* an organization is generally responsible, the one that practically overrides all other provisions [1], and the one that, consequently, is particularly contested. So, for our purposes, it will suffice to focus on the *NFRD's* general provision on materiality to provide "information to the extent necessary for an understanding of the undertaking's development, performance, position and impact of its activity" (Article 1(1) – for full quote, cf. above, p. 3).

The 2017 *guidelines*, as mentioned above, make it very clear just how important materiality is in non-financial reporting. Among the "key principles" that are being discussed, therefore, the principle "3.1 Disclose material information" comes first and it's also being dealt with in most detail (cf. European Union, 2017, pp. 5–7). The *guidelines* first discuss materiality as a generic term, as it is being commonly used in financial reporting, referring to the earlier *Accounting Directive (2013/34/EU)* that the 2014 *directive* amends. Accordingly, by quoting *Article 1(1)* of the *NFRD*, the *guidelines* emphasize "a new element to be taken into account when assessing the materiality of non-financial information by referring to information 'to the extent necessary for an understanding of the [. . .] impact of (the company's) activity'." (p. 5) This "new element", again, can be directly traced back to the *Commission's* "new definition of *CSR* as »the responsibility of enterprises for their impacts on society«." (European Commission, 2011, p. 6) A recent *supplement* to the *guidelines* on reporting climate-related information further underpins that reading. It openly addresses the "double materiality perspective" of the *NFRD*, covering "both financial materiality and environmental and social materiality" (European Union, 2019, p. 4). Based on that distinction and on some reflection about how "[t]hese two risk perspectives already overlap in some cases and are increasingly likely to do so in the future", the *supplement* makes it unmistakably clear that an issue (here the climate) has to be reported if it "is a material issue from either of these two perspectives." (p. 4)

The extension of the principle of materiality that this "new element" of "environmental and social materiality" entails is generally recognized and agreed upon by interpreters of the *NFRD*. Yet, what's still being contested is the issue whether an organization's impacts on society, in their own right, constitute material information that it has to disclose in its report. According to the *GRI Standards*, as we saw, they definitely do. According to the *IIRC's <IR> Framework*, they do not. As we shall see, legislators and experts alike, in their interpretations and implementations of the *NFRD*, do follow either one of these takes on materiality in non-financial reporting. They either go for what's been called a "cumulative" interpretation of the "general provision" or else what could be called an "additive" interpretation.

3.4 The political contest for materiality

When it comes to legislators, it is instructive to compare the national adoptions of the *NFRD* in Austria and Germany. While these two countries share a common language, they do differ remarkably in their respective readings of the "general provision" on materiality. The language issue is not exactly irrelevant here, because the German translation of the *NFRD*, instead of a simple "*und*" (for the English "and"), chose the conjunction "*sowie*" (rather "as well as" or "at the same time") to link the "impact of . . . activity" to the other, more generic provisions on material information. Indeed, the interpretation of the general provision on materiality – itself a proxy for *CSR* – eventually *did revolve around the interpretation of that single word "sowie"*.

The Austrian "*Nachhaltigkeits-und Diversitätsverbesserungsgesetz*" (*NaDiVeG*) pretty much follows what could be called an "additive" interpretation of the general provision on materiality. Indeed, during the public consultation process, the interpretation of materiality was not an issue at all. Business interest groups generally expressed their wish for a *1:1* adoption of the *NFRD*, instead of what they called "gold-plating". Yet, in a general aim for more concreteness and legal security, many parties, including the agricultural ministry (*BMFLUW*), the *Industriellenvereinigung* (the major lobby group for big Austrian corporations), *respACT* (the major business-led *CSR* program) and the national *Kammer der Wirtschaftstreuhänder* (the major advocacy group of chartered accountants) did advocate the use of the *GRI* framework (cf. Österreichisches Parlament, 2016). Eventually, the legislator's comments on the bill clearly profess an understanding of materiality in terms of sustainability reporting: "In case an organization applies a reporting framework, it has to make sure to meet all legal requirements in full. This, at present, certainly is the case with the comprehensive option of the Global Reporting Initiative's G4 Guidelines, based on the materiality analysis it stipulates." (Österreichische Bundesregierung, 2016, p. 3 - own translation) Thus, the Austrian *NaDiVeg* provides an *additive* interpretation of materiality in non-financial reporting, according to which an organization also has to disclose information that allows to understand its impacts on society and the environment, in their own right (cf. Schneider, 2019, p. 219).

The German "*CSR-Richtlinien-Umsetzungsgesetz*" (*CSR-RL-UG*), on the other hand, provides a very contrary interpretation of the general provision that's been dubbed "cumulative" (Rimmelspacher *et al.*, 2017, p. 227; Schneider, 2019, p. 219). It also provides a telling example for just how hard (and hard-lobbied) a single country could try to circumvent the implications of the *NFRD* – or prevent them in the first place. In some ways, this process can be seen as a sequel of the German *Sonderweg* on *CSR*: From the very beginning, Germany had been the fiercest opponent of stricter regulation on *CSR* in general and of stricter reporting rules in particular – to the point of imminent failure of the *NFRD* (cf. Howitt, 2014; Kinderman, 2015, p. 615). Without being able here to recap that whole history and its deeper reasons, it's probably safe to sum it up in the words of its most important chronicler: "Germany was by far the fiercest and most open critic of the directive." (p. 614; also Schweren and Brink, 2016, pp. 180–181)

As soon as the *NFRD* had come into effect, however, its opponents turned towards mitigating what they considered its most perilous implications. One of these was the new take on materiality the *NFRD* entails. While even the *Bundesrat,* the second chamber of the German Parliament, had unsuccessfully urged cancellation of the narrower interpretation of "material risks" in the bill (cf. Ausschuss für Recht und Verbraucherschutz, 2017, p. 42), it was the cumulative interpretation of the general provision on material information that provoked the fiercest criticism. The demand for revision filed by the German *Greens* sums up that criticism: "If these risks do not have an impact on the results and future development of a business, it does not have to disclose that information, even if its activity has an impact on society and the environment. In effect, this reporting duty comes to nothing". (Die Grünen/ Bündnis 90 *et al.*, 2016, p. 4 - own translation)

Nevertheless, the law passed the *Bundestag* against the votes of the *Green* and *Left-Wing* opposition parties, without major revisions. In their closing statements in the final session, *MPs* of the ruling coalition of conservative *CDU/CSU* and social democratic *SPD* did openly acclaim the new law for introducing public accountability of corporations (cf. Deutscher Bundestag, 2017, pp. 22,257–22,259). Yet, the comment on the bill leaves no doubt that corporations are not supposed to report on their social and environmental impacts, *per se*, but only if they "also, at the same time" – as the term "sowie" is being interpreted here – have an impact on the company's performance, position and development. So, the general provision on material information has been interpreted by the German legislator in a *cumulative* way, i. e. information on an issue has to be disclosed only *if* a material impact both of and on the organization occurs (cf. Deutscher Bundestag, 2016, pp. 48–49).

3.5 The professional contest for materiality

Academics and accountants have regularly taken this legal definition for granted and restricted themselves to pointing out its implications: "Information that is necessary for an understanding of an organization's impact on non-financial aspects, but not for an understanding of its performance, position and development, is not part of the minimum content of a non-financial statement." (Kajüter, 2017, p. 621 - own translation;, cf. also Rimmelspacher *et al.*, 2017, p. 227) Following this interpretation, the non-financial statement would contain only "a sub-set of those issues that already had to be reported according to § 289 Abs. 3 HGB" (Kajüter, 2017, pp. 620–621 – own translation), and it would thus "not constitute a comprehensive sustainability report" (p. 621 – own translation).

While most commentators do restrict themselves to just explicating the new law, some also provide additional justification for the narrow, cumulative take on materiality. For one, it would both shield addressees from information overload and companies from bureaucratic overload (cf. Kumm and Woodtli, 2016, p. 222). It would prevent double-reporting on issues already included in the extended annual report. Above all, in practice, material impacts of and on an organization would overlap anyway (cf. also Deutscher Bundestag, 2016, p. 49). This "business case" proposition, eventually, has also been proffered in order to take sides for an understanding of materiality that's "closer to integrated reporting than it is to sustainability reporting" (Baumüller and Schaffhauser-Linzatti, 2018, p. 101): "If this business case is identified and communicated properly via the means of nonfinancial reports, relying on the application of the principle of materiality, then it might serve the aims of sustainability more, however, than (in financial terms) less down-to-earth approaches of sustainability reporting in the past." (p. 110)

However, such a proposition is by no means backed up by scientific evidence. An extensive body of academic research examined the relationship between *CSR* or sustainability and good business performance, already back in the mid-2000s, when "making the Business Case" was still the "Holy Grail" (cf. Blowfield and Murray, 2008, p. 131): "Its central conclusion can be easily summarized: at best, it is inconclusive." (Vogel, 2005, p. 29, cf. also Blowfield and Murray, 2008, pp. 138-140) What's more, as the short historical excursion at the beginning of this article was to show, the *EU*'s 2011 "new definition" and strategy on *CSR* and the 2014 *directive* actually marked a *departure* from the business case approach that had dominated the *EU*'s earlier take on *CSR*. So, neither the historical reasons behind the *NFRD*, nor the directive or the *guidelines* themselves can be invoked to argue such a position – a position that, eventually, boils down to an apology of cover-up.

Finally, other commentators, in a similar effort to be true to the actual intent of the *NFRD*, did derive at a completely different interpretation – one that does rather support an *additive* understanding of materiality. As mentioned earlier, the "new perspective" that the *NFRD* adds to the generic understanding of material information has also been recognized by hard-core proponents of a cumulative view, calling it the "inside-out approach: topics are material if they reflect effects the reporting organization has on its stakeholders" (Baumüller and Schaffhauser-Linzatti, 2018, p. 106). While, for the above reasons, they still see no need to disclose this information in its own right, other commentators do, based on an observation of "several decisive differences in the materiality of non-financial information", pertaining to the "direction of impact", the "circle of addressees" and the need for "qualitative information" (Milla and Haberl-Arkhurst, 2018, p. 24 - own translation). It is the first aspect, in particular, that would call for a "reversed mindset" focusing on what an organization "*causes* or may cause" (p. 24 - own translation). Consequently, when it comes to abide by the new legal provisions, these commentators advise companies to follow the *GRI Standards* rather than the *IIRC's <IR> Framework* (cf. p. 25) – as does the Austrian legislator, as we saw above.

According to other commentators, the *NFRD* "entails a paradigm change, because it's no longer only about the value of a business, but also about »knowing and showing«, *Due Diligence* with respect to the business and its supply chain, and accountability towards investors and civil society. It's no longer just about information, but about a change of conduct, or transformation through »soft« forms of governance." (Spießhofer and Eccles, 2014, pp. 27–28 - own translation) The ultimate aim of non-financial reporting as promoted by the *NFRD*, thus, was "not only risk assessment and management, but to prevent »negative impacts«" (p. 30 – own translation): "The transformative function is therefore evident." (p. 31 – own translation)

At the end of the day, the question is whether the *NFRD* does make any difference at all. Those opting for an *additive* interpretation of materiality tend to say that it does. Those promoting a *cumulative* interpretation, in effect, say that it does not, given that it's supposedly limited to a "sub-set" of what companies already had to report about. Indeed, it is hard to see, then, whether the *NFRD* would bring any improvement at all, compared to the 2003 *Accounts Modernization Directive* – also given its narrower scope and unchanged lack of concretion. So, if anything, the step forward made with the *NFRD* consists in the new take on material information that comes with it.

4. Conclusion and outlook

Materiality is a crucial issue in non-financial reporting. It addresses the question what the social responsibility of business is supposed to be. That's what the *contest for materiality* is actually all about. It serves as a proxy for the much more fundamental debate on the social responsibility of business.

Currently, this contest turns around two different kinds of reporting: Sustainability reporting, as evident in the *GRI Standards*, calls for the systematic recognition and realization of other, social, environmental and economic goals, apart from corporate profits. Integrated reporting, as evident in the *IIRC's <IR> Framework*, calls for the systematic integration of social, environmental and economic values into the shareholder value. The most important difference between these reporting approaches, however, is their very different take on materiality. One focuses on the impacts *of* the reporting organization on its stakeholders – or what's been called an *inside-out* approach. The other focuses on the impacts *on* the reporting organization or on its shareholders – or what's been called an *outside-in* approach to materiality.

In this paper, I tried to explicate this *contest for materiality* in theoretical terms and in empirical detail – including an exemplary case of how very differently the *NFRD* has been adopted in Austria and Germany, based on these conflicting notions of materiality. I also provided my view which of these notions is more true to the *spirit* of the 2014 *NFRD* – and the more ambitious policies that followed it.

Recent developments in the revision process of the *NFRD* in 2021 indicate that the additive or "double materiality" interpretation could prevail when the *EU* eventually sets out to transform it into a "European non-financial reporting standard", as it had first been announced by Valdis Dombrovskis in early 2020 (European Commission, 2020). The *EC* report on the consultation process states that "the Directive is no longer fit for purpose" (European Commission, 2021b, p. 19), it links that to its limited scope (p. 18), level of guidance (p. 20), but also to problems with materiality of reports, particularly since "many companies do not disclose material non-financial information on all major sustainability-related matters" (p. 17). Consequently, so the report exacts, all future revisions will have to take account of developments – such as the *SDGs,* the *Paris Agreement* or the *Green Deal* – that "have given a stronger political impetus to the transition to a sustainable economy, and contributed to a growing awareness of the strategic importance of sustainability issues among businesses and investors." (p. 19) All in all, another throwback to the old *business case* thinking looks less likely than ever.

The EC's proposal for a *Corporate Sustainability Reporting Directive (CSRD)* issued the same day is very clear what this means for the issue of materiality, based on the EC's own consultation process and the recommendations of the multi-stakeholder task force set up by *EFRAG*: These provide a clear mandate to "clarify the obligation to report according to the double materiality perspective" (European Commission, 2021a, p. 8) and also to clarify the very concept itself, "removing any ambiguity about the fact that companies should report information necessary to understand how sustainability matters affect them, and information necessary to understand the impact they have on people and the environment." (p. 13, cf. also p. 28). Eventually, the contest for materiality could turn out to deliver a truly *synthetic* concept containing both narrow and broad (cf. Christensen *et al.*, 2021), "outside-in" and "inside-out perspectives" – the very result of that "progressive competition" that an *essentially contested concept* promises to be.

Note

1. This has been dubbed the "double materiality caveat" (cf. also Blöink and Halbleib, 2017, p. 187; Kajüter, 2017, pp. 621–622; Rimmelspacher *et al.*, 2017, pp. 227–228; Schmidt and Schmotz, 2017, pp. 2878–2879).

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