



Directors Quarterly

Insights from the Board Leadership Center

April 2024



Setting the pace on Gen AI

With the rise of generative artificial intelligence (Gen AI), companies are facing the challenge of moving quickly—but not too quickly. Gen AI governance has moved to the top of many board agendas as directors understand the potential competitive advantages as well as the potential risks that the transformative technology poses for the company and its strategy.

For insights on the current state of board oversight, check out findings from our director survey and our recent KPMG Board Leadership Center webcast discussion of the risks, opportunities, and disruptions posed by Gen AI.

Our financial reporting and auditing update includes the latest developments on the Securities and Exchange Commission final rule on climate-related disclosures, final rules and guidance related to special purpose acquisition companies (SPACs), and the recent dialogue about the Public Company Accounting Oversight Board (PCAOB) proposal on noncompliance with laws and regulations (NOCLAR).

In this edition, we also report on trends in Latino representation on Fortune 1000 boards. Our latest study, in collaboration with the Latino Corporate Directors Association, finds that Latino directors held 5.0% of Fortune 1000 board seats in 2023, up from 2.7% in 2019.

Finally, we share insights from our discussions with private company directors and CEOs on how independent voices can help add value to private company boards, with practical takeaways for successfully tapping into the value of independent directors.

John H. Rodi
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Financial reporting and auditing update

Current quarter financial reporting matters

SEC stays final rules on climate disclosures

On April 4, 2024, the SEC issued [an order](#) staying its final rules on climate-related disclosures pending the completion of the Eighth Circuit's review of legal challenges to the final rules. "In issuing a stay, the Commission is not departing from its view that the Final Rules are consistent with applicable law and within the Commission's long-standing authority to require the disclosure of information important to investors in making investment and voting decisions."¹

The [final rules](#) as adopted on March 6, 2024, while scaled back from the proposed rules, would require public companies to make detailed climate-related disclosures in their annual reports and financial statements. A number of industry and environmental organizations, as well as state attorneys general, challenged the final rules in various courts, and on March 21, a judicial panel issued an [order](#) consolidating these cases in the Eighth Circuit Court of Appeals.² The SEC's April 4th order stays the Commission's final rules pending the Eighth Circuit review and decision. That decision could affect the legality and scope of the final rules, including the scheduled compliance phase-in.

Notwithstanding this uncertainty, companies currently assessing reporting requirements under the California climate laws as well as EU and other international standards can now use the SEC's final rules to complete their analysis of reporting obligations and create a rigorous, repeatable, and timely climate reporting process. The final rules comprise disclosures with two distinct components:

- **Reg S-X financial statement disclosures**, which will be part of the audited financial statements and therefore in the scope of the company's internal control over financial reporting.
- **Reg S-K climate-related disclosures** in the company's annual report or registration statement.

The two sets of disclosures are connected because the Reg S-K disclosures require quantitative and qualitative disclosure of any material expenditures incurred and material impacts on financial estimates and assumptions that directly result from certain items.

Financial statement disclosures

Certain disclosures (qualitative and quantitative) are required in a note to the financial statements for the company's most recent fiscal year and include disclosures about:

- severe weather events and other natural conditions (not defined):
 - expenditures and losses, if the aggregate amount thereof is $\geq 1\%$ of the absolute value of income or loss before income tax expense or benefit for the relevant fiscal year—subject to a de minimis amount of \$100,000; and
 - capitalized costs and charges, if the aggregate amount thereof is $\geq 1\%$ of the absolute value of stockholders' equity or deficit at the end of the relevant fiscal year—subject to a de minimis amount of \$500,000;
- material effects on financial estimates / assumptions related to severe weather events and other natural conditions, or any climate-related targets or transition plans disclosed by the registrant; and
- carbon offsets or renewable energy credits / certificates if their use is a material component of the company's plans to achieve its disclosed climate-related targets or goals.

¹ US Securities and Exchange Commission, In the Matter of the Enhancement and Standardization of Climate-Related Disclosures for Investors (Order Issuing Stay), April 4, 2024.

² US Judicial Panel on Multidistrict Litigation Consolidation Order, March 21, 2024.

Climate risk disclosures

The climate risk disclosures outside of the financial statements are arranged under the broad categories of governance, strategy, and risk management, which is consistent with the structure in the SEC's recent rule on [cybersecurity reporting and disclosures](#).

These disclosures include the following governance and risk management disclosures:

- the board's oversight of climate-related risks and, if applicable, the (sub)committee responsible for such oversight and the process by which the board or such (sub)committee is informed about such risks;
- management's role in assessing and managing material climate-related risks, and the relevant expertise of such individuals; and
- the company's process for identifying, assessing, and managing climate-related risks and integration into its overall risk management system or processes.

The disclosures also include quantitative and qualitative disclosure of any material expenditures incurred and material impacts on financial estimates and assumptions that directly result from the company's:

- activities to mitigate or adapt to climate-related risks;
- transition plan; and
- targets or goals, or actions taken to make progress toward achieving those targets or goals.

Scopes 1 and 2 GHG emissions

Large accelerated filers and accelerated filers (except for smaller reporting companies and emerging growth companies) are required to disclose gross Scope 1 and/or Scope 2 greenhouse gas (GHG) emissions, if material. Limited assurance will be required three years after the disclosures are first required. For large accelerated filers only, reasonable assurance will be required four years after that.

The rules do not prescribe a specific approach to be followed. Instead they require the company to describe the methodology, significant inputs, and significant assumptions used to calculate GHG emissions, including the:

- organizational boundaries;
- operational boundaries; and
- protocol or standard used, with details about the calculation approach, data, and tools.

Phased transition

The April 4th stay order does not address the scheduled phase-in of the Commission's final rules. While the earliest compliance date is scheduled for the fiscal year beginning in calendar year 2025 for large accelerated filers, there is uncertainty as to how the Eighth Circuit litigation and any subsequent SEC action might affect the scheduled phase-in.

Also see [SEC stays its climate rule pending judicial review](#).

PCAOB seeks additional insight on NOCLAR proposal

On March 6, a diverse group of auditors, preparers, legal experts, investors, and professors gathered for a virtual roundtable hosted by the PCAOB. The focal point of the dialogue was the PCAOB's [proposal](#) on noncompliance with laws and regulations (NOCLAR)—an extensive proposal that would significantly increase auditors' responsibilities related to NOCLAR. Although the proposal is targeted to auditors, the potential effects would be wide-reaching, extending to company management and audit committees alike.

The roundtable aimed to foster public outreach and facilitate discussions on various aspects of the proposal as the PCAOB staff strives to develop an operable standard that adequately safeguards investors' interests. Despite achieving some consensus, the discussions underscored the substantial work that remains before the PCAOB can issue a final standard.

The varied perspectives on the proposal's key concepts, expressed at the roundtable and in submitted comment letters, underscore the significant challenges that remain in developing an updated NOCLAR standard. The PCAOB's standard-setting agenda indicates that a final standard is anticipated in 2024. However, this timeline will depend on the PCAOB's redeliberation of the feedback, the extent of changes made to the proposal, and the decision on whether to re-propose. Whether re-proposal is necessary was yet another area where the panelists were divided.

SEC compensation clawback rules become effective; checkbox clarifications

The national exchanges' (NYSE and Nasdaq) final [compensation clawback listing standards](#) became effective on October 2, 2023. Companies were required to adopt their recovery policies by December 1, 2023, and have had many questions about how to apply their new recovery policies under the rules. Among them, companies have asked about when to check Boxes 1 and 2 in their annual report filing.

At the 2023 AICPA and CIMA Conference on Current PCAOB and SEC Developments, staff from the SEC's Division of Corporation Finance clarified that companies should check Box 1 for any annual financial statements that reflect an error in previously issued financial statements as defined by Topic 250 (accounting changes and error corrections). Box 1 is not checked (1) for changes in accounting principle or (2) if there is an out-of-period adjustment reflected in current-year financial statements that does not change any prior-year financial statements.

A company checks Box 2 if the financial statements included in the filing reflect the correction of one or more errors that required a recovery analysis—i.e., either a “Big R” or “little r” restatement to previously issued financial statements as defined in the rules.

There could also be circumstances where a company can check Box 1 but not Box 2. An issuer checks Box 1 any time there is an error correction, regardless of materiality. The issuer checks Box 2 only if those error corrections are “Big R” or “little r” restatements that require the issuer to perform an analysis under its recovery policy.

SEC finalizes SPAC rules

The SEC has adopted [final rules and guidance](#) to enhance investor protections in response to concerns arising from the surge in 2020 and 2021 of special purpose acquisition company (SPAC) IPOs and the subsequent acquisition of private operating companies (de-SPACs). Key provisions of the final rules include:

- **Enhanced disclosure.** The final rules require enhanced disclosures in SEC filings relating to a SPAC IPO and the subsequent de-SPAC transition.
- **Aligning de-SPAC transactions with IPOs.** The rules include various new requirements to align the existing rules and disclosure requirements governing de-SPAC transactions with those of a traditional IPO.
- **Increased transparency in using projections.** Financial projections are a common feature in SPAC-related and traditional IPO filings. In an effort to drive greater transparency in using financial projections, the rules (among other things) eliminate safe harbor provisions for those projections from SPAC-related filings, require SPACs to distinguish between projections based on historical results and those that are not, and provide more clarity when projections include non-GAAP measures.

For more detail about these and other issues potentially affecting you in the current period or near term, see the [KPMG Q1 2024 Quarterly Outlook](#).

A boardroom lens on Gen AI



“Generative AI brought AI from a tool used by data scientists thousands of times to one used by consumers a billion times in a matter of months,” said Per Edin, Advisory GTM leader for Generative AI at KPMG. “It’s an amazing development.”

In a recent KPMG BLC survey, directors said that they recognize the potential value of generative AI—primarily to drive greater efficiencies, but also to grow market share and revenue, and develop new services.

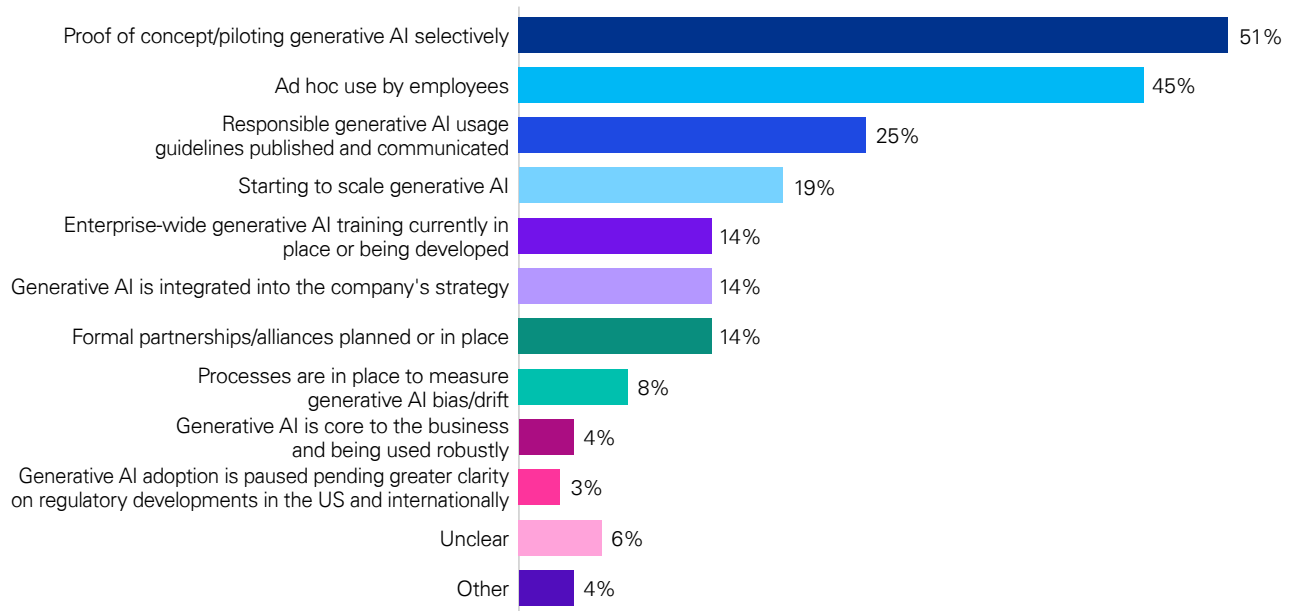
“I think some of the fundamental board Gen AI discussions right now are around risk, implications for strategy, and implications for the business model,” said KPMG BLC Senior Advisor Claudia Allen during a March 21 webcast with Edin and KPMG BLC Leader John Rodi.

“Boards, perhaps more than almost anyone at a corporation, need to have the longest term view,” said Allen.

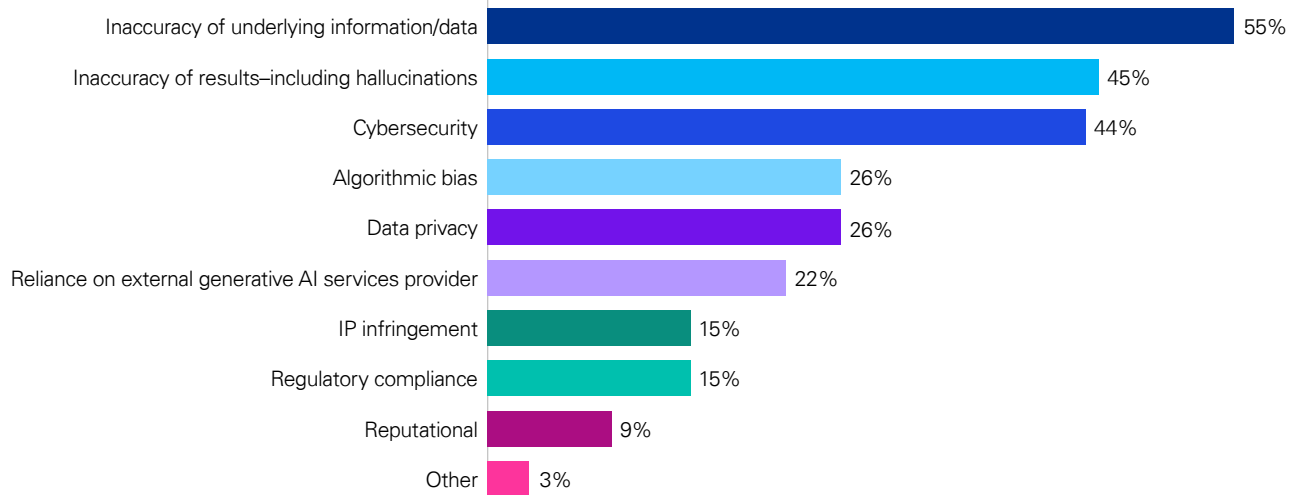
Watch our [webcast replay](#) and view the results of our [director survey](#).

A boardroom lens on Gen AI: Select survey findings*

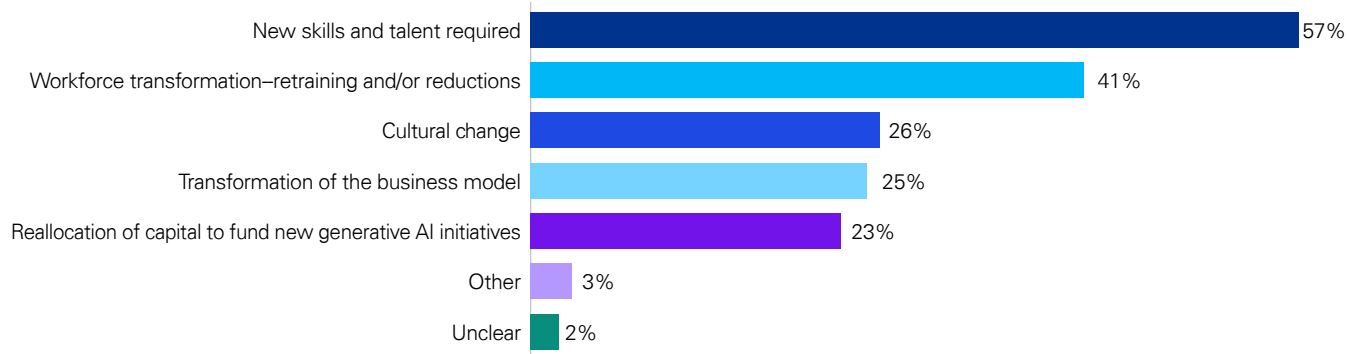
What is the state of your company’s adoption of generative AI? (select all that apply)



Which of the following risks posed by the company’s adoption of generative AI are of greatest concern?
(select up to three)



In your view, what are the most significant disruptions facing the company in its adoption of generative AI?
(select up to two)



*Results are based on a survey of 106 US board members, nonexecutive chairs, and lead directors, conducted January 30–February 29, 2024.

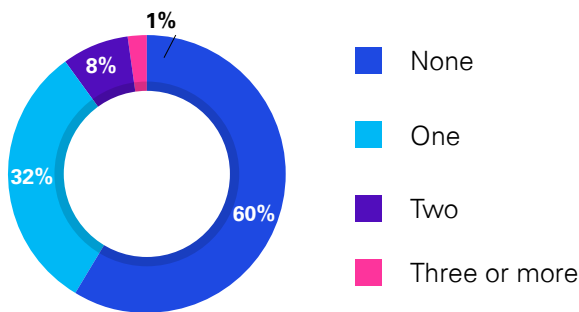


Latino representation on Fortune 1000 boards

Increasing board diversity remains a priority for both boards and shareholders. Among S&P 500 companies, 94% disclose that they incorporate gender diversity and racial/ethnic diversity into their director search criteria, while 19% reference diversity of sexual orientation.¹ Institutional investors expect boards to consider and disclose how their composition supports company strategy and performance, with some investors voting against nominating/governance (nom/gov) committee chairs or members for lack of board diversity or related disclosures.

Latino representation on Fortune 1000 boards: 2023 Edition, a study conducted by the KPMG BLC and the Latino Corporate Directors Association, finds that Latinos held 5.0% of Fortune 1000 board seats in 2023. However, with nearly 20% of US residents identifying as Latino,² there is a ripe opportunity for change and for this missing voice to be incorporated at the highest level of corporate leadership.

Number of Latino directors per Fortune 1000 board 2023; n=1,000 companies



Note: Does not equal 100% due to rounding.

Below are highlights from the report:

The Latino presence in Fortune 1000 boardrooms increased to 5.0% in 2023 from 2.7% in 2019.

Although Latino director representation remains low overall, more Fortune 1000 companies now have a Latino director. In 2019, the first year of this study, 77% of Fortune 1000 boards had no Latino directors compared to 60% in 2023.

Larger companies are more likely to have a Latino director.

Fifty-four percent of Fortune 100 companies have at least one Latino director, compared to 47% of Fortune 500 boards and 40% of Fortune 1000 companies.

More than half of the Latino directors studied joined their boards within the last five years.

By comparison, 45% of all public Fortune 1000 directors have served for less than five years. Only 18% of Latino directors have served for 10 years or more, compared to 28% of all public Fortune 1000 directors.

The number of public Fortune 1000 nom/gov committees chaired by Latino directors increased to 32 in 2023 from 24 in 2022.

The Latino directors who serve on at least one board committee are most likely to serve on the audit committee (49%) and nom/gov committee (47%), followed by the compensation committee (42%). Latino directors served as chair of 32 audit committees, 32 nom/gov committees, and 30 compensation committees in 2023.

To read the full report, visit kpmg.com/us/blc.

¹ KPMG Board Diversity Disclosure Benchmarking Tool, powered by ESGAUCE, December 31, 2023.

² US Census Bureau, United States QuickFacts, population estimates as of July 1, 2023.

How independent directors can add value to private company boards

In any boardroom conversation, independent voices are vital to the quality of the discussion and the rigor of thinking and decision-making. For private companies, it can be game-changing, with the potential for taking the thinking on strategy, risk, talent, and the future of the business to a different level.

In our recent survey of private company directors, nearly 90% of respondents said their company has at least one independent director. And three-quarters said independent directors can add the most value to the business by serving as a sounding board for the CEO and other executives, advising on strategy, and helping to balance the views of management and owners. Indeed, private company directors—whether CEOs, founders, or investor representatives—are not uniform in their views, but the real and potential value offered by independent private company directors is evident in our [survey findings](#).

To get behind the data and better understand the real-world factors driving the use and effectiveness of independent directors, we convened roundtables with private company directors—in conversation with CEOs—around the US. These candid discussions provided insights into the value that private company directors and CEOs see independent directors adding—from providing a broader perspective on strategy, offering additional expertise in critical areas such as emerging technologies, international markets, and risk management, to helping instill the right tone and culture, and helping define the path as the company matures to a more robust governance structure. Participants also said that effectively drawing on the talent and skills of independent directors takes planning and work.

Our conversations, conducted under the Chatham House Rule, highlighted a number of factors that both private company directors and CEOs view as essential to successfully tapping into the value of independent directors.

Identifying the background, skills, and experiences desired in independent directors

A key consideration is the background, skills, and experiences the company should be looking for in an independent director, given the company's unique circumstances and needs, including its size, stage, and ownership structure. For example, family-owned companies may be looking for an independent director to help professionalize the board and formalize governance structures and processes, whereas institutional owners such as private equity and venture capital investors may be homing in on a director's industry-specific experience or preparing for an IPO by building a public company-ready board.

Other considerations might include:

- Can an independent director help provide a new direction—e.g., fresh thinking, new energy, strategy, or leadership?
- Some of the biggest challenges relate to digital transformation. As one director noted, “Reimagining your business and core strategy is an evolving process.” Digital transformation is key to strategic growth, and it is critical that the board have a “technology evangelist” to help cascade technology ownership across the company. “It’s not just the CTO’s responsibility.”
- Family-owned businesses face unique challenges. Investor-backed companies often follow a well-worn path—i.e., an IPO or sale to a strategic or financial buyer; however, family-owned businesses may face tension both between and among generations. For a family-owned business, consider where the company is on its journey—e.g., first, second, third, or fourth generation. “An independent director can play an important role in balancing the diverse interests and backgrounds of the family shareholders and considering their role in the management of the business.”
- Independent directors may bring specific expertise that the company needs—e.g., M&A, international markets, or emerging technologies, risk management, legal/regulatory compliance. “M&A would not have been possible without the experience of our independent directors,” said one CEO.

Serving in board leadership

Would independent board leadership (e.g., board or committee chair) help the board's governance structure and processes mature and thus improve the board's effectiveness? In our survey, 26% of respondents said that an independent director serves as board chair and another 15% said that an independent director serves as lead director. Of the survey respondents who indicated that their boards had audit or compensation committees, two-thirds said that those committees are chaired by an independent director.

Using an advisory board as a first step

Particularly for a family-owned business exploring adding independent perspectives and experience, an advisory board may be an important interim step. The advisory board—as distinct from the fiduciary board—can serve as a consultant to the CEO and senior management, providing advice and guidance on issues including the development and execution of strategy, operations, financial performance, risk management and mitigation, key business initiatives, senior management succession plans, capital projects and transactions, and corporate culture. An advisory board can also provide additional business acumen, as well as an unbiased view of company performance and the management team.

Companies that do not utilize an advisory board can still access outside thinking at the board level by bringing in board observers (who are often already investors in the company). “Even observers can make a difference,” said one independent director and observer to an employee-owned company board.

Bringing objectivity, challenging the status quo, and focusing on performance.

Our conversations highlighted the value of the objective perspective and unbiased viewpoint independent directors can provide, as well as their willingness to challenge the status quo. Other ways independent directors can add value include:

- Insisting on forward-looking, strategic board agendas and fewer management-led discussions. Focus on the future of the business by discussing culture, investment in the business, and key strategic initiatives, and spend less time on quarterly results and lookbacks. “Flip the agenda,” suggested one CEO, “and be very clear that you want the directors’ help in building forward-looking board agendas.”
- Focusing on a culture of performance, not just loyalty. In a family-owned business, talent can be a difficult discussion, and independent directors can provide

important insights. “Talk to senior leadership,” advised one director. “Make sure that company leaders have access to the board. They may not have an immediate need for the expertise of the outside director, but when they do, there’s a real opportunity to learn.”

- Helping the CEO understand blind spots on the leadership team and develop maturity models to solve for those blind spots—including robust leadership succession planning. Think in terms of a window of three to seven years. How will the company diversify its business and where should roles and skills be upgraded? Consider the board’s skill sets and capabilities, as well as future needs. A sharp focus on performance is essential for both CEO and board succession planning.

Formally onboarding new directors

As one director noted, “Onboarding is critical, and I have been surprised at the number of private companies that don’t have formal onboarding. My experience taught me to ask for it, but a lot of CEOs and boards don’t think about it.” In our survey, “onboarding of new directors” was ranked among the lowest areas of board effectiveness. Orientation and onboarding can help new directors understand the business and the CEO’s expectations (including skill sets gaps to be filled and where the company is headed) and be more effective from day one. “For new directors joining a private company board, have a board buddy, ask for a thorough orientation and onboarding. Then attend every meeting for every board committee, if possible.”

It is clear from our survey work and ongoing conversations that private company boards continue to improve their effectiveness in areas including overseeing strategy and agenda-setting, communicating with management, conducting board meetings, and communicating among directors. Independent directors can be pivotal in helping private companies navigate the challenges ahead—from AI to geopolitical uncertainty to CEO succession.

At a time when CEOs and boards need to be challenging assumptions and widening their company’s aperture on strategy, risk, and talent, having independent voices in the boardroom can be game-changing. That said, simply adding an independent director to the board is not enough. Adding real value requires planning, work, and close collaboration among the members of the board, the CEO, and other company executives.

To find this article on our website, visit kpmg.com/us/blc.

Mark your calendar

HITEC's Spring Leadership Summit

May 7–9, Houston, TX

As part of the Hispanic Technology Executive Council (HITEC) and KPMG Board Readiness Program, KPMG will host a session on May 7 of the HITEC Summit to equip technology executives with the knowledge, skills, and strategies essential for boardroom success.

For more information, visit HITECGlobal.org.

NACD Battlefield to Boardroom

May 22–23, Washington, DC

NACD's Battlefield to Boardroom, sponsored by KPMG, is an exclusive board development program designed to prepare retired and soon-to-retire military general and flag officers to serve in the boardroom. Programming will cover topics ranging from boardroom basics to more complex issues such as strategy and shareholder engagement.

To register, visit NACDOnline.org.

KPMG BLC quarterly webcast

June 27, 11:00 a.m.–12:00 p.m. EDT

Join us for our quarterly KPMG BLC webcast as we discuss takeaways and trends from the 2024 proxy season.

To register, visit watch.kpmg.us/BLCwebcast.

KPMG Board Insights Podcast

On demand

Conversations with directors, business leaders, and governance luminaries to explore the emerging issues and pressing challenges facing boards today.

Listen or download now at listen.kpmg.us/BLCpodcast.

Selected reading

10 commandments for audit committees

Mayer Brown

CEO transitions in 2023

Spencer Stuart

NIST updates cyber framework

NIST

2024 KPMG US CEO Outlook

KPMG LLP

Shareholder engagement in 2024

Wilson Sonsini via HLS Forum

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