On the 2022 board agenda

KPMG Board Leadership Center

As in Switzerland companies focus on repositioning themselves for the future, it is increasingly clear that resilience – of strategy, the organization and operating muscle – is proving to be the great differentiator of the pandemic era. From pivoting to "remote everything" and focusing on workforce well-being to deepening digital engagement with customers and recalibrating supply chains, the ability to quickly adapt to dramatic disruptions and dislocations has defined the survivors and thrivers.

The unprecedented events of the past two years have clearly put corporate governance processes, including board oversight, to the test. Demands for action on ESG performance, including climate risk, increased cybersecurity risks (including ransomware attacks), economic and supply chain challenges, a fast-changing regulatory landscape and other factors impacting the global risk environment will continue to challenge even those boards at the top of their game.

In short, boards are at a pivotal moment. The need for today's boards to help their company reimagine, rethink and reset itself is probably a once-in-a-generation opportunity.

Eight burning topics

Drawing on insights from our latest survey work and interactions with board members and business leaders, we highlight here eight issues for boards to keep in mind as they consider and carry out their 2022 agendas.

Deepen the board's engagement in strategy and in envisioning the future

Given the volatile and fluid business environment ahead – managing remote workforces, employee activism, digital transformations and other accelerating megatrends, building more resilient supply chains and strengthening connections with customers whose behaviors, preferences and expectations are changing – it takes time to reassess the board's engagement in strategy. Organizations are well advised to review the alignment of their corporate purpose, culture, values and strategy. In addition, they should identify specific practices to drive quality boardroom discussions about strategy and the future.

A fundamental question for every board is whether boardroom conversations are, in fact, conversations. Does the board allocate sufficient agenda time to meaningful, two-way discussions between management and the board about forward-looking issues – challenging assumptions and considering scenarios (likely and unlikely) – versus reviewing historical, compliance-related information which, while essential, can crowd out valuable agenda time.

Effective engagement in strategy discussions (which investors expect) increasingly calls for a collaborative mindset: How can the board help management think through the implications of pressing and potentially existential strategic questions and decisions? And is management helping to set the context, providing meaningful materials to the board to prepare board members for those critical conversations and maximize the board's contribution?

In our discussions with experienced board members over the past year, a number of elements and practices were highlighted that may be helpful:

- Encourage management to revisit the strategic planning process. Is the process adequate in light of the speed and impact of megatrends – and does it capture the risks and potential disruptions on the horizon? Does the process challenge the validity of key assumptions that the company's strategy and business model are based on? Is it an iterative process – with milestones and opportunities to recalibrate – and does it bring in perspectives from throughout the organization, beyond the inner team?
- Develop a vivid picture of the future. This is never an easy undertaking, and it's particularly challenging today, given the level of uncertainty and transformational changes underway. Where are the company's industry and competition (both industry competitors and those in adjacent industries) headed? What might the business look and feel like in two, five or ten years? Make time for the board to have meaningful "what-if" discussions in a focused and urgent way – including devoting time to less likely scenarios (without getting overly theoretical). Risks and scenarios related to climate, ESG, human capital and supply chain should be front and center.
- Make resilience part of the strategy discussion. Full resilience is not only the ability to bounce back when something goes wrong; it's also the ability to stand back up with viable strategic options for staying competitive and on the offense.
- Understand the value of the board's lens. Management is immersed in running the business, looking around the corner and staying competitive – as they should be. Board members are likely to pick up broader perspectives and signals from their activities – and may be seeing and hearing things differently than management.

Embed ESG issues into risk and strategy discussions

How companies address climate change, child labor and other ESG risks is now viewed – by investors, research and ratings firms, activists, employees, customers and regulators – as fundamental to the business and critical to long-term sustainability and value creation. Expect the intense international regulatory focus on these issues and on transparency in particular to continue in 2022.

For many large companies in Switzerland, reporting on environmental, social and governance (ESG) aspects is already standard practice. According to KPMG's Survey of Sustainability Reporting 2020 "The Time has come", 80 of the 100 largest Swiss companies have already established a sustainability report. However, mandatory requirements become more frequent and complex. The heterogenous regulatory landscape is challenging to navigate.

As per this year's Corporate Governance Survey conducted by SWIPRA, 84% of asset managers and 89% of pension funds consider the current non-financial/sustainability report as not sufficiently meaningful.

Responsible Business Initiative: New reporting requirements for Swiss companies
With regard to sustainability reporting, the new law enters into force as per 1 January, 2022 and foresees a reporting obligation similar to the EU's Non-Financial Reporting Directive (NFRD) that companies in scope have to fulfill from 2023 on. Public interest companies (PIEs) that have more than 500 FTEs and whose revenue or balance sheet total exceeds CHF 40 million or CHF 20 million in two consecutive years, respectively, should report annually on environmental and social issues, employee matters, respect for human rights and anti-corruption. Further disclosures must be made in regard to strategy, business model and other aspects. The new legal provisions do not specify a reporting standard but allows the application of certain generally accepted standards. This means that companies reporting for the first time can initially focus on those reporting elements required by law.

Besides these general transparency requirements, further reporting and due diligence rules in the area of conflict minerals and child labor might be relevant for a broader scope of companies, not only PIEs. This might require companies to implement new compliance management systems and establish additional transparency in their supply chain.

The clamor for attention to climate change as a financial risk has become more urgent, driven by a confluence of factors, the most visible of which is the accelerating physical impact of climate change – including the frequency and severity of floods, wildfires, rising sea levels and droughts – as well as concern by many experts that the window for preventing more dire long-term consequences is rapidly closing. The Task Force on Climate-related Financial Disclosures (TCFD) recommendations on climate-related financial disclosures are already widely adopted and applied by a growing number of organizations across sectors and jurisdictions. They were designed to enable investors to take decisions based on relevant, forward-looking information on the potential impact of climate change on a company's business model and strategy that can be included in mainstream financial filings. The Swiss Federal Council, in line with the developments in other countries, has decided to introduce new binding rules to require large Swiss public interest entities to report along the TCFD recommendations.

Monitoring the rapidly changing legal and regulatory developments regarding climate change is critical as regulators and policy makers globally are placing greater demands on companies to take action – as evidenced by the recent COP26 summit which brought parties together to accelerate action towards the goals of the Paris Agreement and the UN Framework Convention on Climate Change.

Several fundamental questions should be front and center in boardroom conversations about the company's ESG journey. After determining which ESG issues are of strategic significance, how is the company 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?

Oversight of these risks and opportunities is a significant challenge, involving the full board and potentially multiple board committees. For example, elements of climate, ESG as well as diversity and inclusion oversight likely reside with the audit and/or remuneration committees – and other committees, such as an ESG or sustainability committee, may have responsibilities as well. 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.

Engage proactively with shareholders, activists, and other stakeholders

Given the intense investor and stakeholder focus on climate risk, ESG and diversity and inclusion, particularly in the context of long-term value creation, engagement with shareholders and stakeholders should be a priority. Institutional investors and other stakeholders are increasingly holding boards accountable for company performance and are continuing to demand greater transparency, including direct engagement with board members on big-picture issues such as strategy and ESG. Indeed, transparency, authenticity and trust are not only important to investors, but increasingly to employees, customers, suppliers and communities – all of whom are holding companies and boards to account.

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 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 board members should be involved?

In short: Is the company providing investors and other stakeholders with a clear, current picture of its 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.)

Strategy, executive remuneration, management performance, climate risk, other ESG initiatives, diversity and inclusion and human capital management as well as board composition and performance will remain squarely on investors' radar during the 2022 AGM season. We can also expect investors and stakeholders to focus on how companies are adapting their strategies to address the economic and geopolitical uncertainties and dynamics shaping the business and risk environment in 2022.

Make talent, human capital management and CEO succession a priority

The last two years further highlighted the strategic importance of human capital management (HCM) issues – including those employee and supply chain health and safety issues that are critical to the company's performance and reputation.

Institutional investors have been increasingly vocal about the importance of human capital and talent development programs and their link to strategy – including calling for more engaged board oversight and enhanced disclosure of HCM-related metrics.

Consider management's processes for developing HCM-related metrics and the controls for ensuring data quality – and help ensure that the disclosures demonstrate the company's commitment to critical human resources issues.

In 2022, we can expect continued scrutiny of how companies are adjusting their talent development strategies. The challenges of finding, developing and retaining talent, amid a labor-constrained market has created a war for talent. Does the board have a good understanding of the company's talent strategy and its alignment with the company's broader strategy and forecast needs for the short and long term? Which roles throughout the organization are mission-critical, and what are the challenges keeping those roles filled with engaged employees? Which talent categories are in short supply and how will the company successfully compete for this talent? Does the talent strategy reflect a commitment to diversity and inclusion at all levels?

More broadly, as millennials and younger employees – who increasingly choose employers based on alignment with their own values – join the workforce in large numbers and talent pools become globally diverse, is the company positioned to attract, develop and retain top talent at all levels?

Pivotal to all of this is having the right CEO in place to drive culture and strategy, navigate risk, and create long-term value for the enterprise. The board should ensure that the company is prepared for a CEO change – whether planned or unplanned, on an emergency interim basis or permanent. CEO succession planning is a dynamic and ongoing process, and the board should always be focused on developing a pipeline of potential CEO candidates as well as all other C-suite positions. Succession planning should start the day a new CEO is named.

How robust are the board's succession planning processes and activities? Is the nomination committee reviewing the plans at least once a year – but likely more often in these uncertain times? Are succession plans in place for other key executives? How does the board get to know the high-potential leaders two or three levels below the C-suite – especially in a work-from-home environment when office visits and board-executive in person meetings may not be feasible?

Approach cybersecurity and data privacy holistically as data governance

The rapid shifts that companies have made during the pandemic to keep their businesses up and running – remote work arrangements, supply-chain adjustments and increased reliance on online platforms – have been a boon to organized crime, hacktivists and nation-states. Cyberattacks of all types proliferated during the pandemic, highlighting the far-reaching implications for supply chains and operations, as well as the ongoing cybersecurity challenge facing companies.

Boards have made strides in monitoring management's cybersecurity effectiveness – for example, with greater IT expertise on the board and relevant committees, company-specific dashboard reporting to show critical risks and more robust conversations with management. Despite these efforts, the acceleration of digital strategies, remote work and hybrid work models, increased regulatory scrutiny of data privacy and the growing sophistication of cyber attackers all point to the continued cybersecurity challenge ahead.

As we've noted, data governance overlaps with cybersecurity, but it's broader. Data governance includes compliance with industry-specific privacy laws and regulations, as well as privacy laws and regulations that govern how personal data – from customers, employees or vendors – is processed, stored, collected and used. Data governance also includes the company's policies and protocols regarding data ethics – in particular, managing the tension between how the company may use customer data in a legally permissible way and customer expectations as to how their data will be used.

Managing this tension poses significant reputation and trust risks for companies and represents a critical challenge for leadership.

To oversee cybersecurity and data governance more holistically:

- Insist on a robust data governance framework that makes clear how and what data is being collected, stored, managed and used, and who makes decisions regarding these issues.
- Clarify which business leaders are responsible for data governance across the enterprise – including the roles of the chief information officer, chief information security officer and chief compliance officer.
- Reassess how the board – through its committee structure – assigns and coordinates oversight responsibility for both the company's cybersecurity and data governance frameworks, including privacy, ethics and hygiene.

Reassess the company's crisis prevention and readiness efforts

The litany and severity of crises that companies have found themselves facing in recent years looms large, with crisis prevention and readiness now featuring more prominently than ever in boardroom conversations. Crisis prevention goes hand in hand with good risk management – identifying and anticipating risks and putting in place a system of reporting and controls to help prevent or mitigate the impact of such risk events.

We're clearly seeing an increased focus by boards on cultural risks as well as key operational risks across the extended global organization – e.g. supply chain and outsourcing risks, information technology and data security risks, etc. Does the company understand its critical operational risks, including "mission-critical" company and industry risks?

What's changed in the operating environment? Has the company experienced any control failures, and if so, what were the root causes? Is management sensitive to early warning signs regarding safety, product quality and compliance?

Periodically reassess the clarity and appropriateness of risk oversight responsibilities among the board's committees – being mindful not to overload the audit committee's agenda and recognizing the importance of good communication and coordination among committees, as certain risks likely touch multiple committees.

Help ensure that management is weighing a broad spectrum of what-if scenarios – from supply chains and the financial health of vendors to geopolitical risks, natural disasters, terrorist acts and cyber threats.

Is the company's crisis response plan robust and ready to go? Is the plan actively tested or war-gamed – and updated as needed? Does it take into account the loss of critical infrastructure – e.g. telecommunication networks, financial systems, transportation as well as water and energy supplies? Are there communication protocols to keep the board apprised of events and the company's response? Even the best-prepared companies will experience a crisis; but companies that respond quickly and effectively – and with a robust communication strategy – tend to weather crises better.

A final, important reminder from the COVID-19 pandemic experience: While management should keep the board apprised throughout a crisis, the board should avoid information requests that unduly add to management's workload and potentially distract the CEO and management team from mission-critical activities.

Help set the tone and closely monitor the culture of the oganization

The events of the last two years have increased the risk of ethics and compliance failures, particularly given the enhanced fraud risk due to employee financial hardship and the pressure on management to meet financial targets. Closely monitor the tone at the top and culture throughout the organization with a sharp focus on behaviors (not just results) and yellow flags. Is senior management sensitive to human resource issues, particularly the pressures on employees (both in the office and at home), employee health, safety and well-being, productivity, engagement and morale as well as normalizing work-from-home arrangements? Does the company make it safe for people to do the right thing?

Headlines of sexual harassment, price gouging, aggressive sales practices and other wrongdoing continue to put corporate culture, leadership and incentives front and center. With the near-instantaneous speed of social media, corporate crises (particularly when self-inflicted) are hitting corporate reputations fast and hard, with investors, regulators and others increasingly asking, "Where was the board?".

Given the critical role that corporate culture plays in driving a company's performance and reputation, we see boards taking a more proactive approach to understanding, shaping and assessing corporate culture. Have a laser focus on the tone set by senior management and zero tolerance for conduct that is inconsistent with the company's values and ethical standards, including any "code of silence" around such conduct. Be sensitive to early warning signs, verify that the company has robust whistle-blowing and other reporting mechanisms in place and that employees are not afraid to use them. Closely monitor the reporting systems to understand how claims are addressed and resolved and identify trends. If the company has a sizeable workforce and few or no claims, the board should dig deeper.

Understand the company's actual culture (the unwritten rules versus those values employees are supposed to adhere to); use all the tools available – surveys, internal audit, hotlines, social media, virtual town halls as well as walking the floors and visiting facilities – to monitor the culture and see it in action. Recognize that the tone at the top is easier to gauge than the mood in the middle and the buzz at the bottom. How does the board gain visibility into the middle and bottom levels of the organization? Make sure that incentive structures align with culture and strategy and encourage the right behaviors. Take a hard look at the board's own culture for signs of groupthink or discussions that lack independence or contrarian voices. Focus not only on results, but also on the behaviours driving results.

Think strategically about talent and diversity in the boardroom

Boards, investors, regulators and other stakeholders are increasingly focused on the alignment of board composition with the company's strategy – with diversity front and center.

Indeed, the increased level of investor engagement on this issue highlights investor frustration over the relatively slow pace of change in boardrooms, and points to the central challenge with board composition: a changing business and risk landscape. Addressing competitive threats and business model disruption, technological innovation and digital changes, climate and ESG risks, cyber risk and global volatility requires a proactive approach to board-building and board diversity – of skills, experience, thinking, gender and race/ethnicity.

Notably, more than half of the board members we surveyed recently said their board's composition would be (moderately or completely) different if they were able to rebuild it to best meet the company's needs for today and the future. And more than 50 percent expressed concern that a lack of diverse views in the boardroom "hampers insightful discussions or identification of blind spots and issues important to the company's future".

About the KPMG Board Leadership Center

The KPMG Board Leadership Center offers support and guidance to board members. We equip you with the tools and insights you need to be highly effective in your role, enabling you to focus on the issues that really matter to you and your business. In addition, we help you to connect with peers and exchange experiences.

Learn more at kpmg.ch/blc

Contacts

KPMG AG
Badenerstrasse 172
PO Box
8036 Zurich

kpmg.ch

Rolf Hauenstein
Partner, Head of the
Board Leadership Center
KPMG Switzerland

+41 58 249 42 57
rhauenstein@kpmg.com

Hélène Béguin
Partner, Chairwoman of
the Board of Directors
KPMG Switzerland

+41 58 249 45 74
hbeguin@kpmg.com

Prof. Dr. Reto Eberle
Partner, Member of the
Board Leadership Center
KPMG Switzerland

+41 58 249 42 43
reberle@kpmg.com