CHARTERED PROFESSIONAL ACCOUNTANTS CANADA

Overseeing Environmental, Social and Governance (ESG) Matters: A Framework for Not-for-Profit Boards of Directors

DISCLAIMER

This publication was prepared by the Chartered Professional Accountants of Canada (CPA Canada) as non-authoritative guidance.

CPA Canada and the authors do not accept any responsibility or liability that might occur directly or indirectly as a consequence of the use, application or reliance on this material.

Preface

The Corporate Oversight and Governance Board (COGB) of the Chartered Professional Accountants of Canada (CPA Canada) commissioned *Overseeing Environmental, Social and Governance (ESG) Matters: A Framework for Non-for-Profit Boards of Directors* to help directors of not-for-profit organizations oversee organizational performance of ESG matters. The Not-for-Profit Committee of the COGB adapted this guide from a similar publication for for-profit organizations, in recognition of the differences between the two sectors in overseeing ESG matters.

While not-for-profit organizations have always been purpose-driven, there is increased attention being paid to how they operate in the broader environmental, social and governance context. Not-for-profit boards should be knowledgeable and engaged in the oversight of ESG matters. Recognizing that this is a vast area, this document provides a practical step-by-step approach and related resources that not-for-profit boards with varying levels of organizational capacity, and at any stage of their ESG oversight journey, can benefit from.

CPA Canada would like to thank the COGB board members, Not-for-Profit Governance Committee members and staff who provided input to this project. We would also like to acknowledge Mr. John E. Caldwell, CPA, CA for generously sharing his time and expertise in advising on this project.

Tom Peddie, FCPA, FCA
Chair, Corporate Oversight and Governance Board

Not-for-Profit Governance Committee

Bobbi-Jean White, CPA, CA, Chair
Deryck Williams, FCPA, FCA, CMC
Debbie Sevenpifer, CPA, CA, CHE, C.Dir.
James Temple, CSR-P
Ina Gutium, MBA
Ruth Abrahamson

Authors

Oujala Motala, CPA, CA
Principal, Corporate Oversight and Governance
Research, Guidance and Support

Robyn Seetal, CPA, CA
Principal and Founder, IkTaar Sustainability

Rayna Shienfield, JD
Principal, Corporate Oversight and Governance
Research, Guidance and Support

Based on a conceptual framework by John E. Caldwell, CPA, CA

Project Direction

Gigi Dawe, LLM
Director, Corporate Oversight and Governance
Research, Guidance and Support

Table of Contents

Executive Summary

There is often a misconception that not-for-profit organizations do not need to be concerned with environmental, social and governance (ESG) matters, or are inherently broadly ESG-focused, because they are purpose driven, with a purpose that often aligns with an ESG-related cause. However, ESG oversight is as much about an organization's operations as it is about purpose. It's simply not enough to have an ESG-related purpose. How the organization operates in the context of other ESG factors is equally important. This document provides a practical step-by-step framework for the boards of directors of not-for-profit organizations to follow for their oversight of ESG matters, and includes examples of the types of matters that are relevant in each of the ESG categories.

In fulfilling their oversight role, we expect that boards will need assistance from the Chief Executive Officer (CEO) / Executive Director (ED) (and through them, management), to determine what ESG matters are important for the organization, to develop relevant goals and standards and to conduct assessments of progress against those goals and standards. As a result, this framework can also serve as an important resource for the CEO / ED and management when engaging in discussions with boards regarding their oversight of ESG matters.

The Growing Importance of ESG in the Not-for-Profit Boardroom

Not-for-profit organizations (NFP) have always been purpose-driven. Often, that purpose, whether for the benefit of members or the public, is related to an "E" or an "S" factor. However, just as private sector companies are being asked to look beyond profit to their broader impact on society, so too should not-for-profit organizations be looking beyond their immediate purpose to how they operate in the context of wider ESG factors. In essence, to meet not only the needs of their specific cause, but the needs of their broader stakeholders.

The importance of reporting on sustainability has been signaled on an international level through the recent formation of the International Sustainability Standards Board (ISSB), which will standardize reporting of sustainability factors for the financial markets. While this is yet to apply to NFPs, it signals a move towards overall consistency and transparency in reporting of ESG factors, which is increasingly expected by members, funders, doners, partners, the media, and the public.

What is the role of the board in ESG oversight?

ESG matters present both risks and opportunities to organizations. From a board's perspective, it can be challenging to understand how to carry out its oversight role in this area. The primary responsibilities of the board are to ensure ESG matters are considered in the organization's strategy and to exercising effective governance of ESG matters.

The Board's ESG Journey

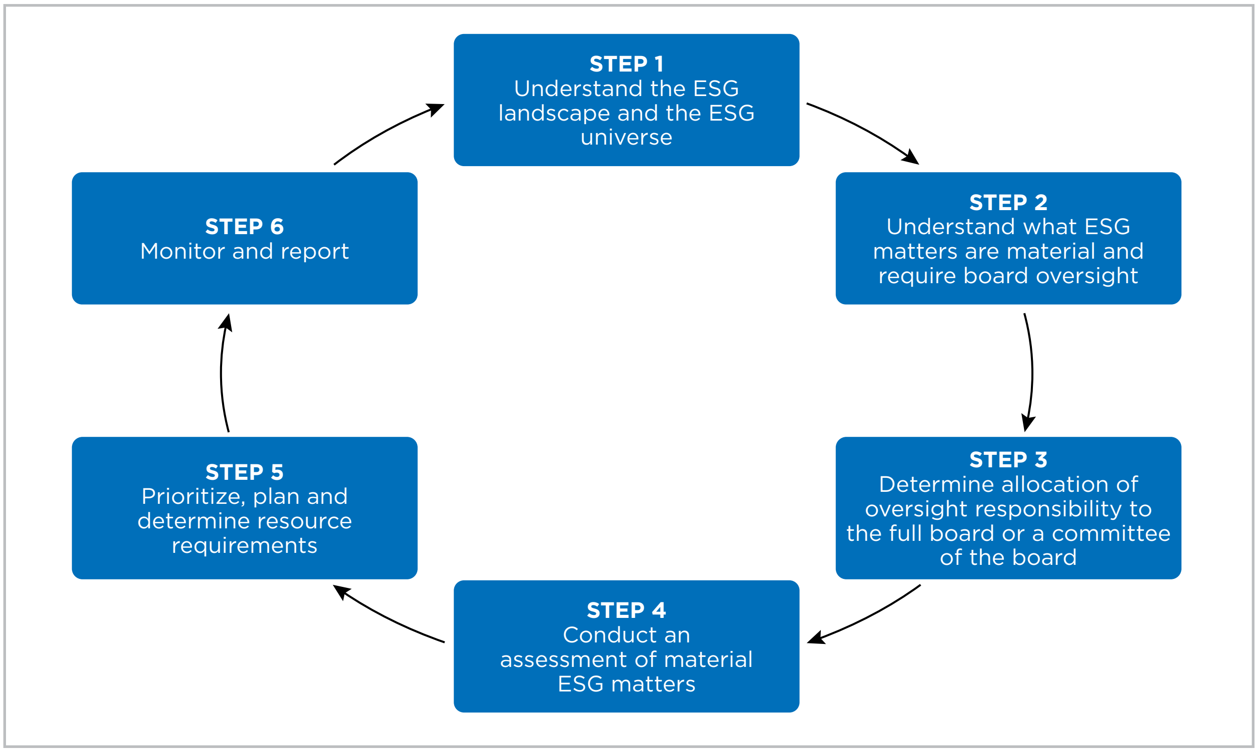
Each board (and individual board member) will be at a different stage in their ESG journey, including having different levels of maturity and resources with respect to its oversight of ESG matters. For example, boards at an earlier stage of their ESG journey may not yet have the appropriate data available to effectively assess the organization's performance with respect to certain ESG matters. As a result, it may take time to complete all the steps set out in the ESG oversight framework. Nevertheless, the ESG oversight framework provides a useful tool for boards at all stages of their ESG journey.

The ESG Oversight Framework

An Overview

The ESG oversight framework (as summarized in **Diagram 1**) provides a step-by-step approach to the oversight of ESG matters by boards, from how to develop an understanding of what types of ESG matters may be relevant to the organization, to establishing desired outcomes, measuring progress and thinking through considerations related to reporting.

DIAGRAM 1: SUMMARY OF THE ESG OVERSIGHT FRAMEWORK



ESG matters and their related oversight can be far-reaching, therefore, there is no one-size-fits all approach. Each board may want to adapt the ESG oversight framework to suit its needs and those of the organization (for example, by performing the steps in the order that makes the most sense in their current circumstance or modifying based on the organization's resources).

The execution of the ESG oversight framework is not a one-time exercise. Rather, it is an iterative process occurring over time. As the organization and the board evolves in its maturity and capacity for engagement and oversight of ESG matters, it should periodically revisit and update prior assessments to ensure relevancy.

Step 1: Understand the ESG Landscape and the ESG Universe

At the outset, boards should first recognize that ESG consists of three distinct categories. As a first step for ESG oversight, the board should gain a broader understanding of the landscape for each category and the current and emerging trends.

The board, with the assistance of the CEO / ED and management (and potentially external subject matter experts, depending on the resources of the NFP), should identify the broad universe of topics for each category – environmental, social and governance. We will refer to the numerous topics that may fall under these three categories as the "ESG universe."

As a starting point to assist board members, we have provided examples of the types of topics that may fall under each of these categories (as shown in **Diagrams 2-4**).

Key considerations

The ESG universe is expansive and the matters that are relevant may differ from organization to organization. For each example provided in the sample ESG universes below, there may be other categories and sub-categories that have not been identified in this document. If a particular matter is relevant or important to the organization, then the board, with the assistance of the CEO / ED and management, should use available resources to "drill-down" and develop a deeper understanding of the topic.

The intent is to ensure that the organization considers the ESG matters beyond their immediate mission. For example, an NFP whose mission is to provide clean drinking water in a developing nation may also need to consider the environmental impacts and labour (including volunteer labour) practices of their work in carrying out that mission.

DIAGRAM 2: ENVIRONMENTAL MATTERS: A SAMPLE UNIVERSE

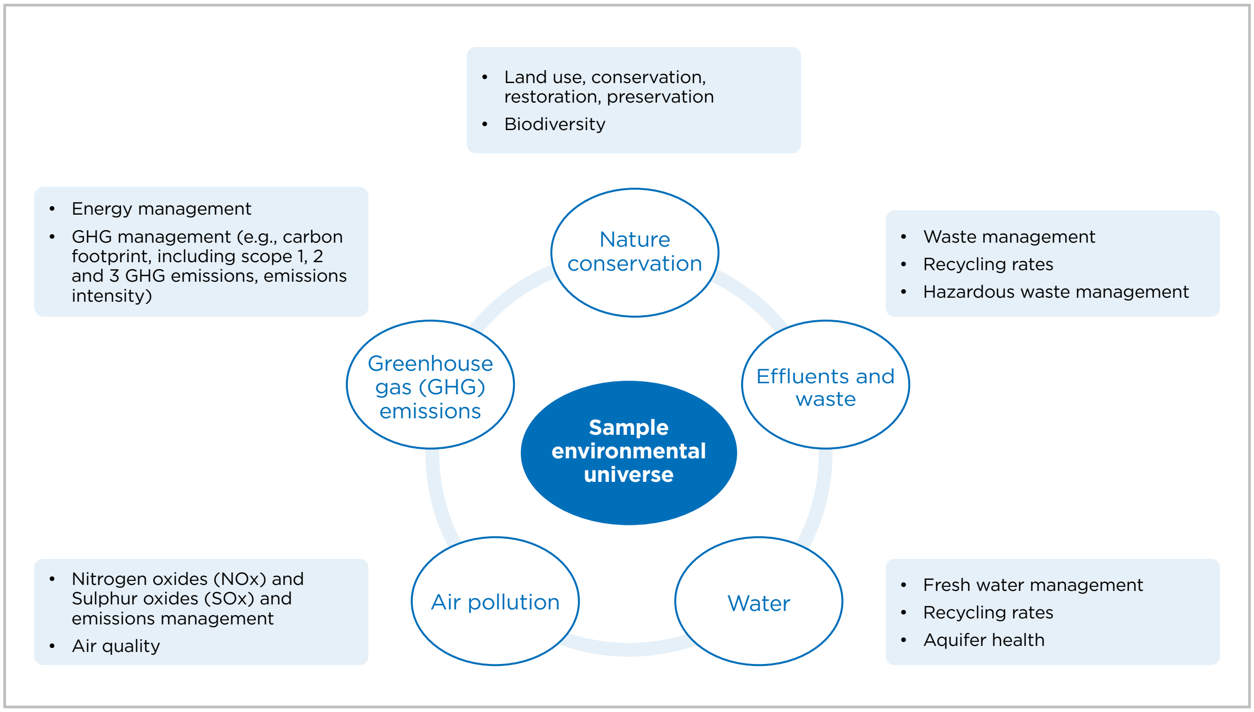
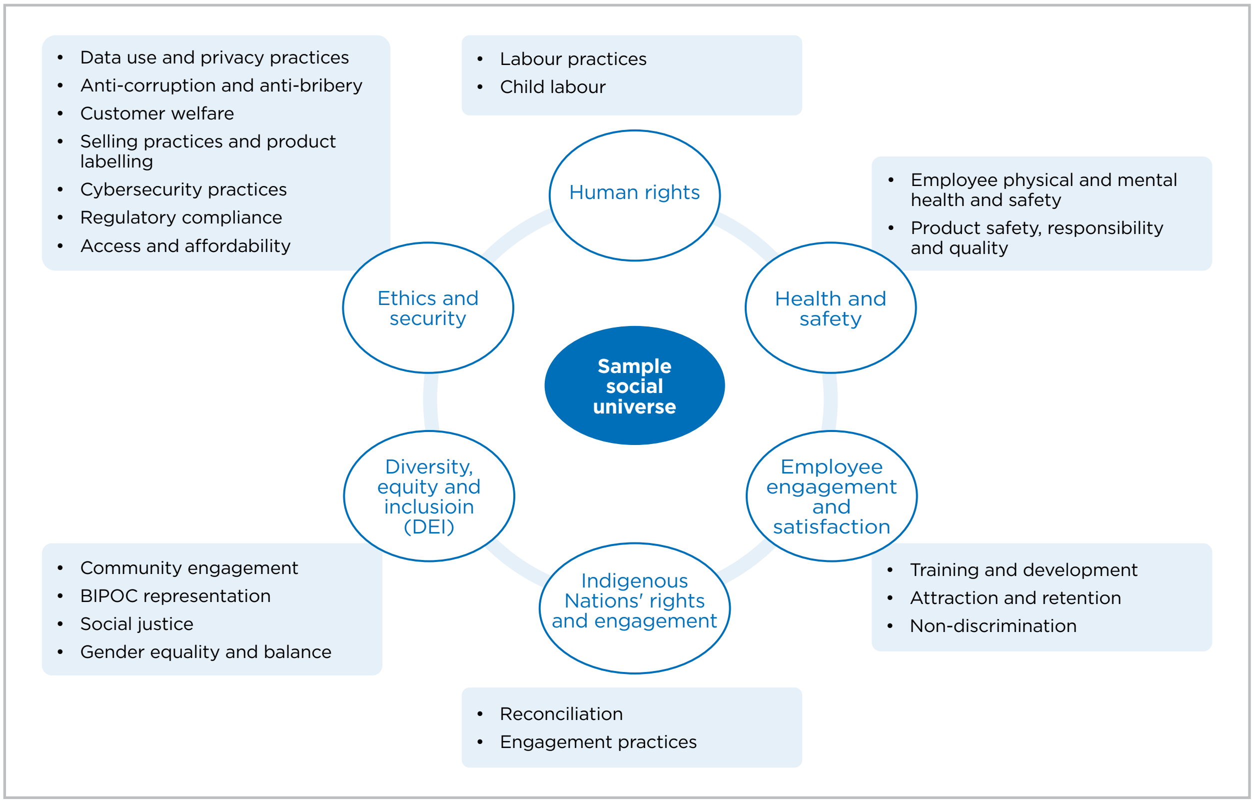
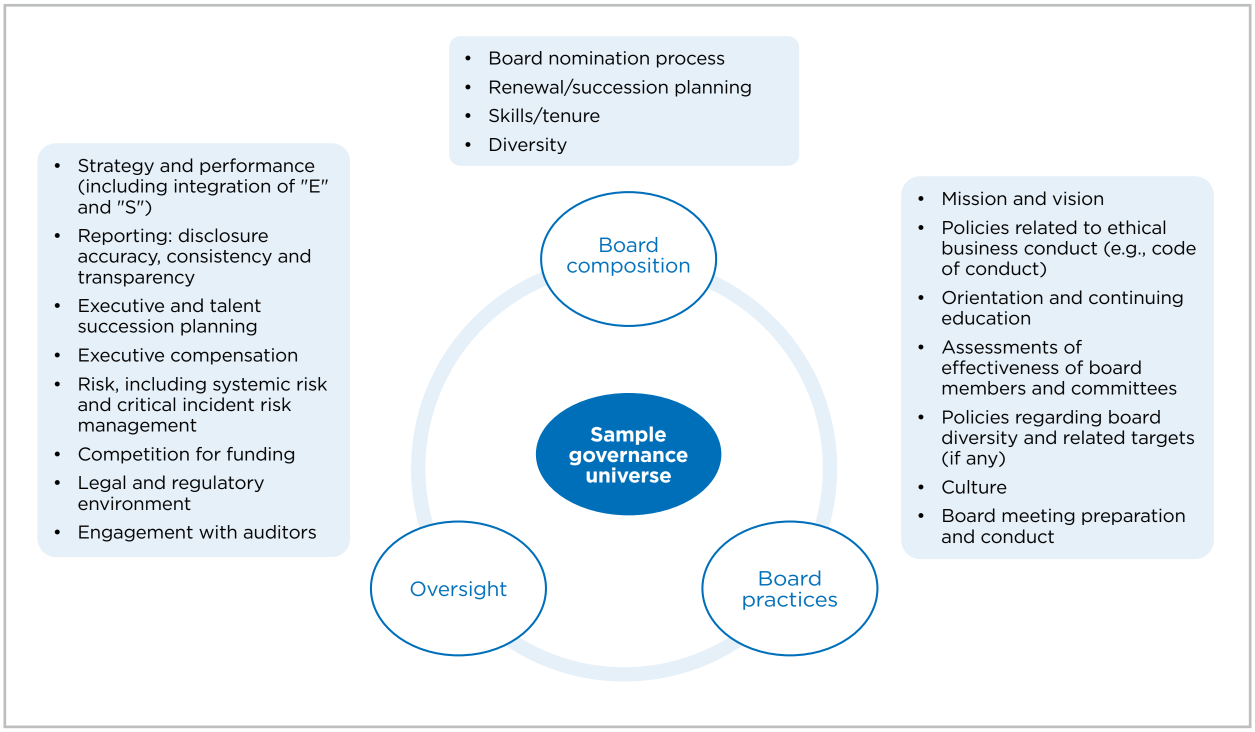


DIAGRAM 3: SOCIAL MATTERS: A SAMPLE UNIVERSE



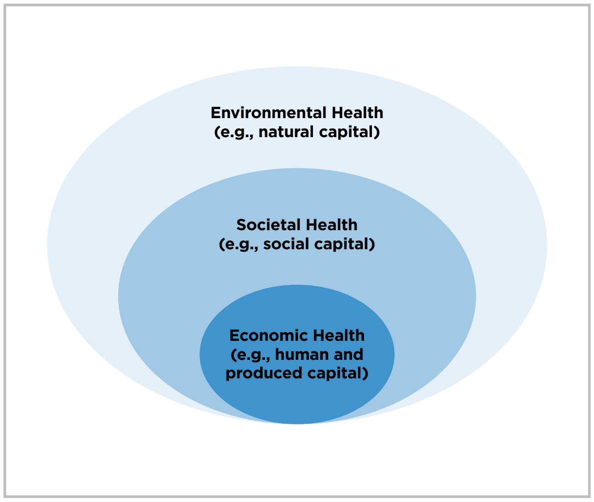
In the case of not-for-profit organizations, labour considerations include both paid-labour and volunteer labour.

DIAGRAM 4: GOVERNANCE MATTERS: A SAMPLE UNIVERSE



Understanding how it's all related

DIAGRAM 5: INTERDEPENDENCE OF ENVIRONMENTAL, SOCIAL AND ECONOMIC WELL-BEING



The health of our environment (e.g., natural capital) and the trust and cooperation built with stakeholders such as members, funders, beneficiaries of services, partners, and communities (e.g., social capital), underpin our economic sustainability and societal prosperity, as shown in **Diagram 5**. Due to the interdependence of our environmental, societal and economic sustainability, organizations are seeing and experiencing overlapping risks and opportunities. For example, climate change is not only an environmental issue that has resulted in economic risks; it is also a human rights and social justice issue. Racialized communities and low-income communities bear the greatest health impacts and financial risks associated with climate change (Levy & Patz, 2015). To address social injustice alongside climate change, these communities and their interests should be included in the identification of climate-change risks and in the development of mitigation and adaptation solutions. Additionally, while governance may have historically been seen as distinct from “E” and “S,” there is increasing recognition that “G” is in fact critically intertwined with “E” and “S” matters. For example, to make meaningful progress with respect to climate change, it is imperative to have the foundation of a strong governance structure.

As another example, Indigenous Peoples have deep knowledge and unique perspectives on the interconnected nature of ESG matters. As stated in Su*stainable Investment: Discussing Opportunities in ESG* commissioned by the First Nations Major Projects Coalition: “[Indigenous people] are the multi-generational stewards of the lands, waters, and resources that are now known as Canada. [They] are a vital part of, and have a vested interest in, building an environmentally and socially responsible future that will benefit all Canadians, Indigenous and non-Indigenous alike. The inclusion of Indigenous standards, knowledge, values and aspirations at all levels in both corporate decision-making, and in ESG frameworks, data collection and evaluation, will improve company performance, investment stability and social outcomes.” (Podlasly, Lindley-Peart & von der Porten, 2021). These considerations apply as much to not-for-profit organizations as they do to for-profit organization.

ESG matters cannot be viewed and managed in silos. Organizations need to account for intersectionality when developing their ESG strategy and process for board oversight.

Step 2: Understand Which ESG Matters Are Material and Require Board Oversight

Materiality is the quality of being important. As a general rule, materiality may be judged in relation to the reasonable prospect of an item or aggregate of items being significant to stakeholders in making decisions.

The next step is to scope and prioritize the board's involvement in the oversight of ESG matters. With the assistance of the CEO / ED (and through them their management team) and, potentially, external experts, the board needs to:

1. Obtain an understanding of which ESG matters identified in **Step 1** are material to the organization.
2. Obtain an understanding of the relevance or relationship of the ESG matters to the organization's risks and strategy (i.e., how does the ESG matter relate to the key risks, mission, strategic pillars and objectives that drive the organization's strategy?).
3. Determine which of these matters the board will be involved in overseeing and which will be assigned to the CEO / ED and management.

Key considerations

1. **Keep the context in mind**
   Determining materiality is a dynamic process and it may be more challenging when dealing with matters that are perceived as intangible and difficult to quantify (e.g., certain social matters). The CEO / ED and the board (with the support of experts as needed) will have to determine which ESG matters are material in the specific context.

2. **Engage Indigenous Peoples and key stakeholders early and often**
   It is critical for management, and potentially the board, to engage with Indigenous Peoples and key stakeholders, such as members, funders, beneficiaries of services, partners, relevant communities and governments to determine which ESG issues are material, or otherwise important, for the organization. Management should consider the communities and stakeholders on which the organization has the largest impact (e.g., minority groups, including Indigenous Peoples). In particular, boards should consider the recommendations of Truth and Reconciliation Commission of Canada: Calls to Action (Truth and Reconciliation Commission of Canada, 2015).

   This process is to ensure broad stakeholder perspectives are considered leading to a robust, inclusive and comprehensive analysis. Engagement with stakeholders and Indigenous Peoples should be conducted early and often in this process.

CASE STUDY: YMCA of Greater Toronto

The mission of the YMCA of Greater Toronto is to be a charity that "ignites the potential in people, helping them grow, lead, and give back to their communities." The organization's primary purpose is to offer a safe, inclusive destination with programs to support all community members through services ranging from children's swim lessons to youth shelters to employment support. However, this mission is not carried out without regard to other ESG considerations. For example, environmental sustainability is addressed through investments in new technology such as low flush toilets and showers, the use of less chlorine in swimming pools, LED lighting, green roofs and heating that reduces gas consumption. By focusing on these initiatives, the overall economic health of the organization is improved through cost savings to operations, funds which can ultimately be reinvested in programs to support their core purpose.

Since 2018-19 the organization has published an annual **Sustainability Report**, informed by the GRI Standards. The report focusses on the ESG issues that the organization considers material to stakeholders.

The YMCA of Greater Toronto also acknowledges where they have ongoing work in their ESG journey and the interconnection with how improvements can better the organization as a whole. In a **letter** to stakeholders dated July 1, 2021, the organization acknowledges that while committed to doing their part with regards to fostering truth and reconciliation with Indigenous communities, they still have work to do in this area in order to better serve not just the Indigenous community, but all of their stakeholders.

Step 3: Determine Allocation of Oversight Responsibility to the Full Board or a Committee of the Board

Once the board has determined which ESG matters will be a priority for board oversight (as identified in **Step 2**), it should determine whether the full board, or alternatively, a committee of the board, will take primary responsibility for oversight of the matter.

Key considerations

In determining how to allocate oversight to the full board or a committee of the board, the board should consider the nature of the ESG issue, the depth of expertise required, the time involved in oversight, and the mandates of existing board committees. For matters that haven't previously been addressed by the board or committee of the board there may be a significant learning curve. Board committees should regularly provide updates to the full board to ensure a cohesive and integrated approach to oversight.

Step 4: Conduct an Assessment of Material ESG Matters

Conduct a gap analysis of the current state versus desired state

The next step in the ESG oversight framework is to get a firm grasp on where the organization currently stands and what its goals or standards are on each ESG matter. To conduct this analysis, the board (or committee of the board as determined in **Step 3**) should complete the following assessment for each ESG matter that is subject to its oversight:

1. Determine the current state for each matter using appropriate quantitative metrics or qualitative considerations.

Key considerations

- The method of determination will vary depending on the nature of the issue. Some can be easily quantified, while others may be more subjective.
- What information is required to determine the current state and how might it be measured?

2. Establish goals or standards for each ESG matter.

Key considerations

- Management should be tasked to establish the goals or standards for each matter for the board's review.
- Such goals or standards may be informed by industry or peer benchmarking, externally imposed requirements (such as funders) and/or stakeholder engagement.
- Consider the appropriate period to realistically meet the goals or standards. Organizations that are earlier in their ESG journey may not yet have historical or current data available, and the board may instead focus on the organization's process or approach to begin to capture this data.

3. Gain an understanding of the gap that exists between the current state and the goal or standard, including considering relevant metrics.

Key considerations

- This assessment can assist in prioritizing and allocating resources. For example, if the gap analysis reveals that there is a significant deficit between the current state and the goal or standard for a critical matter, the board may decide to allocate more resources to quickly close the gap.
- A large deficit may also signal the need to engage external experts to better understand the reason for the gap, and steps required to meet the goal or standard.

Understand the strategy and actions to close the gap

Given the exposure identified by the gap, the CEO / ED and management should develop and present a plan, including strategy, actions, resources and timelines needed, to close the gap.

Step 5: Prioritize, Plan and Determine Resource Requirements

While all ESG matters can be significant, with the benefit of **Steps 1 through 4**, the board or committee of the board should prioritize the issues identified for the purpose of monitoring, as set out in **Step 6**.

Step 6: Monitor and Report

Monitoring and reporting are critical components of the iterative nature of the ESG oversight framework. To effectively monitor the organization's progress on ESG matters, the board in conjunction with the CEO / ED and management should determine the depth of review, the frequency of reporting and the appropriate metrics. This may include, for example, reporting the status of current and planned initiatives and performance against goals or standards.

Certain ESG matters may require reports from external advisors such as environmental assessments.

To meet the rising interest in ESG matters, organizations may have to consider disclosure of these matters in their annual report, which may be driven by funder demand or other key stakeholder interest.

Conclusion

In this rapidly evolving landscape, organizations are experiencing heightened scrutiny over their management of ESG matters. Modern and effective boards must be actively engaged in these critical matters to assist in managing risk and fostering long-term sustainability of the organization. The framework outlined above provides not-for-profit boards with a step-by-step tool to maintain effective oversight and governance of ESG matters.

Additional Resources

CPA Canada Resources

- CPA Canada, *Overseeing Environmental, Social and Governance (ESG) Matters: A Framework for Boards of Directors*
- CPA Canada, *The Rise of the Social Pillar: An Introduction to the 'S' in ESG*
- CPA Canada and TMX Group, *A Primer for Environmental & Social Disclosure*
- CPA Canada, *Environmental and Social Risks and Opportunities: Questions for Directors To Ask*
- CPA Canada, On the Radar, *The Business Impact of Environmental and Social Issues*
- CPA Canada, *Climate Change Briefing Questions for Directors to Ask*
- CPA Canada, *Climate Risk – Is it on Your Radar?*
- CPA Canada, *Disclosing the Impacts of Climate Change: A Process for Assessing Materiality*

Voluntary Reporting Standards and Frameworks for Disclosure of ESG Factors

- SASB Standards[1]
- TCFD Recommendations & Implementation Guidance
- TCFD Knowledge Hub
- GRI Standards

1 On June 9, 2021, the International Integrated Reporting Council (IIRC) and the Sustainability Accounting Standards Board (SASB) officially announced their merger to form the Value Reporting Foundation (VRF). Further, on November 3, 2021, the IFRS Foundation announced the planned consolidation of the VRF with the IFRS Foundation by mid-2022.

References

CPA Canada and TMX Group. (2020). *A primer for environmental & social disclosure* [PDF].

Levy, B. & Patz, J. (2015). *Climate change, human rights, and social justice*. *Annals of Global Health, Volume 81, Issue 3*, 310-322.

Locke, H. et al. (2021). *A nature-positive world: The global goal for nature* [PDF].

Podlasly, M., Lindley-Peart, M., & von der Porten, S. (2021). *Indigenous sustainable investment: Discussing opportunities in ESG*. Commissioned by the First Nations Major Projects Coalition.

Science Based Targets. Accessed on August 17, 2021. *Companies taking action*.

Truth and Reconciliation Commission of Canada. (2015). *Truth and Reconciliation Commission of Canada: Calls to action* [PDF].

YMCA of Greater Toronto. (2021). *Sustainability Report 2020-2021*.

YMCA of Greater Toronto. (2021). *Letter dated July 1, 2021*.