

Governance Professionals of Canada
ESG Governance: A New Expectation of Boards
Discussion Paper

Introduction

ESG Governance is becoming a new board standard, yet in general, boards and those who advise them lack education, case studies, guidelines and benchmarks to help them enhance board competency in this area.

To address this gap, Governance Professionals of Canada convened a session on ESG Governance in Vancouver, on May 27, 2019. It was attended by participants from a cross-section of business, academia and the non-profit sectors, and included people in corporate director, governance professional, sustainability and investment roles.

The purpose of the session was to explore the emerging trend and best practice of board oversight of company social and environmental risk, impacts and performance and begin to lay out a roadmap on this topic in Canada. The session addressed the following questions:

- **Drivers:** What is the legal, investor and business case for ESG governance and oversight by boards?
- **Knowledge and Practices:** What should sustainability practitioners, governance professionals and corporate directors know about ESG governance? What practices should competent boards have in place to build ESG governance in their organizations?
- **Role and Barriers:** What is the ESG role of the Governance Professional? What are the barriers, how to address them and what do governance professionals need to advance their efforts?

This Discussion Paper summarizes the key messages and take-aways of the session and is intended to stimulate further progress in ESG Governance at organizations across Canada.

The list of moderators, panelists and resources is provided in the appendix along with a link to a recording of the session.

Drivers

The imperative for addressing ESG at the board level is due to a whole new set of risks. Boards need to be equipped to understand the emerging social and environmental risks to which their organizations are exposed. Organizations are expected to disclose these risks and boards are asking “What does this new level of transparency mean?”, “How does an organization prepare for and address decarbonization and climate change in the economy?”, and “What are the human rights issues in our supply chain?”.

In Canada, there is no legal risk for a board to consider the organization's ESG performance. Nowhere does shareholder value legally supersede environmental and social imperatives. A board's fiduciary duties are to the best interests of the corporation viewed as a good corporate citizen, and under our common law that includes a duty to treat stakeholders equitably and fairly. The Supreme Court of Canada, for example, includes the environment as stakeholder. Current climate lawsuits served on governments and companies around the world will create a ripple effect. It's far better to be a leader than a laggard with respect to these issues. Leaders demonstrate due diligence through ESG policies, commitments and actions in addressing their ESG risks and opportunities.

Directors need to ask more questions of their advisors like: "Where does the environment fit in this?" "What are our climate-related financial risks?" "What is the life-cycle impact of our product?" "What are the negative externalities of our business model?" All of these are important questions from a legal perspective. Courts won't interfere if the due diligence is done.

Many investors are concerned with how ESG affects the value of corporations. Issues like sexual harassment, cyber security, corruption, human rights, climate risks are on their radar. Social expectations are growing. Given rising issues like Black Lives Matter, MeToo, gun violence, and the fact that our economy takes place on the traditional territories of Indigenous peoples, boards need to develop an understanding of stakeholder issues. Some boards are responding by adopting Board Diversity Policies in attempts to address gender, race and implicit bias on boards and within their organization's culture.

There is a gap with respect to a lack of professional training for Boards on ESG Governance. Directors need good advice and access to continuing education for professionals.

Knowledge and Practices

Within Canada, a number of companies have good ESG governance practices. The three organizations that shared their practices and journey at the conference were all recent recipients of the GPC annual Excellence in Governance ESG governance award. Their practices are combined and summarized below as a potential check list of good practices.

- Sustainability education is provided to the Board and Management
- Board formed a task team to explore and adopt sustainability strategies and management systems; another Board commissioned work to understand future scenarios that could impact its operations, and develop a long-term sustainability vision which became its corporate vision
- Board adopted a Sustainability Policy for the organization; another Board connected its government mandate to its mission statement, which framed the organization's definition of sustainability, adopted by the Board
- Board established an ad hoc board sustainability committee which became a standing committee five years later
- Board adopted a sustainability strategy with goals and targets

- Sustainability is included in the corporate scorecard
- Sustainability education is provided at the company AGM
- Sustainability is a factor in director recruitment via the skills matrix
- Sustainability is included in board onboarding and orientation
- Board has annual education session on a sustainability topic
- Board adheres to sustainable meeting practices for their meetings
- CEO compensation philosophy includes sustainability
- Executive leaders have an incented sustainability goal
- Board and management used guidance from the TCFD (Task Force on Climate-Related Financial Disclosures, see the appendix) to determine appropriate climate oversight roles of the risk and sustainability board committees and created a roadmap to improve governance and management in this area
- Board provides oversight of the company's disclosure of its ESG risks and performance

Boards of organizations that have sustainability in their mission, mandate and purpose seek strong sustainability performance and demonstrate enhanced EDG oversight. Co-operatives and government agencies are examples of this type of organization.

Top ESG issues which boards should address include:

- **Climate change** is a systemic risk for all organizations and all boards must address climate change as a macro disruptor of the economy and their organizations;
- **Income inequality**, covering both CEO and workforce compensation. This links to how organizations manage their human capital and whether workers are valued and recognized as an asset, not just a cost;
- **Ethical practices** such as the ethical implications of emerging digital technologies, and organizational diversity and inclusion;
- **Stakeholder governance** is an essential board practice; boards need to be much closer to the organization's stakeholders to understand their issues and expectations – having diverse stakeholders on the board can address this;
- **Truth and Reconciliation** needs to be understood by boards – they need education on the topic and to understand how their organization recognizes indigenous rights and advances employment; aboriginal board directorships are one possible board response.

Discussion topics included rotating chairs of other board committees to sit on the board sustainability committee; linking executive compensation to long-term ESG goals; strategies to recruit stakeholders to the board; and the importance of Director Education on sustainability governance.

Role and Barriers

Governance professionals shared how they have been advancing sustainability governance with their boards and participants discussed how to get started and advance on board ESG oversight.

Here are some of the strategies and recommendations presented as a checklist of options for the governance professional:

How to get started and advance on board ESG oversight:

- Commitment:** Commit to board ESG oversight and include ESG in the organization's strategic plan
- Education:** Invest in board education and include risks and benefits of ESG to create a common understanding among the directors and foster buy-in; seed committees of the Board with information from reputable sources to influence conversation
- Scenario Planning:** Develop the ESG culture of the board through scenario planning. Create and map ESG scenarios related to your organization and pick the easy ones to get started
- ESG Decision Tool:** Consider a "Sustainability Case Document" (which adds sustainability to financial considerations) to inform board decisions
- In Camera Discussions:** Create opportunities for ESG discussions within board in-camera sessions
- Benchmark:** Track best practices in ESG governance and determine where your organization is placed on the continuum; formalize these practices so they endure; for example, use GPC's ESG Award criteria as an education and benchmarking tool; organizations can assess their ESG governance performance and progress against it; recognize that issues may not be flagged as sustainability and that the organization and board may already have good sustainability practices in place
- Compensation:** Tie CEO compensation to sustainability and ESG performance and progress
- Risk Assessments:** Ensure risk assessments include climate change and other emerging ESG risks; Board Audit or Risk Committee can consider financial impacts of climate change
- Skills Matrix:** Include sustainability within the skills matrix to influence board recruitment
- Governance Advisors:** Require governance advisors and consultants to have ESG competencies so ESG becomes part of their routine advice

Participants identified the following barriers to pursuing ESG Governance and suggested some strategies to address them.

Barriers:

- Information overload for boards
- Lack of board turnover (inhibits diversity)
- Lack of business case
- Lack of internal resources and expertise
- Difficulty in making structured governance changes
- Lack of ESG Governance benchmarking for industry peers

How to address the barriers:

- Boards and management should prioritize and focus on material ESG issues
- Boards and Governance Committees should formalize the structures needed that will endure even with management turnover

- Corporate secretary to build relationship with board chair to enable structural change
- Show Boards and Governance Committees the ESG governance platform adopted by corporate leaders (e.g. UK); illustrate the “burning platform” by showing examples of industry leaders in ESG
- Governments and regulators should require ESG certification for companies and mandate ESG through corporate law
- Encourage universities to embed and mainstream ESG and business ethics in degree programs
- Create a continuing professional education program to upgrade the skills and knowledge of those who advise boards on ESG, beyond directors and corporate governance professionals (e.g. Investor Relations, Finance Executives)

The roles and barriers discussion concluded it is important for governance professionals to assess their ESG Governance practices to an ESG governance continuum or benchmark. This information could be shared with the Governance Committee to address and close gaps.

Conclusion

Governance Professionals of Canada will be furthering ESG Governance education and tool development over the coming few years. It believes ESG Governance is fast becoming a critical governance skillset for boards and those who advise them.

Appendix:

References and Resources:

- [Sustainability Accounting Standards Board](#) (SASB)
- [Principles for Responsible Investment](#) (PRI)
- [Chartered Professional Accountants of Canada](#) (CPA) (20 questions)
- [Canadian Coalition for Good Governance](#) (CCGG)
- [Task Force on Climate Related Financial Disclosures](#) (TCFD)
- [Canada 2030: Embedding Sustainability into Corporate Governance](#) (Conference Board)
- A link to the archived GPC webinar, which will be made available upon request.

Conference Moderators and Panelists:

- **John Bell**, Chief Advisor, Strategic Planning, Governance and Sustainability, BC Housing
- **Stephanie Bertels**, Director, Centre for Corporate Governance and Sustainability, SFU Beedie School of Business and Founder, Embedding Project
- **Michelle de Cordova**, Principal, ESG Global Advisors Inc.
- **Wendy King**, Vice President Legal, Risk & Governance, Capstone Mining Corp.
- **Annie Kors**, Lead Researcher for Diligent Institute, Diligent

- **Argiro Kotsalis**, Vice President, Legal and Chief Governance Officer, Vancouver Airport Authority
- **Carol Liao**, Assistant Professor, Peter A. Allard School of Law, University of British Columbia
- **Christopher Main**, Associate General Counsel, TELUS Corporation
- **Rita Parikh**, Board Director of Vancity, past Chair of MEC
- **Ian Robertson**, Vice President, Director and Portfolio Manager, Odlum Brown and Chair of the Responsible Investment Association
- **Shannon Rohan**, Responsible Investment Leadership Director, SHARE (Shareholder Association for Research & Education)
- **Christie Stephenson**, Executive Director, Dhillon Centre for Business Ethics, University of British Columbia's Sauder School of Business
- **Coro Strandberg**, President, Strandberg Consulting and GPC advisor on Sustainability Governance
- **Alexandra Wilson**, Board Director of The Co-operators, Chair of the Risk and Compensation Committee
- **Duncan Wilson**, Vice President, Environment, Community and Government Affairs, Vancouver Fraser Port Authority

Acknowledgements

GPC acknowledges the following people for contributing to this discussion paper:

Ann Duffy, President, The Ann Duffy Group

Coro Strandberg, President, Strandberg Consulting and GPC ESG Governance Advisor