

# Four ways to advance risk oversight



Building a better  
working world

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# Four ways to advance risk oversight

The unprecedented scale and pace of disruption in the market today requires a new way of thinking about risk and transformation. Technological advances are blurring industry lines and changing the nature of work. Changing social demographics and an accelerating climate crisis are calling into question how, and for whom, businesses create value. These and other developments, from cybersecurity threats to a volatile geopolitical landscape and pandemics, are putting pressure on organizations to build risk resiliency and create long-term value while sustaining trust across stakeholders – consumers, investors, regulators, employees and third parties.

Embracing the upside of risk and sustaining stakeholder loyalty and trust is fundamental to achieving competitive market advantage in this era of disruption. According to the Embankment Project for Inclusive Capital (EPIC), as little as 20% of a company's value is now captured on its balance sheet – “a staggering decline” from about 83% in 1975 – as real value today is in innovation, culture, corporate governance and trust.<sup>1</sup>

Today's level of transformation, both within organizations and across global economies, coupled with the uncertain economic environment, requires risk management to be more dynamic. This calls for a new risk mindset that moves from a focus on traditional downside risks to embracing the upside of risk and weaving trust into all facets of the

business. At the board level, this translates to adopting a future-fit risk approach that is more attuned to external business trends and one that allows management to focus on identifying and capitalizing on risks that enhance trust and enable innovation, speed and value creation.

We surveyed 500 global board members and CEOs to better understand their perspectives on today's top risks and what resources they need to better execute risk oversight while sustaining trust in today's business climate. We learned that whether it be in relation to reporting, skill sets or the sheer time spent discussing risk, board members acknowledge their organizations – and boards themselves – need to evolve to keep pace with disruption and maintain their strategic advantage. To operate in these market conditions, our risk survey indicates that boards can advance their oversight of risk in the following four ways, which will require enhancements to enterprise risk management, insightful risk reporting and new remits between boards and CEOs:

- 1. Reprioritize top risks to keep pace with market disruption**
- 2. Turn risk into strategic value**
- 3. Redefine risk reporting to reflect the dynamic risk landscape**
- 4. Evolve the board's role in enterprise risk management (ERM)**

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1. Embankment Project for Inclusive Capitalism report, which brought together more than 30 global capital market leaders to identify and create new metrics to demonstrate long-term value to financial markets, available at: <https://www.epic-value.com/>

## How we see it – the importance of building risk resiliency

The findings in this report are based on surveys conducted prior to the coronavirus (COVID-19) outbreak, which at the time of publication continues to spread globally and has brought increased disruption and uncertainty to businesses and economies. Declared a global emergency by the World Health Organization, COVID-19 has rapidly emerged as a critical outside risk for businesses. Many companies are experiencing vulnerabilities related to quarantined workers/travel restrictions, significant fluctuations in product demand and heavy supply chain disruption from the affected areas. The scope of risks continues to expand and has highlighted critical global interdependencies and the need for heightened crisis management planning, including the ability to quickly execute business continuity plans and deploy a rapid response to mitigate related risks, including medical and security protocols.

Unpredictable events, such as the spread of COVID-19, reinforce our survey findings around the importance of having a robust ERM program and well-honed crisis management plans. While companies cannot predict when a crisis or black swan event may occur, boards that prepare organizations to have the strategic, operational and financial resiliency to recover from emerging global risks will be better positioned to respond and minimize their impact.



# Reprioritize top risks to keep pace with market disruption

As market disruption and changing stakeholder expectations rewrite the risk landscape, board oversight priorities need to keep pace. Our survey uncovered today's top risks from the board and CEO perspective, revealing a need for stronger alignment and more rigorous oversight of key emerging risks.

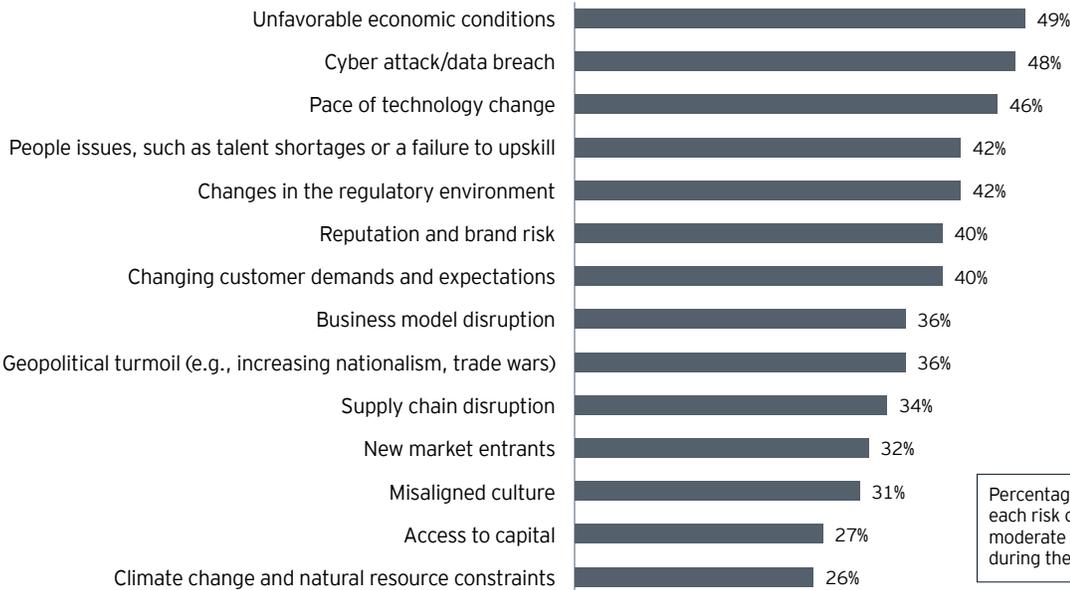


**Today's top risks from the board perspective: economic headwinds, cyber attacks and technology disruption**

Economic cycles are inevitable, with the question being not if, but when and how severe, the next financial downturn will be – and never before have economic signals and indicators been more confusing. Nearly half of board members believe unfavorable economic conditions will have more than a moderate impact on their business in the next 12 months, making it the most important risk category.

Some of those unfavorable economic conditions may result from growing geopolitical risks that are felt acutely in the US. While all surveyed board members rank geopolitical turmoil as the ninth most important risk, those that sit on boards of US companies rank it as their joint-second (along with people issues) most important risk (vs. 36% of board members in Europe, the Middle East and Africa (EMEA) and 29% of board members in Asia-Pacific).

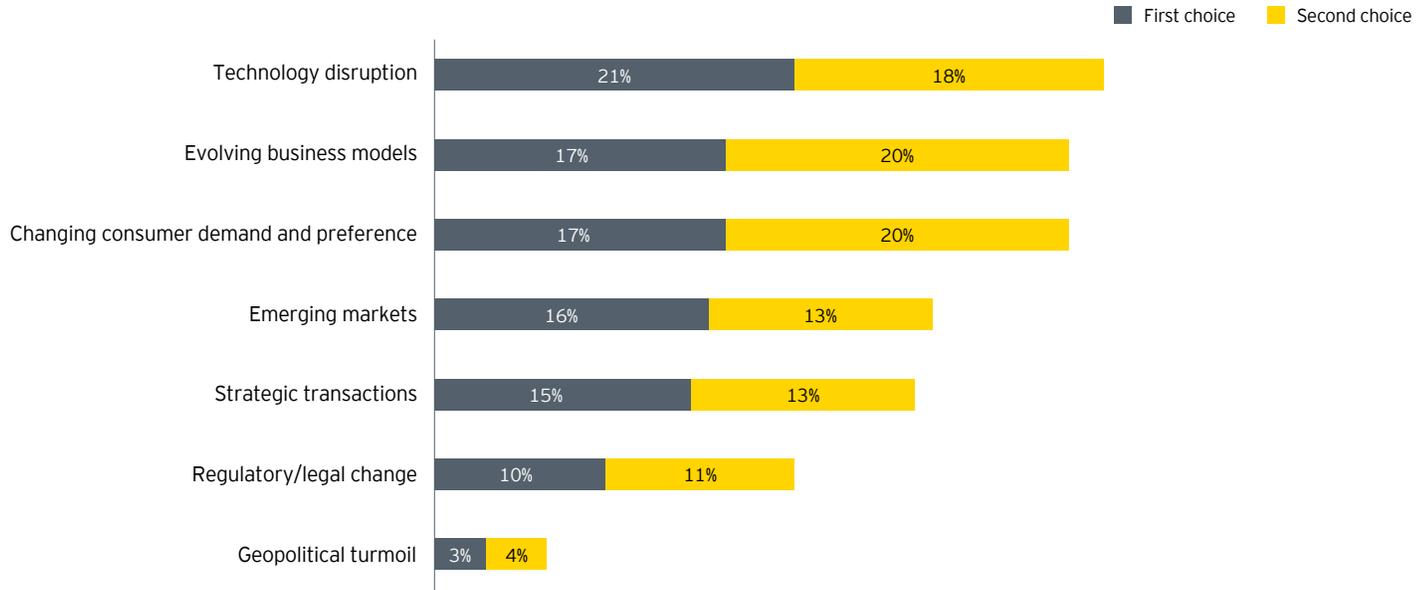
**Risks that will most impact businesses in the next 12 months**



Percentages relate to those that believe each risk category will have more than a moderate impact on their organization during the next 12 months.

How significantly do you expect the following risks to impact your organization during the next 12 months?

## Technology disruption represents the greatest strategic opportunity



Which of the following areas represent the greatest strategic opportunities for your organization?

Cyber attacks/data breaches and the pace of technology change also appear to be creating a complex set of pressures for boards. Forty-eight percent of board members overall (and 69% of board members of financial services companies) believe cyber attacks/data breaches will more than moderately impact their business over the next 12 months, and 46% believe the same for the pace of technology changes. Of course, these risks go hand in hand.

Organizations today must harness technological innovations to survive as well as to self-disrupt and transform, which board members clearly acknowledge. Nearly 40% of them rank technology disruption among the greatest strategic opportunities for their organizations. At the same time, introducing new technologies also introduces new cyber and data privacy vulnerabilities, creating an increasingly complex cybersecurity landscape.

The reason why cybersecurity risk is ranked as one of the top risks may be due in part to board members lacking confidence in their organizations' cyber attack mitigation

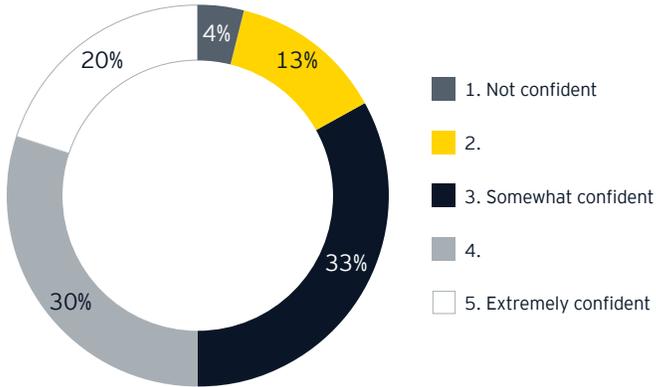
measures. Half of board members say they are, at best, somewhat confident that the cybersecurity risks and mitigation measures presented to them can protect the organization from major cyber attacks.

In our *2020 Global Information Security Survey (GISS)* report, 25% of respondents say they can quantify,<sup>2</sup> in financial terms, the effectiveness of their cybersecurity spending in addressing the risks faced by the business, and only 7% of security leaders are able to financially quantify the impact of breaches.

Around 40% of board members say that cybersecurity is not a regular discussion item on their full board agenda, revealing an opportunity for many boards to strengthen oversight of this existential threat. Many CISOs are concerned that their boards do not have a structured way to review cyber risk. This could be a symptom of the way the function chooses to communicate with the board – the emphasis is typically on current-state security and audit results rather than performance or innovation.

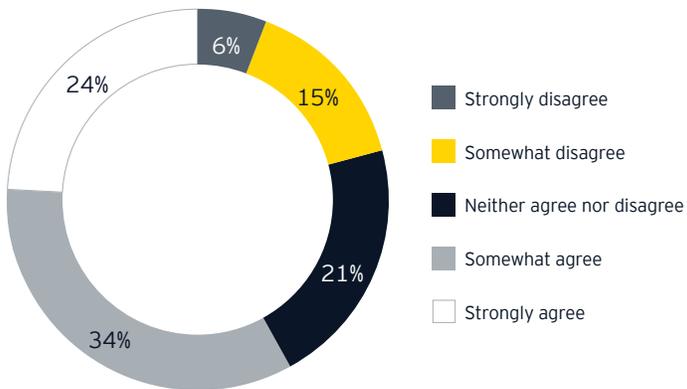
2. See the EY report *2020 Global Information Security Survey*, [https://www.ey.com/en\\_us/giss](https://www.ey.com/en_us/giss)

**Boards lack confidence in their organizations' cyber attack mitigation measures**

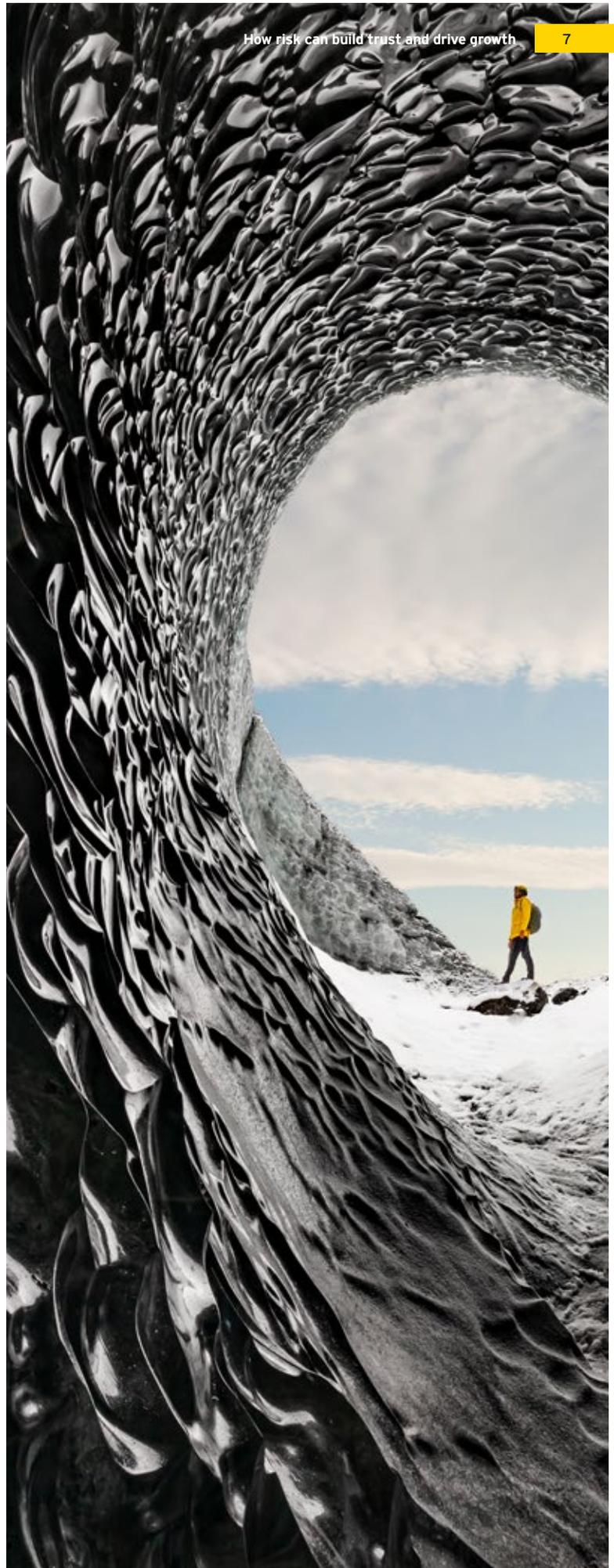


How confident are you that the cybersecurity risks and mitigation measures presented to you can protect the organization from major cyber attacks? (Please answer on a scale of 1 to 5, where 1 is not confident, 3 is somewhat confident and 5 is extremely confident.)

**Cybersecurity is not a regular discussion item on a large minority of full board agendas**



To what extent do you agree with the following statement: Cybersecurity risk is a regular discussion item on the full board agenda.





## People issues, supply chain disruption and geopolitical turmoil are top-of-mind issues for CEOs, revealing the need for better alignment with board risk priorities

In contrast to non-executive directors (NEDs), CEOs are more concerned about people issues, such as talent shortages or a failure to upskill, supply chain disruption and geopolitical turmoil.

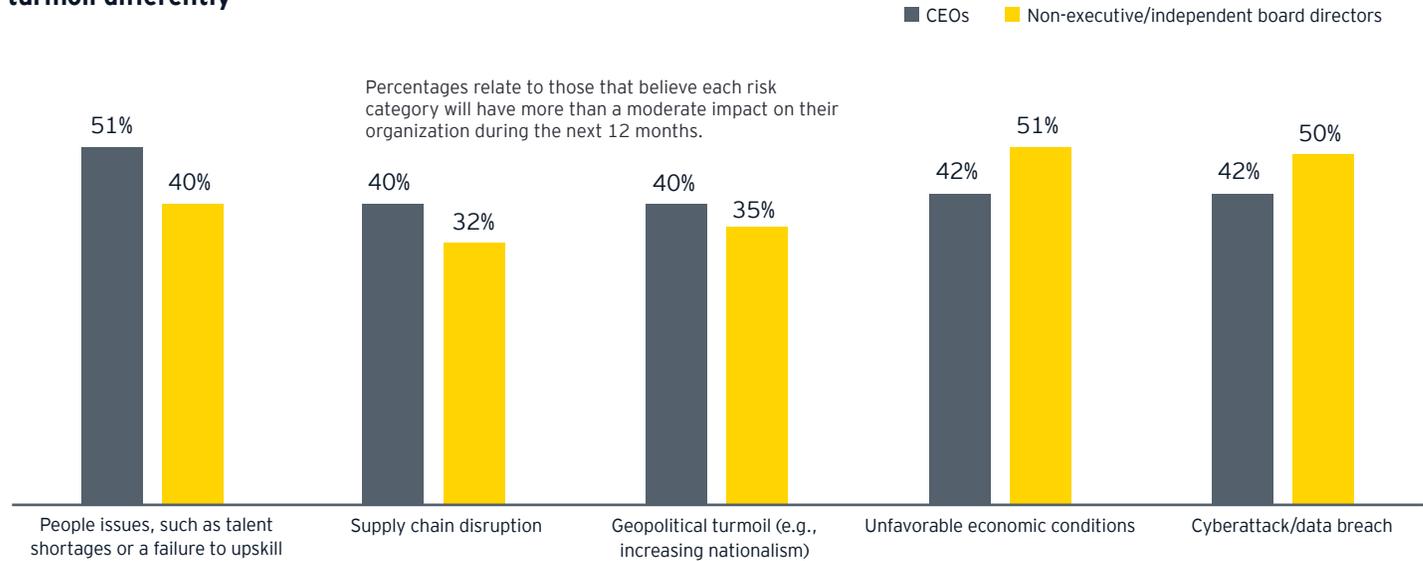
CEOs understand that when it comes to growth and innovation, the risks and rewards associated with an organization's talent may be the most critical area of all. From building a culture where innovation thrives, to defining the company's purpose, to investing in retraining workers to meet the demands of evolving business models, a company's people strategy is increasingly emerging as critical to competitive strength and long-term value creation.

Most CEOs believe people issues will have more than a moderate impact on their organization during the next 12 months vs. just 40% of directors. This difference may stem from the two groups' different experiences and traditional areas of focus. For example, talent continues to gain momentum in the boardroom as human capital and culture comprise a growing share of market value and are recognized as key strategic enablers and competitive differentiators in today's information age.

Traditionally, boards focused on talent development and succession planning for the C-suite without the deeper view into talent risks and opportunities across the workforce. The overlapping nature of so many of these risks may also complicate insights into how the two are ranking different risks. For example, people issues are closely linked to the pace of technology change, because the need to upskill, retain and recruit top talent is critical to drive technological transformation in today's business environment.

Forty percent of CEOs ranked both supply chain disruption and geopolitical turmoil as significant risks that will moderately impact their organizations in the coming year vs. only approximately a third of NEDs. Rising channel complexity, increasing volatility and the growth of emerging markets require new levels of agility and responsiveness, while pressure on costs and overcapacity drive the need for increased efficiency. These pressures are also driving CEOs

## CEOs and NEDs prioritize the importance of people issues, supply chain disruption and geopolitical turmoil differently



How significantly do you expect the following risks to impact your organization during the next 12 months?

and organizations to reinvent supply chains to drive more competitive advantage while also introducing new risks (such as additional cybersecurity-related risks from digitized smart factories or robotic process automation) to the organization.

Geopolitical pressures are also growing increasingly complex and volatile, introducing new and evolving risks (including supply chain disruption) to strategy and operations that CEOs must navigate. The impact of some of the related risks is often diffused and hard to discern, such as the changing roles of China, Russia and the US, or the rise of populism across democracies. Others are more palpable, such as trade wars, nation-state cyber warfare or the impact of Brexit. In today's changing geopolitical environment, risks need consistent monitoring and dynamic incorporation into strategy and operations.

Whatever nuances are shaping the gap between directors' and CEOs' risk priorities, it is critical that boards and executive leadership achieve alignment on the risks considered most material to the business over the short and long terms. Misalignment and the lack of a clear, united tone from the top on risk priorities can lead to mismanaged risks and expose the organization to more vulnerabilities.

## Why culture and climate risk warrant more rigorous oversight

Only around a quarter of board members believe climate change and natural resource constraints will have more than a moderate impact on their organization during the next 12 months, making it the lowest priority on the board's risk agenda. Misaligned culture came in only slightly higher, with 31% of board members viewing it as a significant near-term risk. Board members' perception of the impact of these risks was low but may likely shift, particularly given the increasing focus on these risks by shareholders and other key stakeholders.

With the manifestation of physical climate risks accelerating at a rapid rate, many investors recognize it as a key threat. For example, in the EY investor outreach leading up to the 2020 proxy season, which included conversations with more than 60 institutional investors representing more than US\$35 trillion in assets under management, around half of the investors identified environmental issues and climate risk as among the biggest threats to their portfolio companies' strategic success in the next three to five years, making it the second biggest threat identified. Climate risk also

emerged as the top investor engagement priority for 2020, with almost 60% of investors telling us they will engage companies on climate risk this year.

In his 2020 letter to CEOs, BlackRock chairman and CEO Larry Fink put climate change front and center, noting that it has become “a defining factor in companies’ long-term prospects” and shared his belief that “we are on the edge of a fundamental reshaping of finance” as we better understand the impacts climate risk will have on the physical world and global financial markets. As BlackRock seeks to make sustainability integral to its portfolio construction, a company’s demonstration of how it is managing climate risk and accelerating the transition to a low-carbon economy may inform its access to capital. And it is not just shareholders that care about a company’s approach to climate risk. More than ever, consumers and employees seek to support companies creating long-term environmental value, and climate change is rising on public and political agendas.

Culture is similarly an increasing area of focus for investors and other stakeholders. Nearly 40% of the investors we spoke with in our outreach identified corporate culture as a key enabler of strategic success, making it the third-highest factor identified. Talent management ranked as the highest strategic enabler, and many of the investors spoke about culture and talent management in tandem, stressing that the right culture is needed to attract, engage, motivate and retain the right talent. This investor focus reflects broader recognition that culture is critical to achieving the level of transformation needed in today’s market. Further, culture is the foundation for behaviors that support appropriate, balanced and informed risk-taking and, where necessary, escalation.

While there may be reasonable explanations for climate risk and misaligned culture appearing to be lower on the boards’ risk agenda (e.g., the question specified a 12-month time frame, and boards may consider these to be longer-term risks), how companies manage and govern these risks and seize related opportunities are coming under increasing scrutiny from key stakeholders. Boards should deepen their understanding of the fast-evolving significance of these factors to investors, employees, customers and other key stakeholders and set the tone at the top for addressing and prioritizing these risks accordingly.





**Key board takeaways:**

## Reprioritize top risks to keep pace with market disruption

- ▶ **Address today's top threats and align on the top risks.** Make sure your board and the organization have the skills and competencies needed to oversee today's most pressing risks. Align with management to create a dedicated and dynamic focus on emerging risks given the faster pace of change today.
- ▶ **Listen to stakeholders.** Consider the views of and engage with key stakeholders, including shareholders, to broaden the board's perspective on risk.
- ▶ **Analyze megatrends and outside data sources to develop an informed point of view on the risk landscape.** The board should verify that the organization is incorporating both internal and external data points in its risk identification process as well as continuously monitoring risks and trends for any material changes.
- ▶ **Develop a strong pulse on culture.** Oversee how culture is defined and aligned to strategy, assign responsibility and accountability for culture, monitor internal culture metrics and constructively challenge the culture of the board itself.
- ▶ **Maintain robust cybersecurity risk oversight.** Challenge whether sufficient time is spent discussing cybersecurity and data privacy risks and consider whether business model and cyber vulnerabilities necessitate additional oversight measures, such as leveraging outside cybersecurity experts to fill knowledge gaps or reevaluating the board's committee structure so that appropriate time and focus is given to cybersecurity risk.
- ▶ **Prioritize oversight of climate and sustainability risk management.** Understand the company's exposure to climate impacts, how it is strategically addressing related risks, and how it is positioning itself for long-term sustainability and success in a carbon-constrained environment.

# Turn risk into strategic value

Risk is no longer viewed as just “downside” as leading companies recognize that focusing on achieving performance management goals and strategic objectives requires looking at the “upside” opportunities that risks can provide.



The transformation of ERM to be more future-fit turns risk into strategic advantage by evaluating the impact to stakeholder trust and aligning the risk response to focus on the achievement of strategic goals and performance objectives. Our survey uncovered opportunities for boards to adjust risk appetite to be more flexible with market changes and the overall business context. Other opportunities include challenging ERM's effectiveness in identifying emerging risks and enhancing risk resiliency to adverse risk events through crisis planning. In doing so, boards can help enable companies to respond to sudden, unpredictable changes with agility and confidence that derives strategic value.

### Boards seek to improve how they adjust risk appetite in response to the changing risk landscape

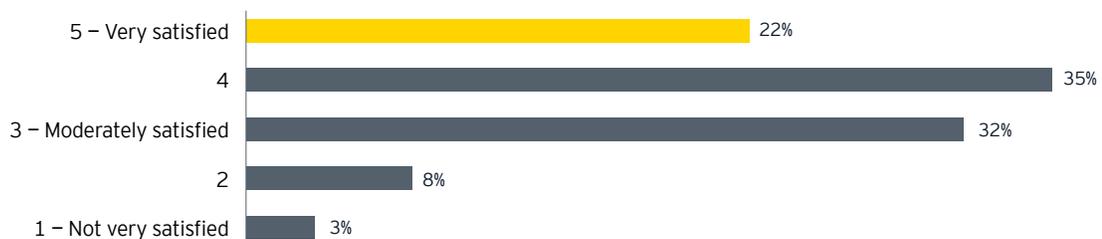
Our survey found that board members are thinking strategically about risk but seek to improve how they adjust their organization's risk appetite in response to the changing landscape. While 73% of board members state that their organization's strategy is aligned with its risk appetite, and 64% state that their board spends enough time discussing risks that could provide a strategic upside to the organization, just 22% of board members are very satisfied with their effectiveness in overseeing changes

to the risk landscape and adjusting the organization's risk appetite accordingly. Boards can enhance their effectiveness in this area by better leveraging external data sources in risk identification and improved monitoring of risk responses.

There is tremendous opportunity for organizations to realize true value from effective risk-taking through defining, managing and measuring risk appetite. In today's business environment, where risk drivers can emerge and evolve quickly, it is critical that boards and executive teams consider a more fluid view to risk appetite, recognizing that it will continue to shift over time and require constant monitoring.

Organizations should conduct enterprise-wide risk assessments that consider upside, downside and outside<sup>3</sup> risk on a continuous basis to help focus and recalibrate on the key risks. Boards should verify that these dynamic risk assessments take a holistic view across the risk categories and are organized to evaluate the impact on stakeholder trust and the organization's strategy. Conducting risk assessments on a more continuous basis can enable timely identification of changes to an organization's risk profile, allowing organizations to better adjust their risk appetite, and change controls and audit plans to better address shifting market and regulatory developments, such as the impacts of technology disruption, changes in customer sentiment and evolving geopolitical and regulatory issues.

### Less than a quarter of boards are very satisfied with their effectiveness in adjusting their organization's risk appetite in response to changes in the risk landscape



How satisfied are you with your board's effectiveness in overseeing changes to the risk landscape and adjusting the organization's risk appetite accordingly? (Please rank on a scale of 1 to 5 where 1 is not very satisfied, 3 is moderately satisfied and 5 is very satisfied.)

3. See the EY article *How trust by design is the new CEO imperative for further discussions on upside, downside and outside risks*.

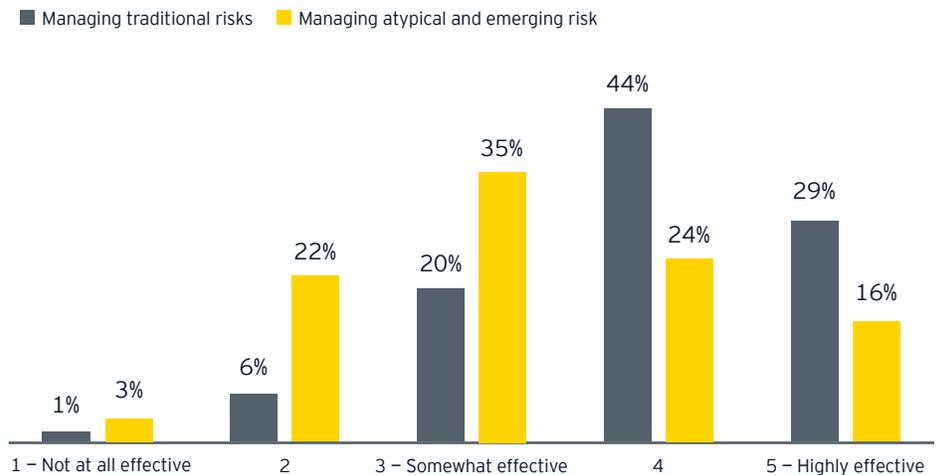
## Boards want improved management of emerging risks, but talent gaps are creating challenges

While boards generally say that ERM at their organization is effective in managing established risks, our survey shows that only 40% of boards are satisfied with the management of new and emerging risks. This highlights the need for organizations to enhance their ERM practices, particularly in the management of emerging risks. Better and faster integrated risk intelligence that provides timely insights on opportunities, risk exposures and external considerations can drive more risk-confident decisions at organizations and allow organizations to respond more quickly to market pivot points.

However, more organizations are examining what they need to put in place to generate this competitive leverage. This paradigm change is causing audit committees and boards to reflect on the organization's skill sets and talent needs for the future. Board members identified lack of talent and skill sets as the top obstacle to effectively managing upside and outside risks. While a number of other obstacles flow closely behind, indicating multiples challenges for management to overcome, upskilling the risk professional of the future should be a clear priority.

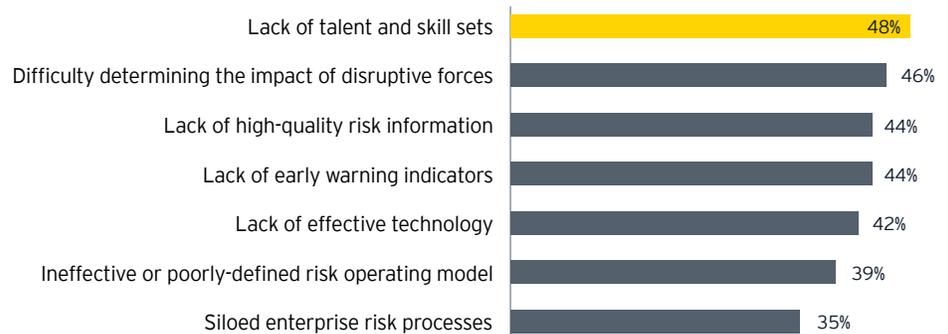
As risks, such as those related to innovation and talent, culture, geopolitics, the abundance (possibly overabundance) of data, privacy, environmental and social factors, and resilience continue to challenge organizations and their risk functions, it will be critical for them to have the right talent with the right skill sets in place. We expect that organizations will be focused on reevaluating their talent strategy and assessing whether they have the right mix of skills to address the

## Significant room for improvement in managing atypical and emerging risks



How effective is your enterprise risk management approach in the following areas: managing traditional risks and managing atypical and emerging risks

## Boards identify multiple organizational obstacles to managing strategic and external risks (percentages indicate those that say each is more than a moderate obstacle)



To what extent do the following organizational obstacles compromise your ability to manage risks that are not within your organization's control, such as strategic and external risks?

current and future risk landscapes. This may include reskilling or obtaining specialized talent with a greater focus on skills around technology automation, machine learning and data analysis to deploy more effective risk management techniques and oversee a complex and dynamic risk landscape. The board can play a crucial role in challenging how the talent strategy is enabling the transformation of ERM.

## Charting the right path forward: the future of risk management

The following five objectives should be considered when designing a vision for the future of risk management. Understanding these objectives can help boards evaluate if their own organization's ERM programs are future-fit:

### 1. Establish an adaptive risk governance framework

An adaptive risk framework requires changes to traditional risk management models, though not necessarily drastic changes. Organizations should explore methods to strengthen their three-lines-of-defense model<sup>4</sup> to enhance the effective management of risks. Operationalizing a three-lines-of-defense model that is suitable to managing the organization's key risks with appropriate first-line accountability and second-line oversight of risks will be critical. Risk and compliance functions will also need to be embedded with business functions to keep up with product and service innovations, while at the same time managing and monitoring real-time risk, predictive business models and significant third-party interactions. Risk teams should provide insights and expectations that will help the business monitor overall effectiveness.

### 2. Make sure you have the right skill sets on the team and appropriately leverage technology tools

New skills – both soft and hard – will also be necessary. For example, organizations will need people who can be dynamic and cover multiple risk topics (e.g., compliance, operational risk, resiliency), as well as individuals with experience in specific types of risks (e.g., cloud, cyber, blockchain). Having the right skills at the table at the right time coupled with leveraging technology tools (such as artificial intelligence and machine learning) will help in identifying and responding to new and emerging risks.

### 3. Build risk and trust considerations into the product and service design phase

Achieving the vision of real-time product development with embedded risk controls requires that companies have technology that observes customer actions in real time and triggers product and service mechanisms designed with a set of risk rules to instantaneously adjust product features (e.g., price, terms). Risk should collaborate with the business on the initial product design with the goal of identifying a comprehensive set of customer attributes and behaviors related to key risk considerations. This includes considerations and risks relating to building consumer trust by focusing on the customers' best interests (e.g., suitability of products/services, privacy, protection of personal data), making sure customer retention and enforcing the company's brand. Such steps are necessary if organizations are to quickly launch, scale and manage new, risk-informed products and services.

### 4. Strengthen resiliency

Resiliency, cybersecurity and privacy are critical considerations for both satisfying customer expectations about reliability and protecting brand reputations and information assets. Resiliency should be infused throughout the extended enterprise, including in the operations of third- and fourth-party vendors, especially critical vendors. Since preparedness is essential to resiliency, organizations should conduct simulations under a variety of disruption or crisis scenarios.

### 5. Harness data intelligence and architecture

Risk functions need a robust foundational platform that integrates with a broader governance, risk and compliance ecosystem. The goals are to use data more effectively and streamline risk management processes. For example, such platforms can support automated risk monitoring and data models for improved business intelligence and decision-making.

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4. The Institute of Internal Auditors' three-lines-of-defense model enhances the understanding of risk management by clarifying roles and duties in its model and notes the following:

- ▶ The first line of defense: the function that owns and manages risk
- ▶ The second line of defense: functions that oversee or specialize in risk management and compliance
- ▶ The third line of defense: functions that provide independent assurance

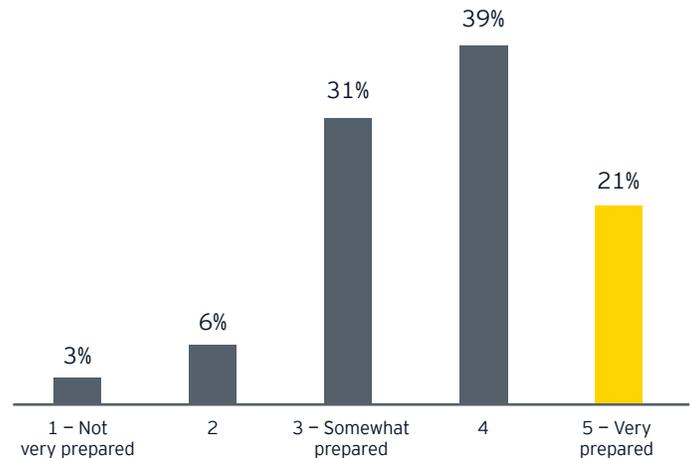
## Boards seek more sophisticated crisis planning to build risk resiliency

Board members do not believe that their organizations are well prepared to respond to an adverse risk event. In fact, only 21% of board members say their organization is very prepared to respond to an adverse risk event from a planning, communications, recovery and resilience standpoint. Advanced manufacturing and consumer businesses are least prepared, as are smaller companies. While simulation exercises, stress testing and scenario analyses are vital for bolstering risk readiness, only 19% of companies undertake these very frequently.

Companies performing scenario analyses and stress testing key assumptions and operating performance variables, such as impacts of upcoming geopolitical challenges, supply chain disruption, climate change and regulatory factors, are far better positioned to respond to emerging challenges with agility and conviction. Indeed, the 42% of board members whose organizations perform simulation exercises, stress testing and scenario analysis on a more-than-moderate frequency say they are very prepared to respond to an adverse risk event, compared with only 16% that conduct exercises less frequently.

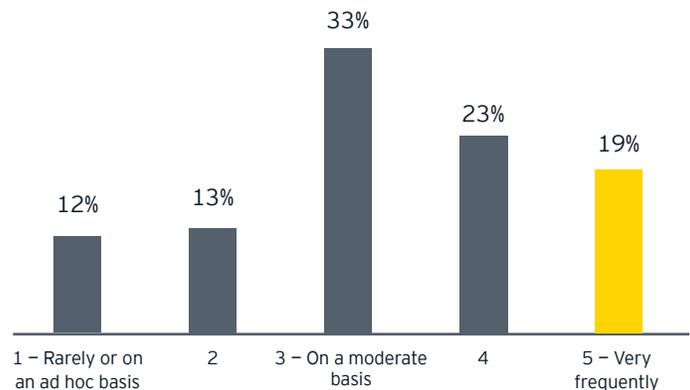
While prevention must always remain a priority, advance crisis preparation is now imperative, as avoiding crises entirely is nearly impossible. To help companies prepare for the challenge, boards should determine whether management has a practical, relevant and rehearsed crisis response program within the company's broader resiliency toolkit and integrated into its ERM program. This integration helps safeguard that crisis response planning is aligned with and informed by the company's strategic plan and risk tolerances, and that it is dynamic and evolves along with changes to risk assessments and prioritization. Boards should actively oversee and challenge all aspects of that program, including key considerations before, during and after an event, and should participate in various simulation exercises with management teams to exercise the muscle that is responsible for crisis response.

## Only 21% say their organization is very prepared to respond to an adverse risk event



How prepared is your organization to respond to an adverse risk event, from a planning, communications, recovery and resilience standpoint? (Please rank on a scale of 1 to 5 where 1 is not very prepared, 3 is somewhat prepared and 5 is very prepared.)

## Simulation exercises are vital preparation for adverse risk events



How often does your organization perform simulation exercises, stress testing and scenario analysis to anticipate and manage future risks? (Please rank on a scale of 1 to 5 where 1 is rarely or on an ad hoc basis, 3 is on a moderate basis and 5 is very frequently.)



### Key board takeaways:

## Turn risk into strategic value

- ▶ **Categorize risks into upside, outside and downside risks.** Make sure the organization has designed a balanced risk portfolio and appropriately prioritized its risks with a greater focus on upside and outside risks.
- ▶ **Turn risk into opportunity.** Make sure the board has the information, capability and time available to explore and discuss how changes in the risk landscape might lead to a change in risk appetite. Look beyond mitigation to also oversee how risk can be leveraged to build trust and drive growth.
- ▶ **Challenge management to bolster risk management skills across the organization and upskill the risk professional of the future.** Boards must evaluate with management whether the organization has the necessary skill sets to effectively manage today's major risks. Challenge whether risk functions have the range of technology and data-related capabilities for deploying more sophisticated risk tools and managing emerging risks. The right mix of future skill sets may include skills around machine learning, data privacy, technology, data security and the climate change agenda.
- ▶ **Help management harness risk to build trust in new technology.** Challenge whether appropriate frameworks are in place to identify, measure and respond to risks associated with adopting disruptive technology. This is essential to building regulator, customer, supplier and employee trust in new technology.
- ▶ **Constructively challenge crisis planning and build risk resiliency.** Challenge whether management has plans in place to prepare for and respond to crises and adverse risk events.

# Redefine risk reporting to reflect the dynamic risk landscape

Board members say they are satisfied with the risk reporting they receive, but they recognize the need for improvement. Nearly a third of board members do not receive reports on some significant risks that are on their radar, and only 21% are very satisfied with the accuracy, completeness and breadth of reports received.

## Boards seek more predictive risk insights and identify multiple areas for improved reporting

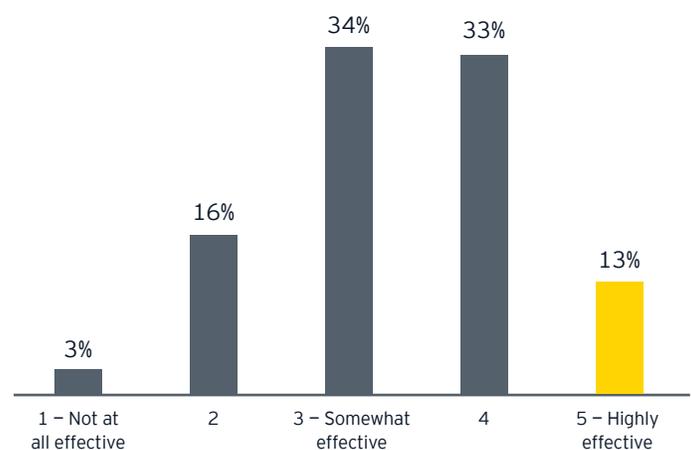
Boards increasingly want predictive or forward-looking insights in addition to reporting on past events to help them effectively oversee risk management. However, only 46% of board members believe that ERM at their organization is better than somewhat effective at generating this insight, and just 13% consider their approach highly effective.

The challenge is more pronounced at smaller companies, where only 9% of board members of companies generating \$1b-\$2b in revenue say that ERM is highly effective in providing predictive and forward-looking insights.

Fewer than 20% of board members are extremely confident in risk reporting from management and want more information on a host of significant risks, such as the driver and results of economic uncertainty; business environment megatrends; new and emerging business models; consumer, social and other trends that could challenge the organization's current strategy; and culture and conduct-related risks.

Risk reporting should help organizations evaluate risk against their strategic goals, performance measures and impact on stakeholder trust. For example, reporting may include scenarios and predictions of upcoming geopolitical

## 87% of boards do not believe that ERM at their organization is highly effective at providing predictive insights



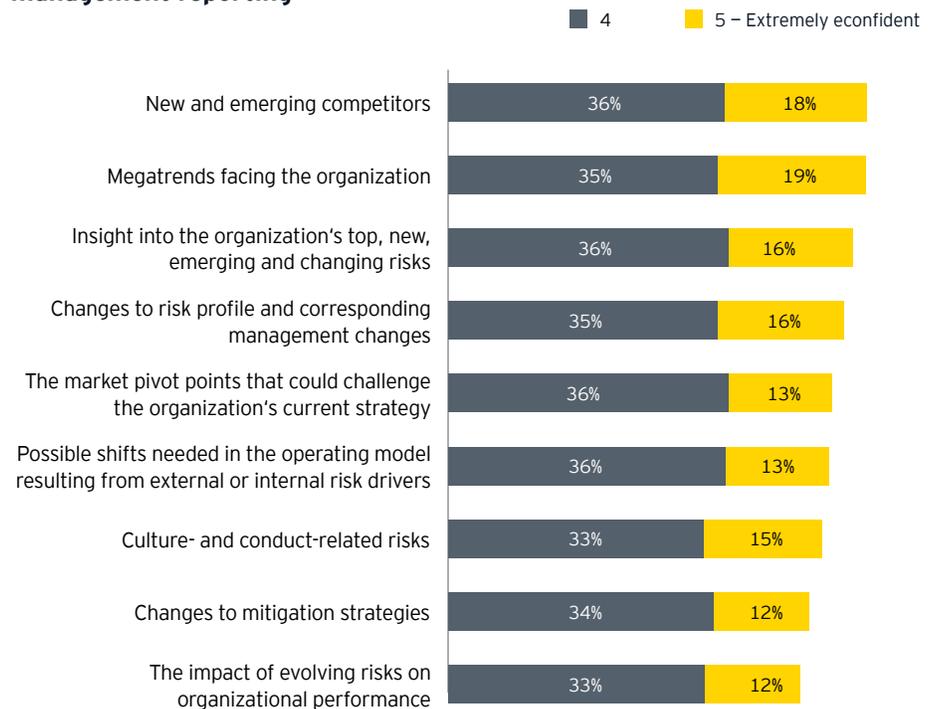
How effective is your enterprise risk management approach in the following area: providing predictive and forward-looking insights and indicators?



challenges, supply chain disruption related to trade and potential impacts of regulatory changes. Such insights would provide the board with a better forecast of the types of risks that might materialize and when.

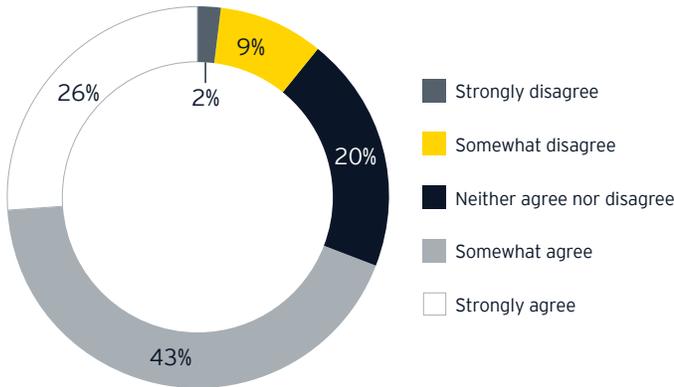
Leading organizations are leveraging machine learning, artificial intelligence and other technologies to enhance their risk management efforts and provide predictive, forward-looking risk insights to management and boards. This is helping chief audit executives, chief risk officers and others to not only provide greater and deeper insight but also to drive efficiencies. Internal audit functions are making use of automated techniques for more ongoing monitoring of emerging risks through dashboards that provide continuous control monitoring and real-time assurance, enabling them to see areas of potential concern before they become an issue by recognizing correlations and patterns in data.

**Most boards are not confident in multiple aspects of risk management reporting**



How confident is the board in risk reporting from management of the following? (Please rank on a scale of 1 to 5 where 1 is not confident, 3 is somewhat confident and 5 is extremely confident.)

**Just 26% strongly agree that they have clearly communicated to management the risk areas where they would like more reporting**



To what extent do you agree with the following statement: We have clearly communicated to management in which risk areas we would like more reporting.

**Boards must clearly communicate their reporting requirements to management**

When it comes to enhancing risk reporting, just 26% of board members strongly agree that they have clearly communicated to management the risk areas where they would like more reporting.

Among the board members who only somewhat agree that they have clearly communicated where they need better reporting, only 54% believe risk reporting is comprehensive enough to enable the board to make the right decisions on behalf of the organization.

As a starting point, boards should clearly articulate to management the risk areas where they would like more reporting, which should include unknown threats and environmental, social and governance issues. Boards should seek more dynamic reporting to surface emerging risks and digitally enabled reporting to predict new threats. Leading boards also request reporting from different executives, such as the chief human resource officer (or equivalent), and seek to expand their focus on intangible assets and key long-term value drivers, including talent, culture and reputation.

**Boards that clearly communicate their reporting requirements to management are much more confident in the reporting they receive**



■ Those that at best only "somewhat agree" that they have clearly communicated to management where they would like more reporting  
 ■ Those that "strongly agree" that they have clearly communicated to management where they would like more reporting

How confident is the board in risk reporting from management of the following?



**Key board takeaways:**

## Redefine risk reporting to reflect the dynamic risk landscape

- ▶ **Request adjusted risk reporting that reflects the new risk landscape, including improved reporting on emerging risks.** Work closely with management to specify the type and format of reporting that is most effective. Verify that management has appropriately identified a set of key performance indicators and key risk indicators that can be used to communicate a risk-centric view.
- ▶ **Ask for more predictive insights.** Question whether risk teams and management could improve how they are leveraging internal and external data to better forecast the types of risk that might materialize and when (e.g., using social media data to anticipate changes in customer sentiment and demand for products).

# Evolve the board's role in ERM

Most boards believe they are well equipped to effectively oversee risk management, but there is no room for complacency. To make sure they stay effective, they need a dedicated focus on emerging and existential risks on the board agenda. Boards should also utilize external experts to upskill the board, advise on specialized risks and stay on top of megatrends to identify risks and uncover opportunities.



### It's time for more time: key risks must be incorporated into the board agenda time

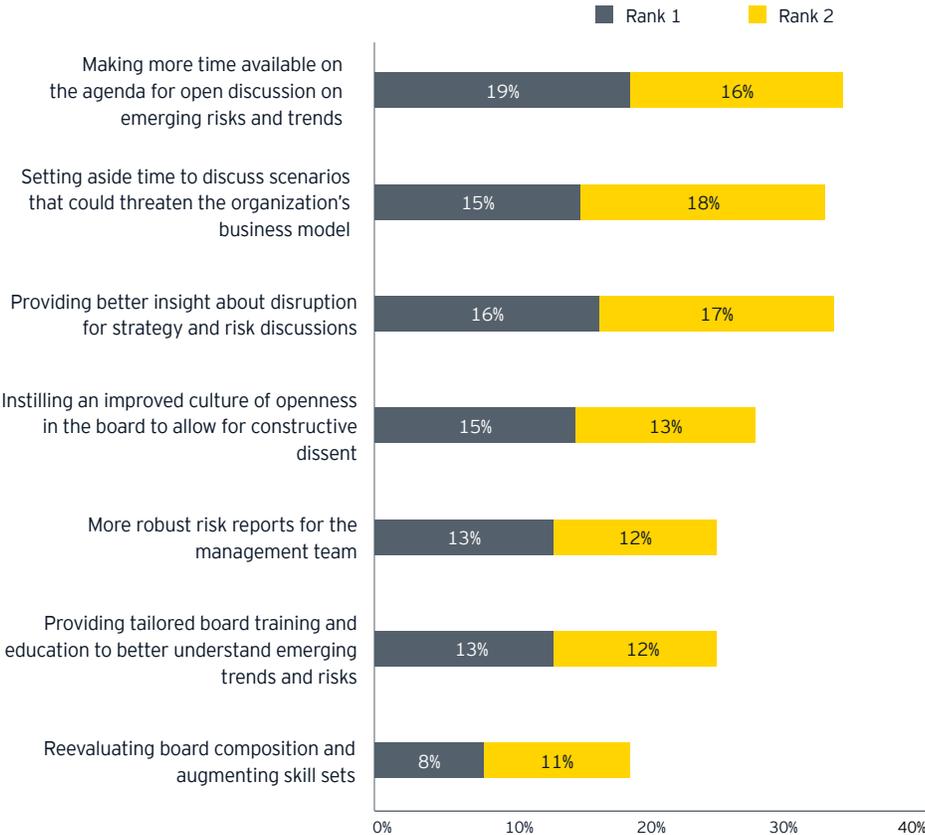
Board members are requesting more time to effectively oversee risk. Board members said making more time available on the agenda for open discussion on emerging risks and trends and setting time aside to discuss scenarios that could threaten the organization's business model are the two most effective measures that would improve their risk oversight capabilities.

### Survey suggests need to upskill boards

Sixty-four percent of board members believe their composition and the represented skill sets are adequate for overseeing their organization's risk management. This finding reveals significant opportunity to strengthen board oversight through challenging current board competencies, assessing the need for board refreshment, enhancing diversity on the board for broader perspectives and experiences, and upskilling the full board through continuing training and education.



#### Boards request more time to effectively oversee risk



Which of the following are most effective in enhancing your board's risk oversight responsibility?

As business environments change, so too must the board competencies and practices that drive board effectiveness. While boards do not need to be experts in all the risks that might impact their business, they need to be sufficiently aware so that they can constructively challenge and question management. Board members should adopt a mindset of continuous learning and performance improvement and regularly participate in education programs that are tailored to the company's business and industry as well as the skill set of the board itself.

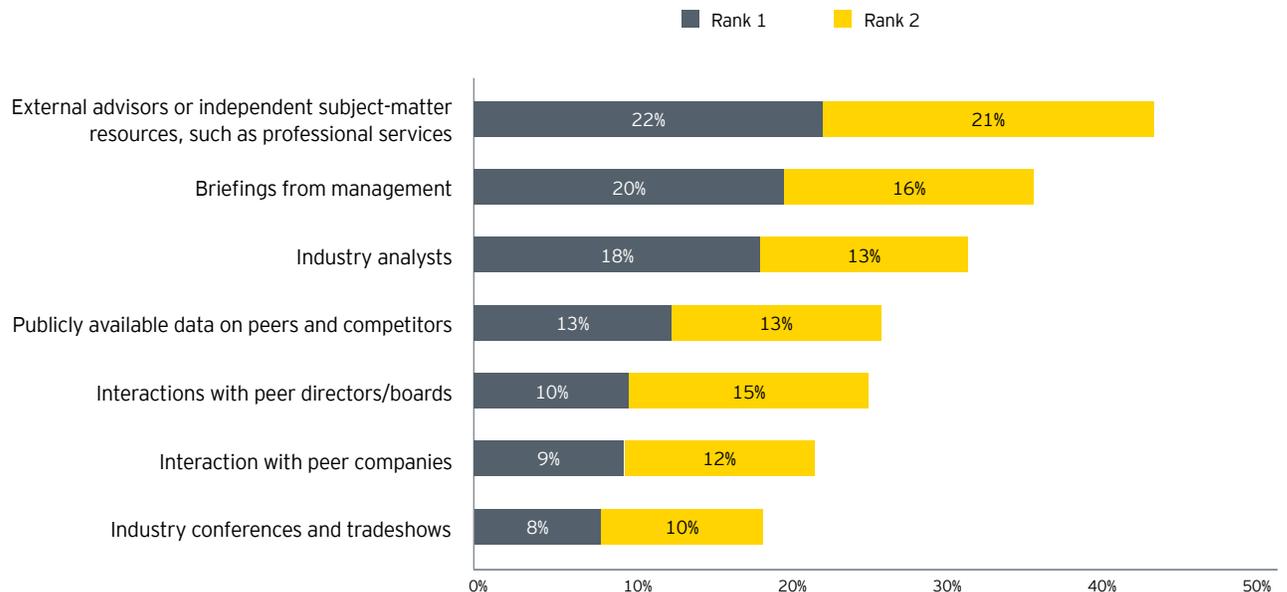
### External advice is key to staying on top of megatrends to identify risks and uncover opportunities

Boards must proactively take steps to keep updated on technology, economic and geopolitical developments so that they can effectively oversee risk management. Briefings

from external advisors, industry analysts and independent subject-matter professionals are the most effective way of doing this. More than 40% of board members said such external advice is key to staying up to date on megatrends, emerging risks and potential strategic inflection points.

External advice is also key to avoiding groupthink and mitigating internal bias. Boards should more regularly complement management's information with data and insights provided by independent sources so that they understand the latest developments and progressive oversight practices to prevent blind spots. As noted earlier, boards cannot be passive in waiting for this kind of information to come to them – they must actively seek out and obtain information, new learning and independent external perspectives.

### External advice is key to staying up to date with megatrends, emerging risks and potential strategic inflection points



Which two of the following are most important in enabling your board to stay up to date on megatrends, emerging risks and potential strategic inflection points?

A photograph of a person silhouetted against a bright opening in a dark, crystalline ice cave. The person is wearing a backpack and is walking towards the light. The ice formations are intricate and layered, creating a complex, textured environment. The lighting is dramatic, with the person and the cave walls in deep shadow, while the opening is a bright, almost white light source.

### Key board takeaways:

## Evolve the board's role in ERM

- ▶ **Include sufficient agenda time.** Make sure there is enough time on the agenda to fully consider emerging risks. Reevaluate risk oversight practices and related structures to assess whether committee oversight changes would enhance oversight.
- ▶ **Seek outside expertise and incorporate external data.** Seek external expertise from advisors, analysts and professionals, and incorporate external third-party data to gain the knowledge necessary to effectively oversee risk management.
- ▶ **Assess and enhance board competency and diversity.** Conduct competency assessments to determine where there are skills and competency gaps that need to be filled.

# Conclusion



Investors, regulators, consumers and other key stakeholders expect boards and risk functions to take responsibility for the expanded range of issues that are now an inescapable part of their environment, particularly emerging risks presented by technology advances, globalization and market disruption.

Boards and management teams need to find the right balance between managing legacy risks and the fresh challenges arising from embracing disruption to maintain their competitive advantage. This search for balance is further complicated by the need to update compliance and risk management models to incorporate a much more dynamic and interrelated risk landscape, as well as to meet enhanced stakeholder expectations for transparency and accountability.

The world of governance and risk management will continue to transform. There's no off-the-shelf playbook to manage many of the complex and major risks identified in this report. For boards, their work should be to remain vigilant, increase their own fluency around emerging risks and external trends, and continually challenge and strengthen their oversight practices to enhance the organization's agility and ability to survive and thrive.

## Questions for the board to consider:

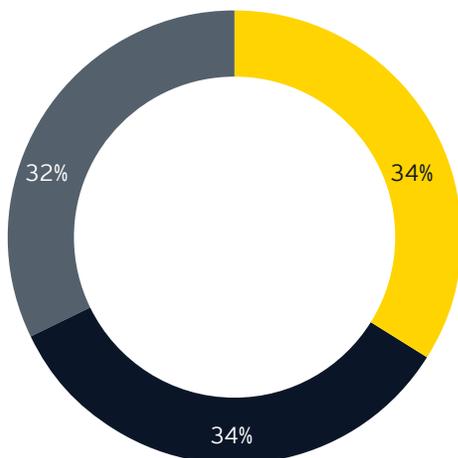
- ▶ Does the organization take into consideration the full view of risks – upside, downside and outside – when developing its strategic blueprint?
- ▶ How frequently does the organization test its strategy for resilience?
- ▶ Is the organization's risk function an intrinsic part of the organization's strategic planning and decision-making process? To what extent does it leverage risk to benefit from the upside of disruption?
- ▶ How effectively does the organization leverage risk intelligence to gather foresights, make better decisions, and increase internal and external agility?
- ▶ Is the board using external perspectives and independent data to identify and monitor emerging risks?
- ▶ Does the organization conduct risk assessments frequently enough to capture new risks and adjust its risk appetite accordingly?
- ▶ Does the board allocate enough time on the agenda for open discussion and brainstorming on emerging risks and trends?
- ▶ How can the organization improve its ERM practices and processes with the use of scenario planning, stress testing, and technology-enabled risk analytics and continuous monitoring?
- ▶ How can the board better instill a risk mindset and culture that drives trust with the organization's stakeholders?

# Full survey demographic breakdown

## About the research

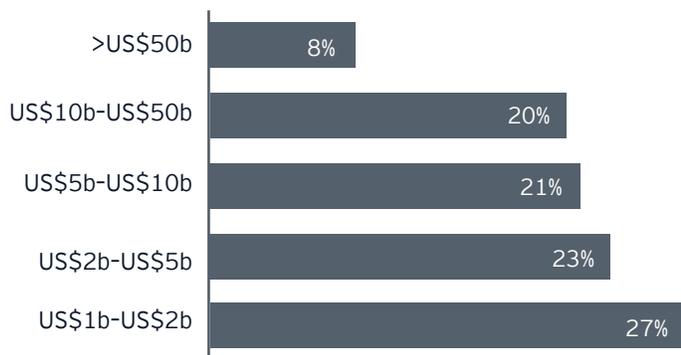
This report is based on a telephone survey of 500 board directors conducted in 2019. 81% are non-executive or independent directors. 19% are CEOs. All participants sit on boards of companies with at least US\$1bn in annual revenue, and 50% sit on boards of companies with at least US\$5bn. Participants were sourced from around the world (Americas: 34%, EMEIA: 34% and Asia-Pacific: 32%) across a wide range of industry sectors.

### Company headquarters of participants' primary board position - by region

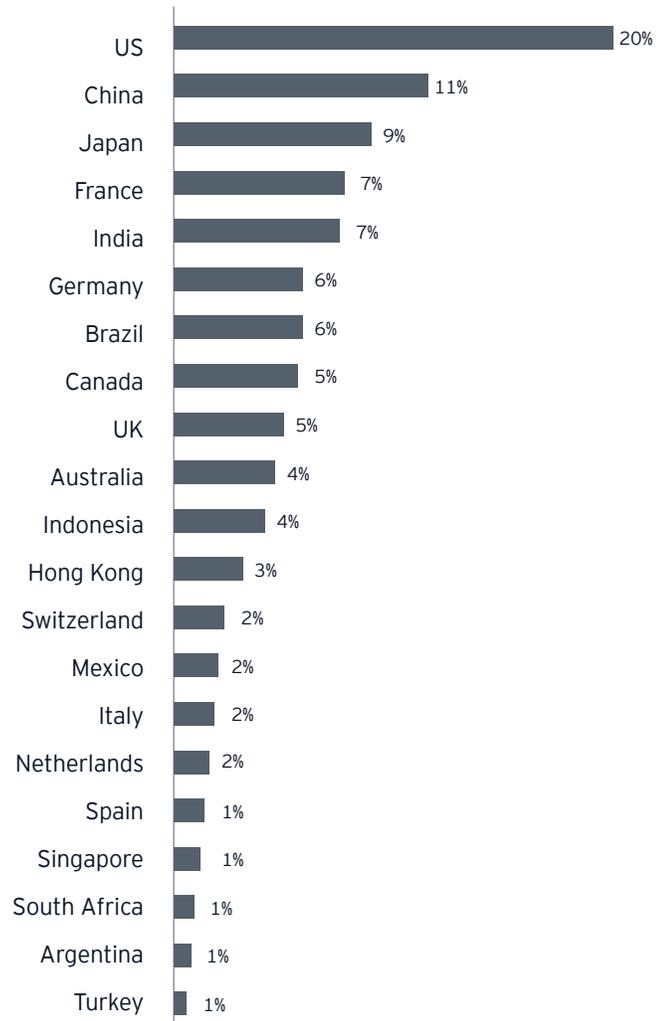


Americas EMEIA Asia Pacific

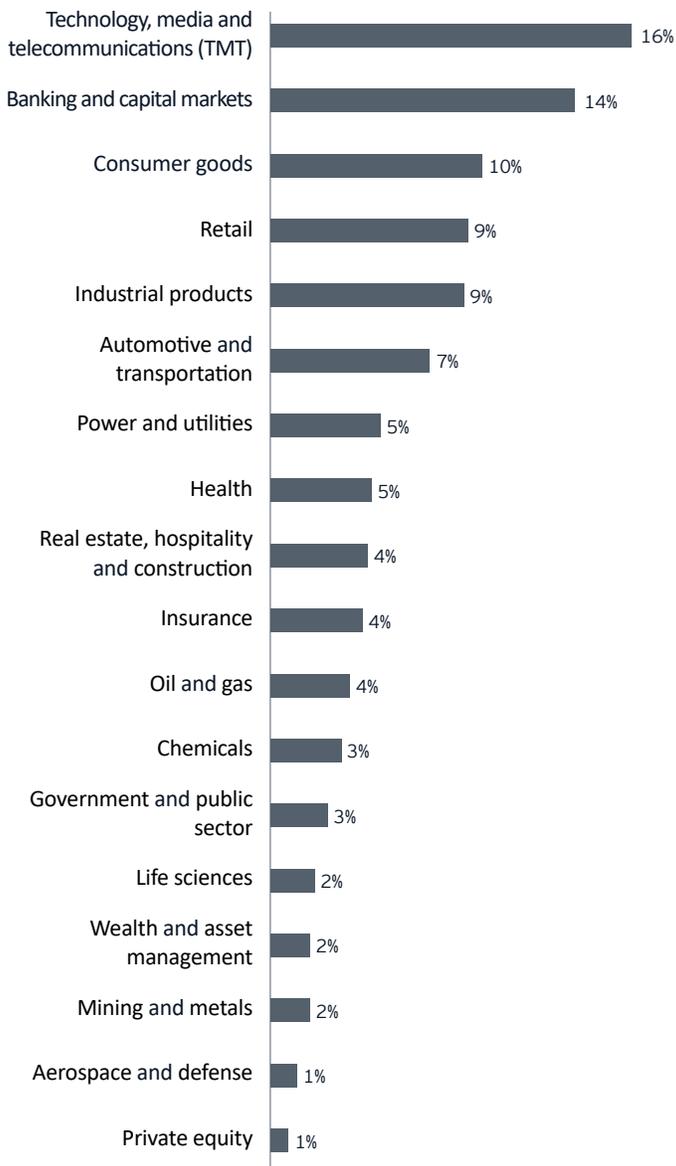
### Revenue of participants' primary board position



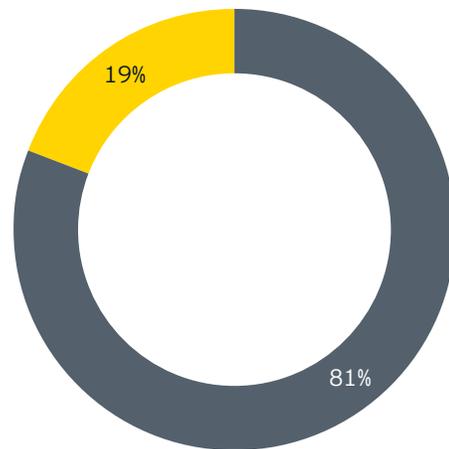
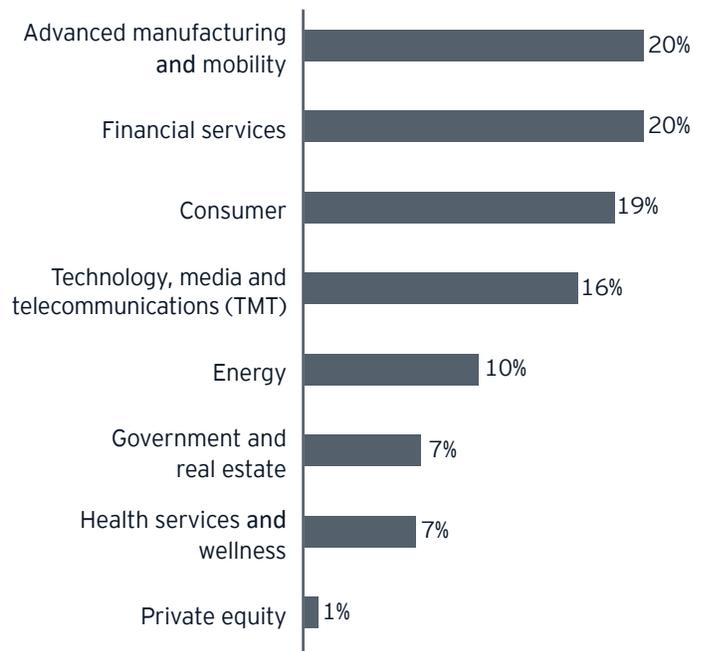
### Company headquarters of participants' primary board position - by country



**Sector of participants' primary board position - expanded**



**Sector of participants' primary board position - consolidated**



■ Non-executive director/independent board director ■ CEO

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2003-3446687  
ED None

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