On the 2023 board agenda

KPMG Board Leadership Center

December 12, 2022

Boards can expect their oversight and corporate governance processes to be tested by an array of challenges in the year ahead—including global economic volatility, the war in Ukraine, supply chain disruptions, cybersecurity risks, regulatory and enforcement risks, and social risks, such as pay equity and the tight talent market.

The business and risk environment has changed dramatically over the past year, with greater geopolitical instability, surging inflation, and the prospect of a global recession added to the mix of macroeconomic risks companies face in 2023. The increasing complexity and fusion of risks unfolding simultaneously, and the increased interconnectedness of these risks up the ante for boards to have holistic risk management and oversight processes.

In this volatile operating environment, demands from employees, regulators, investors, and other stakeholders for greater transparency and disclosure—particularly around cybersecurity, climate, and other environmental, social, and governance (ESG) risks—will continue to intensify.

Drawing on insights from our latest surveys and interactions with directors and business leaders, we highlight nine issues to keep in mind as boards consider and carry out their 2023 agendas:

- **Maintain focus on how management is addressing geopolitical and economic risks and uncertainty.**
- **Monitor management's projects to build and maintain supply chain resilience.**
- **Reassess the board's committee structure and risk oversight responsibilities.**
- **Keep ESG, including climate risk and DEI, embedded in risk and strategy discussions and monitor U.S. and global regulatory developments.**
- **Clarify when the CEO should speak out on social issues.**
- **Approach cybersecurity, data privacy, and artificial intelligence (AI) holistically as data governance.**
- **Make talent, human capital management (HCM), and CEO succession a priority.**
- **Engage proactively with shareholders, activists, and other stakeholders.**
- **Think strategically about talent, expertise, and diversity in the boardroom.**

Maintain focus on how management is addressing geopolitical and economic risks and uncertainty.

Heading into 2023, developments in the war in Ukraine, tensions with China, supply chain disruptions, energy shortages in Europe, cybersecurity, inflation, rising interest rates, market volatility, trade tensions, and the risk of a global recession will continue to drive global volatility and uncertainty.

© 2022 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved. The KPMG name and logo are trademarks used under license by the independent member firms of the KPMG global organization. NDP382757-1A

This environment will call for continual updating of the company's risk profile and more scenario planning, stress-testing strategic assumptions, and analyzing downside scenarios. Leaders will need to assess the speed at which risks are evolving, their interconnectedness, the potential for multiple crises at the same time, and whether there is flexibility in the company's strategy to pivot.

Oversee management's reassessment of the company's processes for identifying and managing these risks and their impact on the company's strategy and operations.

- Is there an effective process to monitor changes in the external environment and provide early warning that adjustments to strategy might be necessary?
- Is the company prepared to weather an economic downturn?

Help management keep sight of how the big picture is changing—connecting dots, thinking differently, and staying agile and alert to what's happening in the world. Disruption, strategy, and risk should be hardwired together in boardroom discussions.

Challenge and question management's crisis response plans.

- Are they robust, actively tested or war-gamed, and updated as needed?
- Do they include communications protocols to keep the board apprised of events and the company's response as well as to determine when/if to disclose matters internally and/or externally?

Make business continuity and resilience part of the discussion. *Resilience* is the ability to bounce back when something goes wrong *and* the ability to stand back up with viable strategic options for staying competitive and on the offense in the event of a crisis, such as ransomware, a cyberattack, or a pandemic.

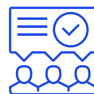
Monitor management's projects to build and maintain supply chain resilience.

Companies continue to navigate unprecedented supply chain stresses and strains with the ultimate goal of assuring supply—and survival. Amid ongoing supply chain turmoil, many companies are implementing efforts to address vulnerabilities and improve resilience and sustainability. Boards should help ensure that management's projects to rethink, rework, or restore critical supply chains are carried out effectively, such as:

- Updating supply chain risk and vulnerability assessments
- Diversifying the supplier base
- Reexamining supply chain structure and footprint
- Developing more local and regional supply chains
- Deploying technology to improve supply chain visibility and risk management
- Improving supply chain cybersecurity to enhance resilience from disruption and reduce the risk of data breaches, such as SolarWinds and Kaseya
- Developing plans to address future supply chain disruptions.

Importantly, are supply chain projects being driven by an overarching vision and strategy? Who is leading the effort, connecting critical dots, and providing accountability?

At the same time, boards need to sharpen their focus on the company's efforts to manage a broad range of ESG risks in its supply chain. Such risks—particularly climate change and other environmental risks as well as important "S" risks such as human rights; forced labor; child labor; worker health and safety; and diversity, equity, and inclusion (DEI) in the supply chain—pose significant regulatory and compliance risks as well as critical reputation risks for the company.



Reassess the board's committee structure and risk oversight responsibilities.

The increasing complexity and fusion of risks unfolding simultaneously requires a more holistic approach to risk management and oversight. At the same time, investors, regulators, ESG rating firms, and other stakeholders are demanding higher-quality disclosures—particularly on climate, cybersecurity, and other ESG risks—and about how boards and their committees oversee the management of these risks.

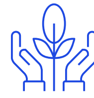
Given this challenging risk environment, many boards are reassessing the risks assigned to each standing committee. In the process, they are considering whether to reduce the major risk categories assigned to the audit committee beyond its core oversight responsibilities (financial reporting and related internal controls and oversight of internal and external auditors)—by transferring certain risks to other committees or potentially creating a new committee.

© 2022 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved. The KPMG name and logo are trademarks used under license by the independent member firms of the KPMG global organization. NDP382757-1A

The challenge for boards is to clearly define the risk oversight responsibilities of each standing committee, identify any overlap, and implement a committee structure and governance processes that facilitates information sharing and coordination among committees. While board committee structure and oversight responsibilities will vary by company and industry, we recommend four areas of focus:

- Does the audit committee have the time and members with the experience and skill sets necessary to oversee areas of risk (beyond the committee's core responsibility) that the audit committee has been assigned—such as cybersecurity, data privacy, supply chain, geopolitical, climate, and other ESG-related risks—as well as the adequacy of management's overall ERM system and processes?
- Does another board committee(s) have the time, composition, and skill set to oversee a particular category of risk? Is there a need for an additional committee, such as a technology, sustainability, or risk committee? Is there a need for new directors with skill sets or experience to help the board oversee specific risks?
- Recognize that rarely does a risk fit neatly in a single, siloed risk category. While many companies historically managed risk in siloes, that approach is no longer viable and poses its own risks.
- Identify risks for which multiple committees have oversight responsibilities, and clearly delineate the responsibilities of each committee. For example, in the oversight of climate and other ESG risks, the nom/gov (or sustainability committee), compensation, and audit committees likely each have some oversight responsibilities. And where cybersecurity oversight resides in a technology committee (or other committee), the audit committee may also have certain responsibilities. To oversee risk effectively when two or three committees are involved, boards need to think differently about how to coordinate committee activities. For example, some boards have established a board-level ESG committee, composed of members of the board's existing standing committees, focused on ESG disclosures and issues. Also see *On the 2023 audit committee agenda*.

Essential to effectively managing a company's risks is maintaining critical alignments—of strategy, goals, risks, internal controls, incentives, and performance metrics. Today's business environment makes the maintenance of these critical alignments particularly challenging. The full board and each standing committee should play a key role in helping to ensure that—from top to bottom—management's strategy, goals, objectives, and incentives are properly aligned, performance is rigorously monitored, and that the culture the company has is the one it desires.



Keep ESG, including climate risk and DEI, embedded in risk and strategy discussions and monitor U.S. and global regulatory developments.

How companies address climate change, DEI, and other ESG issues is viewed by investors, research and ratings firms, activists, employees, customers, and regulators as fundamental to the business and critical to long-term value creation. At a time of low trust in government and institutions, corporations are being asked to do more to solve societal problems—or run the risk of losing the social license to operate.

While there are trillions of dollars in investments in various types of ESG funds, there is also pushback against ESG, as some states and public officials are stepping up efforts to prevent investors—particularly state pension funds—from considering ESG issues in their investment decisions.

Forbes noted that this pushback may, in fact, be good for ESG: "Recent pushback on ESG is a sign that it is evolving, with stakeholders taking steps to make ESG efforts more consistently tangible, meaningful, and measurable. Calling out misinformed approaches helps make the case for proper design and action. Many business leaders are using the critique of ESG programs to analyze their current approach and rethink their strategies to create more value and impact."[1]

The ESG issues of importance will vary by company and industry. For some, it skews toward environmental, climate change, and emission of greenhouse gases. For others, it skews toward DEI and social issues.

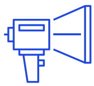
- How is the board helping to ensure that these issues are priorities for the company and that the company is following through on its commitments?
- How is the company embedding these issues into core business activities (strategy, operations, risk management, incentives, and corporate culture) to drive long-term performance?

[1] John M. Bremen, "Why the Pushback On ESG Is Good for ESG," June 16, 2022.

© 2022 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved. The KPMG name and logo are trademarks used under license by the independent member firms of the KPMG global organization. NDP382757-1A

- Is there a clear commitment and strong leadership from the top and enterprise-wide buy-in? Are there clear goals and metrics?
- Is management sensitive to the risks posed by greenwashing?

Demands for higher-quality climate and other ESG disclosures should be prompting boards and management teams to reassess and adjust their governance and oversight structure relating to climate and other ESG risks—and to monitor SEC and global regulatory developments in these areas. Indeed, the spotlight has intensified with the SEC's rulemaking proposals for climate and cybersecurity disclosures, anticipated SEC rulemaking on HCM disclosures, recent ESG-related SEC enforcement actions, shareholder proposals on ESG issues, and other global ESG and sustainability proposals (EU, UK, etc.).



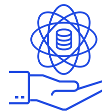
Clarify when the CEO should speak out on social issues.

From *Roe v. Wade* and voting rights to climate change and equity and inclusion, polarizing social and political issues are moving front and center in the boardroom as employees, customers, investors, and stakeholders sharpen their scrutiny of a company's public positions—or silence. When should a CEO speak out on controversial issues, if at all, and what are the potential consequences?

Consider what role the board should play in establishing parameters for the CEO as the voice of the company. Some boards have written policies; others have an informal understanding that the CEO will confer with board leadership before speaking on a controversial issue. Some companies have cross-functional management committees to vet issues on a case-by-case basis to determine when speech is appropriate.

Directors and business leaders we spoke with identified a number of criteria or considerations for determining whether or not the CEO should speak out on highly charged social and political issues:

- Is the issue relevant to the company and its strategy? Is it in alignment with the company's culture, values, and purpose?
- How will speaking out resonate with the company's employees, investors, customers, and other stakeholders? In a tight labor market, employees often choose where to work based on company values, including its willingness to speak out on certain issues, such as DEI.
- *Not* speaking out can be as powerful as speaking out on certain issues. How do the CEO and the board come to terms with that ambiguity and risk and weigh the consequences of speaking out or not?
- As the views of stakeholders are not uniform, how should CEOs and companies manage the inevitable criticism of their choice to speak or not speak? Having felt the backlash of speaking out on social/political issues, some companies have adjusted their approach to take action without trumpeting what they're doing.
- Make sure that the company's lobbying and political contributions are aligned with its speech.



Approach cybersecurity, data privacy, and AI holistically as data governance.

Cybersecurity threats are dynamic and related impacts continue to intensify. The acceleration of AI and digital strategies, the increasing sophistication of hacking and ransomware attacks, and the lack of definition for lines of responsibility—among users, companies, vendors, and government agencies—have elevated cybersecurity risk and its place on board and committee agendas.

Boards have made strides in monitoring management's cybersecurity effectiveness. For example, some have greater cybersecurity expertise on the board and relevant committees (although that expertise is in short supply). Other efforts include company and business-line-specific dashboard reporting to highlight and prioritize critical risks, vulnerabilities, and threats; war-gaming breach and response scenarios; and discussions with management on the findings of ongoing third-party risk assessments of the company's cybersecurity program. Despite these efforts, the growing sophistication of cyberattacks and the complexity of cyber risk management point to the continued challenges ahead.

These issues, and frequent failures to address concerns, have pushed regulatory bodies into action. Board should monitor developments in the SEC's proposal on Cybersecurity Risk Management, Strategy, Governance, and Incident Disclosure as well as management's preparations to comply. The SEC rule proposal would, among other things, establish a four-business-day deadline for reporting a material

© 2022 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved. The KPMG name and logo are trademarks used under license by the independent member firms of the KPMG global organization. NDP382757-1A

cyber breach (before relevant information may be available), would *not* allow for delayed reporting for incidents subject to law enforcement or national security investigations, and would require disclosure of any cybersecurity expertise on the board. Final SEC action on the proposed rule is expected in the spring of 2023.

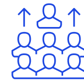
While data governance overlaps with cybersecurity, it's broader and includes compliance with industry-specific privacy laws and regulations as well as privacy laws and regulations that govern how personal data—from customers, employees, or vendors—is processed, stored, collected, used, shared, and disposed. Data governance also includes 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 what data is being collected, how it is stored, managed, and used, and who and how decisions are made regarding these issues.
- Clarify which business leaders are responsible for data governance across the enterprise—including the roles of the chief product officer, chief information officer, chief information security officer, chief data officer, and chief compliance officer.
- Reassess how the board—through its committee structure—assigns and coordinates oversight responsibility for the company's cybersecurity and data governance frameworks, including privacy, ethics, and hygiene.

An increasingly critical area of data governance is the company's use of AI to analyze data as part of the company's decision-making process. Boards should understand the process for how AI is developed and deployed. What are the most critical AI systems and processes the company has deployed? To what extent is bias—conscious or unconscious—built into the strategy, development, algorithms, deployment, and outcomes of AI-enabled processes? What regulatory compliance and reputational risks are posed by the company's use of AI, particularly given the global regulatory focus on the need for corporate governance processes to address AI-related risks, such as bias and privacy? How is management mitigating these risks?

Many directors may be uncomfortable with responsibility for overseeing AI risk because of a lack of expertise. But, as observed by Debevoise & Plimpton: "As the SEC has made clear with respect to cybersecurity, boards need to find a way to exercise their supervision obligations, even in areas that are technical, if those areas present enterprise risk, which is already true for AI at some companies. That does not mean that directors must become AI experts or that they should be involved in day-to-day AI operations or risk management. But directors at companies with significant AI programs should consider how they will ensure effective board-level oversight with respect to the growing opportunities and risks presented by AI."[2]



Make talent, HCM, and CEO succession a priority.

Most companies have long said that their employees are their most valuable asset. COVID-19; the difficulty of finding, developing, and retaining talent in the current environment; and an increasingly knowledge-based economy have highlighted the importance of talent and HCM—and changed the employer/employee dynamic. This phenomenon of employee empowerment has prompted many companies and boards to rethink the employee value proposition.

While the most dramatic change in the employee value proposition took place during the pandemic, employee empowerment hasn't abated, and employees are demanding fair pay and benefits; work-life balance, including flexibility; interesting work; and an opportunity to advance. They also want to work for a company whose values—including commitment to DEI and a range of ESG issues—align with their own.

In 2023, we expect continued scrutiny of how companies are adjusting their talent development strategies to meet the challenge of finding, developing, and retaining talent amid a labor-constrained market. 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? What are the challenges in keeping key 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 DEI at all levels? As millennials

[2] Avi Gesser, Bill Regner, and Anna Gressel, "AI Oversight Is Becoming a Board Issue," Debevoise & Plimpton LLP via HLS Forum on Corporate Governance, April 26, 2022.

© 2022 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved. The KPMG name and logo are trademarks used under license by the independent member firms of the KPMG global organization. NDP382757-1A

and younger employees 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?

In addition to monitoring SEC and global rulemaking developments, boards should discuss with management the company's HCM disclosures in the 2022 10-K—including management's processes for developing related metrics and controls ensuring data quality—to help ensure that the disclosures demonstrate the company's commitment to critical HCM issues. HCM will likely be a major area of focus during the 2023 proxy season, given the high level of investor interest in the issue.

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 help 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, ongoing process, and the board should always be focused on developing a pipeline of C-suite and potential CEO candidates. Succession planning should start the day a new CEO is named.

How robust are the board's succession planning processes and activities? Has the succession plan been updated to reflect the CEO skills and experience necessary to execute against the company's long-term strategy? In many cases, those strategies have changed over the last two years. 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?

Engage proactively with shareholders, activists, and other stakeholders.

Two SEC developments will be important areas of board focus in upcoming shareholder and stakeholder engagements. Ahead of the 2023 proxy season, the SEC adopted a "pay versus performance rule" that requires detailed new disclosures in proxies and information statements for fiscal years ending on or after December 16, 2022. The SEC's universal proxy rules, which require the use of "universal" proxy cards in all director election contests, are already effective. The threat of universal proxy can serve as an important lever, encouraging greater focus on the skills and experience of individual directors and making it easier to launch a proxy fight.

Given the intense investor and stakeholder focus on executive pay and director performance, as well as climate risk, ESG, and DEI, particularly in the context of long-term value creation, engagement with shareholders *and* stakeholders must remain a priority. Institutional investors and stakeholders are increasingly holding boards accountable for company performance and are continuing to demand greater transparency, including direct engagement with independent directors on big-picture issues like strategy, ESG, and compensation. 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.

The board should request periodic updates from management about the company's engagement activities:

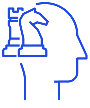
- Does the company know, engage with, and understand the priorities of its largest shareholders and key stakeholders?
- Are the right people engaging with these shareholders and stakeholders—and how is the investor relations (IR) role changing?
- What is the board's position on meeting with investors and stakeholders? Which independent directors should be involved?

In short: Is the company providing investors and 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.

As reflected in 2022 proxy voting trends, strategy, executive compensation, management performance, climate risk, other ESG initiatives, DEI, HCM, and board composition and performance will remain squarely on investors' radar during the 2023 proxy 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 2023.

Having an "activist mindset" is as important as ever—particularly given the convergence of ESG and more traditional hedge fund activism as well as the universal proxy rules, which will enable activists to use the universal proxy card to gain leverage in their negotiations with boards.

© 2022 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved. The KPMG name and logo are trademarks used under license by the independent member firms of the KPMG global organization. NDP382757-1A



Think strategically about talent, expertise, and diversity in the boardroom.

Boards, investors, regulators, and other stakeholders are increasingly focused on the alignment of board composition—particularly director expertise and diversity—with the company's strategy.

Indeed, the increased level of investor engagement on this issue points to the central challenge with board composition: Having directors with experience in key functional areas critical to the business while also having deep industry experience and an understanding of the company's strategy and the risks to the strategy. It is important to recognize that many boards will not have "experts" in all the functional areas such as cybersecurity, climate, HCM, etc., and may need to engage outside experts.

Developing and maintaining a high-performing board that adds value requires a proactive approach to board-building and diversity—of skills, experience, thinking, gender, and race/ethnicity. While determining the company's current and future needs is the starting point for board composition, there is a broad range of board composition issues that require board focus and leadership—including succession planning for directors as well as board leaders (the lead director and committee chairs), director recruitment, director tenure, diversity, board and individual director evaluations, and removal of underperforming directors. Boards need to "tell their story" about the composition, skill sets, leadership, and functioning of the board and its committees.

Boards have made progress on diversity, but change has been slow. According to Spencer Stuart's 2022 S&P 500 Board Diversity Snapshot, 46% of the new directors added during the 2022 proxy season are Black/African American, Hispanic/Latino/a, Asian, American Indian/Native Alaskan, and multiracial directors, largely driven by an increase in the recruitment of Black/African American directors. And 46% of new directors are women. However, due to low boardroom turnover, the addition of new directors from underrepresented groups has had little impact on the overall diversity of S&P 500 boards. Just 22% of all S&P 500 directors in 2022 are from these underrepresented groups. And women now represent 32% of all S&P 500 directors.[3]

Board composition, diversity, and renewal should remain a key area of board focus in 2023, as a topic for communications with the company's institutional investors and other stakeholders, enhanced disclosure in the company's proxy, and most fundamentally positioning the board strategically for the future.

[3] Spencer Stuart, 2022 S&P 500 Board Diversity Snapshot, June 2022.

© 2022 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved. The KPMG name and logo are trademarks used under license by the independent member firms of the KPMG global organization. NDP382757-1A

Contact us

John H. Rodi
Leader, KPMG Board Leadership Center

Stephen Dabney
Leader, KPMG Audit Committee Institute

Claudia Allen
Senior Advisor, KPMG Board Leadership Center

Susan Angele
Senior Advisor, KPMG Board Leadership Center

Annalisa Barrett
Senior Advisor, KPMG Board Leadership Center

Stephen Brown
Senior Advisor, KPMG Board Leadership Center

Patrick Lee
Senior Advisor, KPMG Board Leadership Center

About the KPMG Board Leadership Center

The KPMG Board Leadership Center (BLC) champions outstanding corporate governance to drive long-term value and enhance stakeholder confidence. Through an array of insights, perspectives, and programs, the BLC—which includes the KPMG Audit Committee Institute and close collaboration with other leading director organizations—promotes continuous education and improvement of public and private company governance. BLC engages with directors and business leaders on the critical issues driving board agendas—from strategy, risk, talent, and ESG to data governance, audit quality, proxy trends, and more. Learn more at kpmg.com/us/blc.

About the KPMG Audit Committee Institute

As part of the KPMG Board Leadership Center, the ACI provides audit committee and board members with practical insights, resources, and peer-exchange opportunities focused on strengthening oversight of financial reporting and audit quality, and the array of challenges facing boards and businesses today—from risk management and emerging technologies to strategy, talent, and global compliance. Learn more about ACI at kpmg.com/us/aci.

Some or all of the services described herein may not be permissible for KPMG audit clients and their affiliates or related entities.

kpmg.com/socialmedia

The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavor to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act upon such information without appropriate professional advice after a thorough examination of the particular situation.

© 2022 KPMG LLP, a Delaware limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved. The KPMG name and logo are trademarks used under license by the independent member firms of the KPMG global organization. NDP382757-1A