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BEC Handbook:

Understanding Materiality
for Environmental, Social
and Governance Reporting

Executive Summary





Background on ESG Reporting

On 1 January 2013, the Hong Kong Stock Exchange (“HKEx”) appended the Environmental, Social and Governance Reporting Guide (the “HKEx Guide”) to the HKEx Main Board Listing Rules.¹ The HKEx currently asks that listed companies respond to the HKEx Guide on a voluntary basis by disclosing the impacts of their ESG activities.²

HKEx has indicated that it may raise the level of obligation of some recommended disclosures to “comply or explain” in 2015. Should this occur as planned, listed companies will be required to comply with some elements of the Guide or explain their non-compliance.

Sustainability is the challenge of our time, and it is one that I believe we must tackle. Corporate sustainability reporting – also known as Environmental, Social and Governance Reporting or ESG Reporting – has an important role to play and is rapidly becoming an essential business management tool, the importance of which is recognised by companies and regulators alike. It is a means by which businesses can better understand the impacts of their activities, mitigate risks and identify opportunities. Simply put, ESG Reporting supports informed decision-making.

**Prof. John Chai, Chairman,
Business Environment Council Ltd**

In any case, the HKEx makes clear that it does not expect that issuers must report on all disclosures from the start. Issuers should report on those Key Performance Indicators which are “relevant and material” to their business. Thus, companies preparing to report must determine which KPIs are material or important enough

to merit disclosure. Appropriately assessing materiality is thus a key component of the ESG reporting process.

BEC Handbook: Understanding Materiality for ESG Reporting

The BEC Handbook: Understanding Materiality for ESG Reporting aims to help HKEx listed companies understand which HKEx KPIs are material to their respective businesses. It is based on a review of ESG disclosures of companies regarded as leaders in the ESG field, by industry. This forms the basis of assessing which ESG issues are likely to be material to different industries, and thus may be a starting point for new reporters beginning to assess materiality for their respective businesses.

Determining materiality requires a deep understanding of how and where you operate your business, and forces management to think outside traditional financial considerations. At the Board level, every listed company needs to consider ESG issues that could significantly impact the bottom line if they were to play out in the market and how they may be relevant to long-term corporate strategy. This makes continuous reporting obligations meaningful over time and part of prudent risk management.

Malini Thadani, Chair, BEC ESG Advisory Group

How to use this Handbook

ESG reporting is the process of gathering and disclosing information regarding the environmental, social and governance performance of an organisation and its activities. The process usually incorporates a number of steps to ensure, among other things, appropriate context, data relevance (or materiality), and completeness of the report, as outlined in Figure 1.

¹ The HKEx ESG Guide forms Appendix 27 of the HKEx’s Main Board Listing Rules.

² “ESG” means “Environmental, Social and Governance.” Governance issues are addressed separately in Appendix 14 of the HKEx’s Main Board Listing Rules.



Materiality and ESG Governance

Assessing materiality is often viewed as a multi-step process that involves identifying and engaging both internal and external stakeholders. However, stakeholder engagement is not a prerequisite for assessing materiality. Assessing materiality begins with a company's executives and directors – those with the knowledge and responsibility to set priorities and gauge the relevance of issues. It is fundamental that ESG considerations are built into company strategy and operations and that

related disclosure mechanisms receive support and oversight at the board level. Without sound governance of ESG considerations, there is risk that material environmental, social, or economic impacts receive only superficial consideration, rendering the disclosure process of limited value to investors and undermining continuous reporting obligations. Although engaging stakeholders may be valuable to fine tune responses to ESG considerations, as a practical matter, it may not be feasible at the outset and, as a result, is rarely the first step.

Figure 1: ESG Reporting Steps – Quick Reference Sheet



a Based on GRI 4 'Defining material Aspects and Boundaries – process overview', as per page 90 of the G4 Reporting Principles and Standard Disclosures, available for download here: www.globalreporting.org/reporting/g4/Pages/default.aspx

b HKEx guidance material available here: www.hkex.com.hk/eng/rulesreg/listrules/listsptop/esg/Documents/reportingstep.pdf

c See the BEC Handbook for more information, available here: www.bec.org.hk/about-us/bec-esg-advisory-group

d HKEx guidance material available here: www.hkex.com.hk/eng/rulesreg/listrules/listsptop/esg/Documents/toolkit.xls



Table 1: Overview of Global Best Practice in ESG Disclosure by Industry Sector

HKEx Subject Areas, Aspects & KPIs	Overview of Global Best Practice ESG Disclosure by Industry Sector						
	Financial Services	Properties & Construction	Consumer Goods	Industrial Goods	Utilities	Tele-communications	Information Technology
Area A	Workplace Quality						
Aspect A1	Working Conditions: General Disclosure Statement						
KPI A1.1	High	High	High	High	High	High	High
KPI A1.2	High	High	High	High	High	High	Medium ^{##}
Aspect A2	Health & Safety: General Disclosure Statement						
KPI A2.1	Medium	High	High	High	High	High	High
KPI A2.2	Medium	High	High	High	High	High	High
KPI A2.3	Medium	Medium	Medium	High	High	High	Medium
Aspect A3	Development & Training: General Disclosure Statement						
KPI A3.1	High	Medium	High	Medium	Medium	High	High
KPI A3.2	High	High	High	High	High	High	Medium
Aspect A4	Labour Standards: General Disclosure Statement						
KPI A4.1	Medium	High	High	High	High	Medium	High
KPI A4.2	Medium	High	High	High	High	Medium	High
Area B	Environmental Protection						
Aspect B1	Emissions: General Disclosure Statement						
KPI B1.1	Medium	High	High	High	High	Medium	High
KPI B1.2	High	High	High	High	High	High	High
KPI B1.3	Low	Low	Medium ^{##}	High ^{##}	High ^{##}	Low	High ^{##}
KPI B1.4	Medium	High	High	High	High	Medium	High
KPI B1.5	High	High	High	High	High	High	High
KPI B1.6	Medium	Medium	Medium	Medium	Medium	Medium	Medium

Table 1 provides an overview of best practice based on disclosure rates by industry sector.

KPIs that are identified as “High” are those that 75% or more of companies within the industry sector include in their ESG reports. These KPIs contain information deemed material based on high disclosure rates and, as a result, may be a high priority for reporting.

Level of materiality was determined with reference to full sustainability reports and annual reports.

Level of materiality was determined with reference to full sustainability reports and/or annual reports, in addition to practical experience of some members of the Working Group.



Executive Summary

HKEx Subject Areas, Aspects & KPIs	Overview of Global Best Practice ESG Disclosure by Industry Sector						
	Financial Services	Properties & Construction	Consumer Goods	Industrial Goods	Utilities	Tele-communications	Information Technology
Aspect B2	Use of Resources: General Disclosure Statement						
<i>KPI B2.1</i>	High	High	High	High	High	High	High
<i>KPI B2.2</i>	High	High	High	High	High	Medium	High
<i>KPI B2.3</i>	Medium	High	High	High	High	High	High
<i>KPI B2.4</i>	Low	Medium	High ^{##}	High ^{##}	High ^{##}	Low	Medium
<i>KPI B2.5</i>	Low	Medium	High	Medium	Low	Medium	High
Aspect B3	The Environment & Natural Resources: General Disclosure Statement						
<i>KPI B3.1</i>	High	High	High	High	High	High	High
Area C	Operating Practices						
Aspect C1	Supply Chain Management: General Disclosure Statement						
<i>KPI C1.1</i>	Low [#]	Low [#]	Medium [#]	Medium [#]	Low [#]	Medium [#]	Medium [#]
<i>KPI C1.2</i>	Medium	High	High	High	High	Medium	Medium
Aspect C2	Product Responsibility: General Disclosure Statement						
<i>KPI C2.1</i>	Low [#]	High ^{##}	High ^{##}	High ^{##}	Low [#]	Medium ^{##}	Low [#]
<i>KPI C2.2</i>	High ^{##}	Medium ^{##}	High ^{##}	High ^{##}	High [#]	High ^{##}	Medium ^{##}
<i>KPI C2.3</i>	Medium ^{##}	Low [#]	Medium ^{##}	Low [#]	Low [#]	Medium ^{##}	Medium [#]
<i>KPI C2.4</i>	High ^{##}	High	High	High	High	High	High
<i>KPI C2.5</i>	Medium ^{##}	Medium	Medium ^{##}	Low	Medium	High ^{##}	High ^{##}
Aspect C3	Anti-corruption: General Disclosure Statement						
<i>KPI C3.1</i>	Medium	High	Medium	High	High	High	Medium
<i>KPI C3.2</i>	High	High	High	High	High	High	High
Area D	Community Involvement						
Aspect D1	Community Investment: General Disclosure Statement						
<i>KPI D1.1</i>	Medium	High	High	High	High	Medium	Medium
<i>KPI D1.2</i>	High	High	High	High	High	High	Medium

KPIs that are identified as “Medium” are those that 50-75% or more of companies within the industry sector include in their ESG reports. These KPIs may or may not be material and the priority for reporting will depend on a company’s particular circumstances and its materiality assessment.

KPIs that are identified as “Low” are those that less than 50% of companies within the industry sector include in their ESG reports. These KPIs may be less important for the given sector, however, each company should nevertheless engage in a materiality assessment to determine the relevance of such a KPI with respect to its own operations.

[#] Level of materiality was determined with reference to full sustainability reports and annual reports.

^{##} Level of materiality was determined with reference to full sustainability reports and/or annual reports, in addition to practical experience of some members of the Working Group.

Differences across Industry Sectors

Materiality is conditioned by the industry sector in which it is analysed, and thus, ESG reporting and disclosure rates and content vary by industry.³ This is consistent with the notion that different industries apply and are affected by environmental, social and governance issues in different ways. Thus, the analysis in this Handbook is divided by industry in accordance with The Hang Seng Industry Classification System (“HSICS”):

- Financial Services
- Properties & Construction
- Consumer Goods
- Industrial Goods
- Utilities
- Telecommunications
- Information Technology
- Conglomerates

This Handbook provides a review of current global best practices for each industry sector and identifies those KPIs that companies have included in their ESG reports. This helps to provide global context and serves as a stepping stone for companies to explore what is most important for disclosure in their own geographic and commercial context.

International companies that are leaders in sustainability reporting were identified for each industry sector on the basis of their (i) inclusion in either the Hang Seng Corporate Sustainability Index (HSSUS), Dow Jones Sustainability Index (DJSI), or the FTSE-4Good Index⁴ and (ii) their use of Global Reporting Initiative (GRI) reporting standards.⁵

The most recent Sustainability or ESG Report of each company was reviewed to determine which of the HKEx Guide Key Performance Indicators (KPIs) were included in the respective report. Based on the proportion of companies within the industry sector which disclosed a certain KPI, a determination of materiality was made. The Handbook also reflects the practical experience of the Working Group in order to ensure that material issues relevant to the China market are identified. Further details on the methodology are available in the Handbook.

³ See “The Need for Sector-Specific Materiality and Sustainability Reporting Standards”, Robert G. Eccles, Harvard Business School, Michael P. Kruzus, Mike Kruzus Consulting, Jean Rogers, Sustainability Accounting Standards Board and George Serafeim, Harvard Business School.

⁴ The Hang Seng Corporate Sustainability Index (“HSSUS”), Dow Jones Sustainability Index (“DJSI”), and the FTSE4Good Index are sustainability indices that are designed



Image courtesy of Schneider Electric (Hong Kong) Limited

The sector-specific best practice tables in the *Handbook* provide an international baseline that HKEx listed companies may find useful. However, each company must determine the extent to which materiality for most companies in a given sector also applies to its own operations and situation. In other words, a company’s ESG disclosure should be specific and reflect the circumstances of each company, taking into account its activities, stakeholders, priorities, values and overall business strategy. Comprehensive materiality assessments should be conducted on a company specific basis to derive definitive recommendations and a comprehensive strategy for ESG disclosure.

Included within the body of the Handbook is a more detailed explanation and analysis of each industry sector, which has been summarised in Table 1. More information on the BEC Handbook can be found here: www.bec.org.hk/about-us/bec-esg-advisory-group.

to provide investors and asset managers with reliable and objective benchmarks regarding sustainability performance of large and mid-cap listed companies. Constituents include Fortune 500 companies, amongst others.

⁵ The Global Reporting Initiative is an independent, non-profit organization that develops and disseminates Sustainability Reporting Guidelines.



Key Questions for Assessing Materiality

Below are some key questions which highlight important issues to consider when reporting on the four Aspects in the HKEx Guide. They are derived from the questions that investors might ask when analysing a company's risks, opportunities and future performance.

A) Work Place Quality

- Has your company had any issues or complaints related to working conditions?
- How do you retain top talent and ensure knowledge management within your organisation?
- Has your company violated any laws or regulations related to health, safety and labour standards?

B) Environmental Protection

- Has your company previously had any incidents related to environmental spills or accusations

related to environmental pollution?

- Is your company's energy and/or resource consumption significantly larger than that of your peers in the same industry?

C) Operating Practice

- Has your company been accused of corruption or had any fines or penalties assessed related to corruption?
- Do you have significant customer-facing activities and customer data collection policies?
- Do your peers have programmes in place to monitor environmental and social impacts throughout the supply chain?

D) Community Involvement

- What are your community or social impacts and activities?

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About BEC

Business Environment Council Limited ("BEC") is an independent, non-profit membership organisation, established by the business sector in Hong Kong. Since its establishment in 1992, BEC has been at the forefront of promoting environmental excellence by advocating the uptake of clean technologies and practices which reduce waste, conserve resources, prevent pollution and improve corporate environmental and social responsibility. BEC offers sustainable solutions and professional services covering advisory, research, assessment, training and award programmes for government, business and the community, thus enabling environmental protection and contributing to the transition to a low carbon economy.



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