

On the 2017 board agenda

Audit Committee Institute

In 2017, corporate growth and shareholder return will still require the essentials - managing key risks, innovating and capitalising on new opportunities, and executing on strategy. But the context for corporate performance is changing quickly - and perhaps profoundly - as advances in technology, business model disruption, heightened expectations of investors and other stakeholders, and global volatility and political shifts force companies and their boards to rethink what it will take to stay competitive in the long term, and what it means to be a corporate leader. Drawing on insights from our recent ACI pulse surveys and interactions with directors and business leaders over the past 12 months, we have highlighted seven items that, in our opinion, boards should keep in mind as they help guide the company forward in the year ahead:

Recognise that connecting and calibrating strategy and risk is more important - and more challenging - than ever.

What a difference a few months can make! The EU Referendum and the US Election - which caught many observers and corporate strategies flat-footed - will have major implications for global markets, and the geopolitical landscape at large.

That so few had predicted these sea changes despite exhaustive analysis in the run-up to both events is a stark reminder to businesses of how marketplace signals can be fundamentally missed (be it *status quo* thinking, bias toward the familiar, or comfortable complacency) and the playing field fundamentally altered overnight. The policy landscape will become clearer, but expect the competitive landscape to remain dynamic and opaque, leaving little lead time.

Technology advances and relentless innovation, business model disruption, the emergence of Millennials and other demographic shifts, evolving customer demands and employee expectations, and more, will put a premium on corporate agility and the ability to pivot as conditions change. Think about constant transformation, talent risk management and the opportunities afforded by 'new' technology. Does management have an effective process to monitor changes in the external environment and test the continuing validity of strategic and risk assumptions? Does this process provide early warning that adjustments may be necessary? Does the board have the right people and perspectives to make the necessary linkages between external forces and the company's strategy and risk profile? Make strategy an ongoing discussion (versus an annual 'decision') that incorporates smart risk-taking and robust scenario planning with plenty of what-if's on the table. In short, 'strategy and risk' should be hardwired together and built into every boardroom discussion.

Develop and execute the strategy based on total impact.

As noted at the outset, the context for corporate performance is changing, and consideration of the corporation's role in society is moving from the periphery to the centre of corporate thinking. Investors, customers, employees, and other stakeholders are sharpening their focus on how companies approach social and environmental issues; and companies are increasingly recognising that societal issues - from sustainability of natural resources to a more diverse talent pool - have real implications for the company's long-term performance, strategy and risk profile. What steps is the company taking to address any negative environmental or social impacts that it is creating or causing? Are there environmental and sustainability-related opportunities that would help drive the company's long-term performance? Are the company's environmental and sustainability activities (both results and ongoing efforts) effectively communicated to its stakeholders?

Take a hard look at the board's composition: Is the talent in the boardroom aligned with the company's strategy and future needs?

Given the demands of today's business and risk environment (and increasing scrutiny by investors, regulators, and the media) aligning boardroom talent with company strategy - both for the short-term and the long-term as the strategy evolves - should be a priority. Not surprisingly, 43 percent of respondents in our recent pulse survey, [Building a great board](#), cited 'resistance to change' and 'status-quo thinking' as hampering their board-building efforts. Make time to read the FRC Feedback Statement, ["UK Board Succession Planning Discussion Paper"](#) and the WCD/KPMG report, ["Seeing Far and Seeing Wide: Moving Toward a Visionary Board"](#).

As recommended in these reports, directors should focus squarely on board composition/diversity and succession planning, robust evaluations, tenure limits, director recruitment and on-boarding, board leadership, stakeholder communications, and continuing director education - all tailored to the company and industry. In short, periodic board refreshment should give way to robust, continual improvement and active board succession planning.

Reassess the company's crisis prevention and readiness efforts. Crisis prevention and readiness has taken on increased importance and urgency for boards and management teams, as the list of crises that companies have found themselves facing in recent years looms large. Crisis prevention goes hand-in-hand with good risk management - identifying and anticipating risks, and putting in place a system of controls to help prevent such risk events and mitigate their impact should they occur. We are clearly seeing an increased focus by boards on key operational risks across the extended global organisation, e.g. supply chain and outsourcing risks, IT and data security risks, etc. Do we understand the company's critical operational risks? What has changed in the operating environment? Has the company experienced any control failures? Is management sensitive to early warning signs regarding safety, product quality and compliance? Of course, even the best-prepared companies will experience a crisis; but companies that respond quickly and effectively - including robust communications - tend to weather a crisis better. Assess how well the company's crisis planning aligns with its risk profile, how frequently the plan is refreshed, and the extent to which management, and the board, conduct mock crisis exercises. Do we have communications protocols in place to keep the board apprised of events and the company's response?

Pay particular attention to potential risks posed by tone at the top, culture, and incentives. A robust risk management process is essential to help prevent and mitigate risk events to acceptable levels. As we have seen in recent years, many of the crises that have presented the most damage to companies - financial, reputation, and legal - have been caused by a breakdown in the organisation's tone at the top, culture, and incentives. As a result, boards need to pay particular attention to these capital 'R' risks, which may pose the greatest risk of all to the company. In today's business environment, it is more important than ever that the board be acutely sensitive to the tone from (and example set by) leadership, and to reinforce the culture of the organisation, i.e., what the company does, how it does it, and the culture of compliance, including a commitment to management of the company's key risks.

Reassess the company's shareholder engagement programme. Shareholder engagement is rapidly becoming a priority for companies as institutional investors increasingly hold boards accountable for company performance and demand greater transparency, including direct engagement with independent directors. Institutional investors expect to

engage with portfolio companies - especially when investors have governance concerns or where engagement is needed to make a more fully informed investment and/or voting decisions. In some cases, investors are calling for engagement with independent directors. As a result, boards should periodically obtain updates from management about its engagement practices: Do we know and engage with our largest shareholders and understand their priorities? Do we have the right people on the engagement team? What is the board's position on meeting with investors? Which of the independent directors should be involved? Strategy, executive compensation, management performance, environmental and sustainability initiatives, and board composition and performance are likely to be on investors' radar.

Refine and widen boardroom discussions about cyber risk and security. Despite the intensifying focus on cyber security, the cyber risk landscape remains fluid and opaque, even as expectations rise for more engaged oversight. As the cyber landscape evolves, board oversight, and the nature of the conversation, must continue to evolve. Discussions are shifting from prevention to an emphasis on detection and containment, and increasingly focused on the company's 'adjacencies' which can serve as entry points for hackers. The Internet of Things and the digital records that surround people, organisations, processes, and products ('code halos') call for deeper - if not wholly different - conversations. The board should help elevate the company's cyber risk mind-set to an enterprise level, encompassing key business leaders, and help ensure that cyber risk is managed as a business or enterprise risk - not simply an IT risk. Do discussions about M&A, product development, expansion into new geographies, and relationships with suppliers, customers, partners, advisers, and other third parties factor in cyber risk? Help ensure that awareness of, and accountability for, cyber security permeates the organisation, with a security mind-set, proper training, and preparation for incident response. Is cyber security risk given regular and adequate time on the board's agenda? Does the board need a separate committee to focus on it? Where are the company's biggest vulnerabilities and how is it protecting its most critical data sets? Do we benchmark against others in the industry? Do we have a cyber security scorecard and a robust cyber incident response plan? Do directors work under the assumption that any email could become public at any time?

Also see KPMG's '[On the 2017 audit committee agenda](https://www.kpmg.co.uk/aci)' at [kpmg.co.uk/aci](https://www.kpmg.co.uk/aci).

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