On the 2022 ESG committee agenda

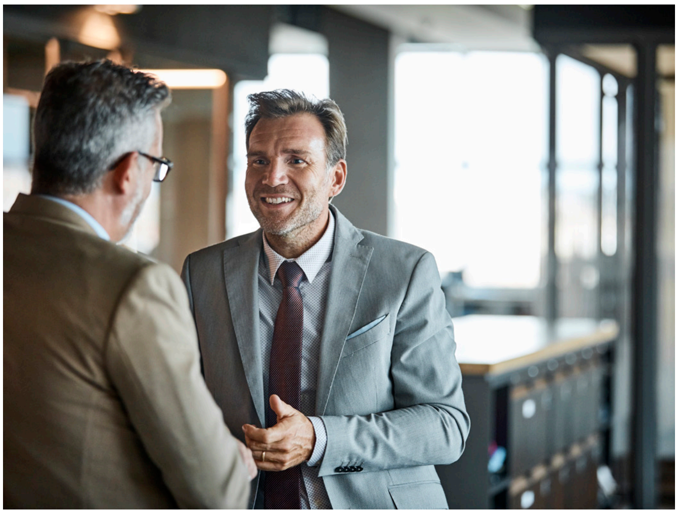
August 2022

How companies address climate change, diversity, equality and inclusion (DEI) issues, and other ESG risks is now viewed – by investors, research and ratings firms, employees, customers, and regulators – as fundamental to business and critical to long-term sustainability and value creation. Oversight of these risks and opportunities is a significant challenge, involving the full board and potentially multiple board committees.

During the last few years, the UAE has implemented various measures to ensure that sustainability is at the forefront of companies' goals. Some of the key initiatives driving this process include:

1. The UAE has deployed extensive efforts towards driving sustainability forward in the country under the framework of the UAE Vision 2021, Dubai 2040 Urban Master Plan, and in alignment with the UAE Green Agenda 2015-2030, the Paris Agreement and the UN Sustainable Development Goals ("SDGs"). The UAE government regards climate change as a significant concern and have enhanced their global participation and internal policies, placing themselves among regional leaders in climate action over the past decade.
2. Abu Dhabi Vision 2030 which intends on building a sustainable and diversified economy that is well-integrated into the global economy.
3. The Securities and Commodities Authority (SCA) requirement to issue sustainability reports for publicly listed companies. The aim is to provide all relevant and material information related to sustainability and show how companies are performing on relevant metrics, and how these factors are affecting the company's strategy and performance.
4. The Abu Dhabi Global Market (ADGM) also unveiled its Sustainable Finance Agenda Declaration at the Abu Dhabi Sustainable Finance Forum (ADSFF). The declaration acknowledges the UAE's and Abu Dhabi's commitment to addressing climate change and to fostering and integrating green and sustainable finance in Abu Dhabi and the region.

Accordingly, many companies within the UAE have already established or are in the process of establishing either a separate ESG board committee or including the mandate of ESG in one of the existing board committee's terms of reference to adequately oversee their ESG related activities.



Drawing on insight from our interactions with directors and business leaders, we highlight seven topics for ESG or related board committees to bear in mind as they consider and carry out their 2022 agendas.

1. Clarity of purpose

Oversight of risks and opportunities is a significant challenge, involving the full board and potentially multiple board committees. For example, elements of climate and diversity, equality and inclusion (DEI) oversight likely reside with the audit, risk, remuneration and other committees.

Consideration needs to be given to the coordination between committees as well as the information flows to the board itself. For example, which governance body is taking responsibility for the data and the systems that produce that data? Which committee is looking the various disclosures in the annual report?

Some overlap is to be expected, but this puts a premium on information sharing and communication and coordination among committees. It also requires that committees have the expertise to oversee the issues delegated to them.

2. An ESG-competent board

Oversight of ESG risk – and equally importantly, the opportunities – starts with an ESG-competent board. Not every board member needs to have deep ESG expertise, but the board, as a whole, needs to have ESG risk and its impact on long-term value creation, at the top of its collective mind. They need to understand which issues are of greatest risk or strategic significance to the company, how they are embedded into the company's core business activities, and whether there is strong executive leadership behind the company's response to ESG matters.

The board can play an active role on understanding ESG issues including the landscape of stakeholder expectations and demands. Ask:

- Is the board ESG literate and is it structured to engage meaningfully on ESG issues?
- Does the board evaluation process assess whether the board has the right mix of skills and whether the ongoing development activities are sufficient?
- How does the board get ESG literate?
- Are ESG matters (including issues around DEI, empathetic leadership, etc.) a factor when hiring directors and the executive team?

Work with the company secretary and senior executives to determine how best to get up to speed and build a strong foundation for informed oversight. Consider one- on-one conversations with the key players in the business and deep dives within committee meetings, alongside in-house briefings, and externally organized training opportunities.

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3. Engage proactively with shareholders and other stakeholders

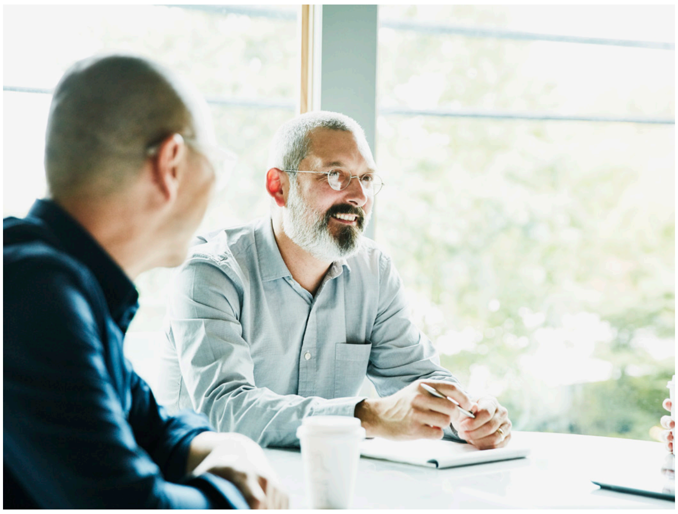
Investors are increasingly holding boards accountable for ESG matters and are eager to understand whether boards have sufficient knowledge and adequate processes to oversee the management of the key ESG-related risks and to provide informed, proactive guidance as stewards of long-term value.

Beyond the investor community, other stakeholders, whether that be employees, customers or the communities that provide companies their license to operate, are also voting against companies they perceive to be paying insufficient attention to ESG issues – whether that be related to climate change matters, diversity and inclusions issues and the treatment of individuals, or the company's contribution to society.

To best understand the views of its key stakeholders, the board should request periodic updates from management as to the effectiveness of the company's engagement activities:

- Does the company engage with, and understand, the ESG priorities of its largest shareholders and key stakeholders?
- Are the right people engaging with these shareholders and stakeholders – and how is the investor relations (IR) role changing (if at all)?
- What is the board's position on meeting with investors and stakeholders? Which independent directors should be involved?
- Will the organization be open to criticism from activists? Does the board have a road map to defend themselves?

In short: Is the company providing investors and other stakeholders with a clear, current picture of its ESG performance, challenges, and long-term vision – free of "greenwashing"? (Investors, other stakeholders, and regulators are increasingly calling-out companies and boards on ESG-related claims and commitments that fall short – and all indications are that they will continue to do so.)



4. Embed ESG, including climate risk and DEI issues, into risk and strategy discussions

How companies address ESG risks is now viewed – by investors, research and ratings firms, activists, employees, customers, and regulators – as fundamental to business and critical to long-term sustainability and value creation.

Climate change as a financial risk has certainly become more urgent over the last few years – not least because of the accelerating physical impacts of the climate crisis – the frequency and severity of floods, wildfires, rising sea levels, and droughts. But for many, the associated "transition risks" are as important and arguably more immediate – whether that be tax and regulatory interventions, technological changes, or customer behavior. A challenge for board and concerned board committee(s) is to help ensure that these transition risks are properly addressed as the company plots its future strategy - together with other climate change risks.

Equally, some of the challenges within the 'S' of ESG have rapidly risen up the agenda in recent years. Social factors such as how a company manages its relationships with its workforce, the societies in which it operates, and the political environment, are now central to a company's financial performance. Wellbeing and DEI issues have become mainstream.

Several fundamental questions should be front-and-centre in boardroom conversations about the company's ESG journey – not least how material ESG risks are identified and assessed in line with the organization's risk appetite. Embedding ESG identification and assessment into the existing enterprise risk management process might be a good starting point, however it is important to avoid focusing only on the downside risks. The board and concerned board committee(s) should also encourage management to consider the potential for innovation, disruption and value creation posed by ESG activities.

After determining which ESG issues are of strategic significance, the board should consider how the company is embedding them into core business activities (strategy, operations, risk management, incentives, and corporate culture) to drive long-term performance. Is there a clear commitment and strong leadership from the top, and enterprise-wide buy-in?

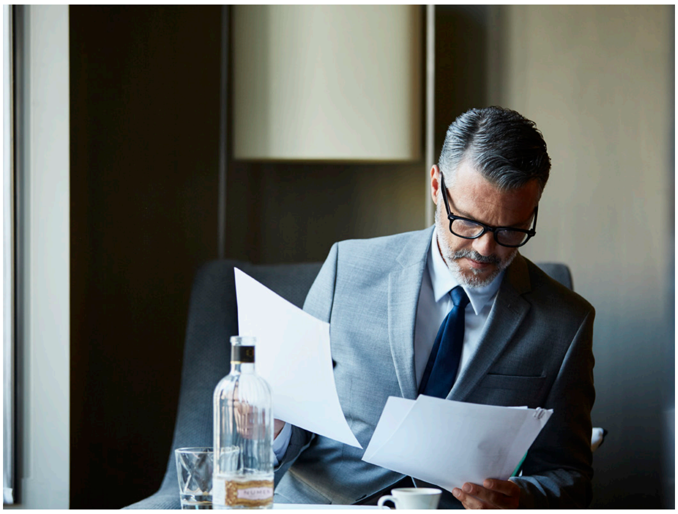
The board and its concerned committee(s) could consider:

- How is the ESG lens applied to the organization's strategic thinking?
- Is ESG thinking incremental to BAU or is it transformative?
- Does the process challenge the validity of the key assumptions on which the company's strategy and business model are based? Is there a case for taking a 'clean sheet' approach to the strategy/business model, asking what our business would look like if we started up today?
- How does the board establish a culture that supports the transition towards a more purposeful ESG-oriented organization?
- Are the incentives connected with executive compensation and the compensation philosophy of the organization as a whole a fit for purpose? When compensation becomes intertwined with something like ESG, other systems and processes quickly fall in line: recruitment, training and development, strategic planning, performance management.
- What metrics are monitored and reported to ensure the organization is on track?

5. Supporting a culture that drives the transition towards a more purposeful ESG oriented organization

Given the critical role culture plays in integrating ESG factors throughout an organization, the board and concerned board committee(s) can play a role in helping the board take a more proactive approach in understanding, shaping, and addressing any necessary cultural changes by considering:

- Does the board understand the culture it wants within the organization?
- Are key processes aligned with desired culture? Hiring, promotion, reward, how poor behaviour is addressed, etc.
- How does the board measure the culture and get assurance that it is what they think it is?
- Is the board leading the charge from the top?



6. Systems, controls and data

The quality of data for both strategic decision-making and reporting is crucial and the board and concerned board committee(s) can play a role in challenging the propriety of collected data and the systems that produce it. Is there substance behind collected and reported data? What additional assurance might be required?

Collecting data in a consistent method is important, especially for businesses with global operations and multiple product lines. In some cases, there is an established standard that is accepted by almost all investor groups. For example, the Greenhouse Gas Protocol is widely recognized as a way to report on emissions.

Still, tracking greenhouse gas emissions means companies need to have all those responsible for collecting data to gather it in the same way. Every level of the business should understand the metric, and how often it should be reported among other criteria. The board and its concerned committee(s) can focus on understanding the procedures and controls in place.

The board and its concerned committee(s) can also play a role in questioning the level of assurance is the company getting on ESG metrics; what is being assured, and by whom; and the value of the assurance received?

There's no single approach to ESG assurance. While it may be distinct for every industry and company, it's critical for companies to begin to identify their priorities before pressure from customers, shareholders, and others push to accelerate the company's timeline.

The board and its concerned committee(s) might work in conjunction with internal auditors (and perhaps the audit committee) to understand which metrics merit assurance. For example, labor in the supply chain could be a key area where a retail company's customers may want assurance. Or a consumer goods company's shareholders may want assurance on their claims of sustainable sourcing. Given its understanding of the rigor required to get the numbers right, the board and its concerned committee(s) can help the company decide how far the journey goes, even potentially working toward assurance of a full sustainability report.

Understanding the current landscape and the company's way forward, coupled with strategic investment in data collection and integrity, not only responds to stakeholder demands, but also may expand an organization's perspective, exposing new risks to its business model along with opportunities for growth and transformation. This is the true significance of bringing standardization and rigor to ESG measurement (and reporting).

7. Reporting to investors and other stakeholders

Investors and other stakeholders want to understand which issues are of greatest risk or strategic significance to the company, how they are embedded into the company's core business activities, and whether there is strong executive leadership behind the ESG efforts as well as enterprise-wide buy-in.

Materiality in the context of climate change and other ESG related topics identifies and assesses the company's impacts, including the actual and potential impacts on its stakeholders and therefore may differ from a purely financial materiality standard. Clarification up front can prevent misunderstandings arising. In any event, it is prudent to look at the spirit of any required regulations and beyond.

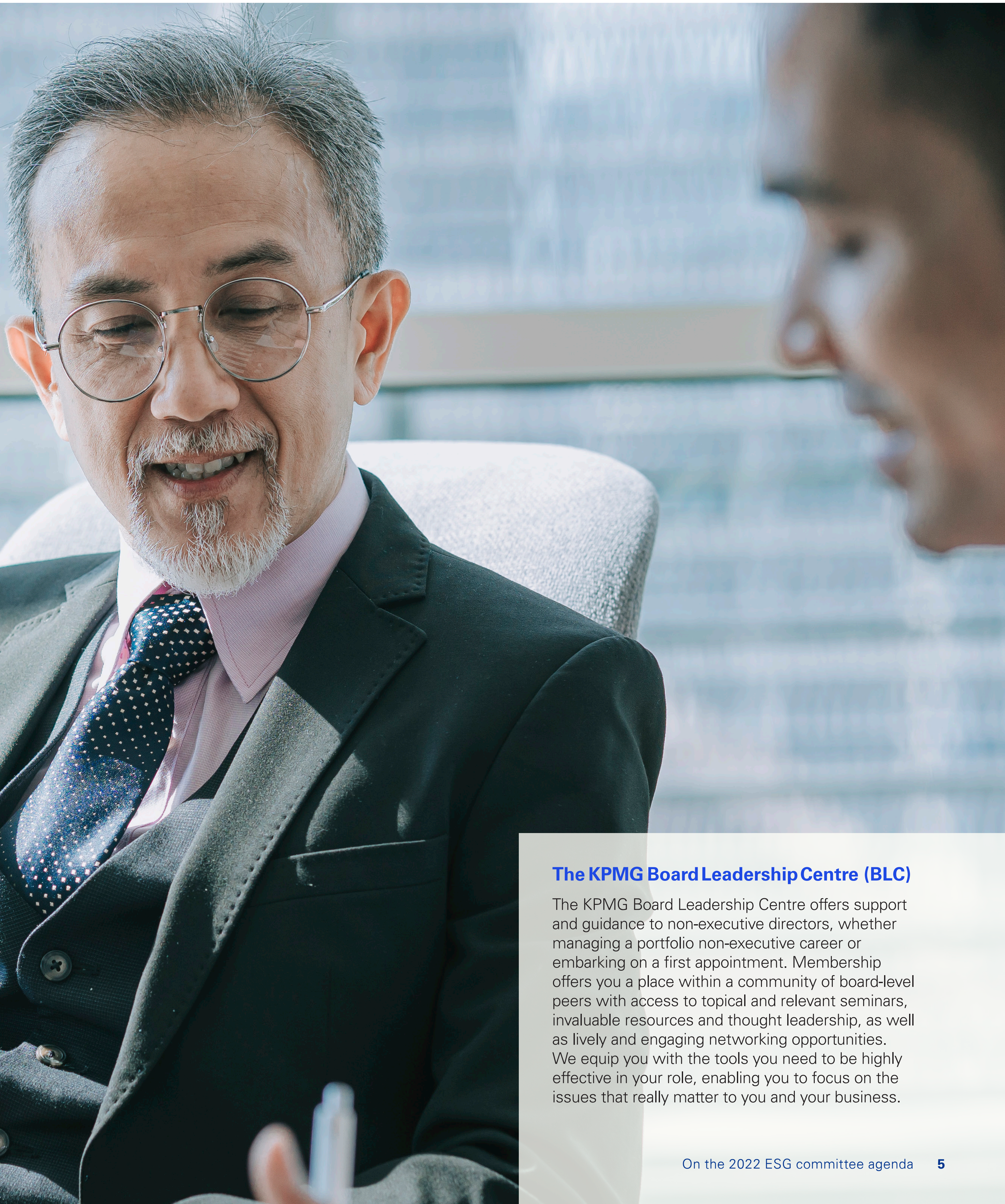
To that end, the board and its concerned committee(s) can encourage management teams to reassess the scope and quality of the company's ESG reports and disclosures. How is the company benchmarking against peers? What reporting frameworks have been considered? Are risks explicitly stated and disclosure provided on how they are mitigated? Is the link to the strategy clear?

Some critical questions for the board and its concerned committee(s) to consider include:

- What are the ESG issues that align most closely to the company's and stakeholders' priorities?
- Is the company currently reporting on its ESG efforts, and where?
- Do the company's disclosures comply with the appropriate laws, regulations and sector best practices?
- Do the company's disclosures reflect both what the company is doing now and where it is going, with accompanying metrics and goals?
- Is ESG-related data handled appropriately and aligned with corresponding regulations and the level of risk associated with the data?
- Is the ESG information included within the annual report monitored with the same rigor as conventional financial data?

- What are competitors measuring and reporting? Are there emerging regulatory requirements that a company should be aware of?
- Lastly, stay alert to International Sustainability Standards Board (ISSB) developments and in particular the prototype standards on climate-related disclosures and general requirements for sustainability disclosures.

These are based on existing frameworks and standards, including Task Force on Climate-Related Financial Disclosure (TCFD) and Sustainability Accounting Standards Board (SASB) and provide an indication of the disclosures that may soon be required under International Financial Reporting Standards (IFRS) Sustainability Disclosure Standards.



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Our KPMG IMPACT initiative aims to help clients future-proof their businesses amid times of increasing focus towards issues such as climate change and social inequality. The goal is to help them achieve success across 17 major Sustainable Development Goals (SDGs) and become more resilient and socially conscious.

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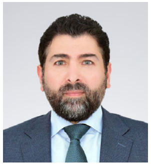

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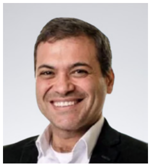

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