Executive Insights

Volume XIX, Issue 9

How Can Boards Find Their "Inner Challenger"?

Boards of directors play two roles. They must protect value by helping companies avoid unnecessary risks, and they must build value by ensuring that the companies change quickly enough to address emerging competitive threats, evolving customer preferences and disruptive technologies.

As technology and business model cycles become shorter and companies face unrelenting pressure to innovate or suffer the consequences, more and more boards need to focus on the second of these roles. To do so, they must be willing to challenge executive teams and stress-test their strategies to ensure they go far enough and fast enough. For boards used to preserving the status quo, this shift can be uncomfortable. Here are four ways boards can become better challengers and champions of change.

Confront unwelcome news or trends

Especially for successful businesses, changing strategy is extremely difficult. In the early 1990s, Blockbuster Inc. commissioned one of several studies on the future of video-on-demand technologies and how these would impact traditional video rentals. The report concluded that expanded cable offerings and broadband Internet would begin to impact video rentals around 2000, and would grow rapidly thereafter. The good news was, Blockbuster had a good 10 years to prepare for the new environment. But the shift never happened: Management ignored the study's findings and continued with the same strategy, supported by the board. In September 2010, Blockbuster filed for bankruptcy protection. In this case, value protection was not enough. The company had clear notice that seismic change was coming. The board's role was to acknowledge the warning signs and challenge management's lack of action — even if this meant contention and dispute in the boardroom.

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Make sure you have challengers in your midst

Boards will be far more effective in their challenger role if they offer seats to individuals with professional experiences and viewpoints that are very different from those of the executive team. Directors can learn to be more direct with management, but it's hard to fake contrarianism when everyone is of the same mind. When a board resembles the CEO in mindset and outlook, it's a recipe for a gatekeeper board, not a challenger board. On the other hand, when boards mix it up by bringing in members with different perspectives, they can effect powerful strategic changes, something I have seen many times in my work with corporate boards.

Often, these "challengers" will be tech-savvy, young executives from digitally disruptive companies who can press their fellow directors and senior management about potential blind spots

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related to digital disruption. But disruption is not always about technology. For example, one highly successful privately held producer of canned foods actively sought a board member who could challenge management to think differently, but who would still fit with the company's family-oriented governance culture. The successful candidate was the CEO of a well-known, family-owned California wine business that catered to consumers who would not dream of buying canned prepared food. The board member helped the company "think outside the can" to identify new product forms that would broaden their customer base and appeal to health-conscious consumers.

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In another instance, a leading chain of retail pharmacies appointed as vice chairman someone with a background in healthcare manufacturing and pharmacy benefit management. The new board member helped management better understand the efficiency advantages of mail-order pharmacies, which rely on automation. As a result, the company added low-cost automated pharmacy services to its existing retail outlets, giving it a competitive advantage over more traditional retail pharmacies.

Stay fresh

Beyond accessing the right expertise, boards can maintain a challenger perspective by ensuring they don't become complacent and drift toward an approver role. One of the most effective ways to do this is to establish mandatory term limits as a part of the board's bylaws. Term limits can also help boards maintain a level of independence between the outside directors and executive leadership. Finally, if the CEO and chairman roles are separated, the chairman can take more active responsibility for ensuring that alternative views and perspectives are brought before the board. Separating the roles is common practice in Europe, and becoming more so in the United States. Another option is to appoint an independent lead director, a less drastic change that can have a similar effect. In fact, the New York Stock Exchange essentially requires listed companies with non-independent chairmen to appoint one of their independent directors as lead director. The lead director, among other duties, is responsible for scheduling and helming board meetings that take place without management. Today, the majority of S&P companies with combined CEO/chairman roles have chosen to counterbalance this arrangement by appointing an independent lead director.

Turn courage and candor into core competencies

It defeats the purpose of having directors with valuable insights if they do not feel comfortable sharing their perspectives and debating issues with management. A recent study by WomenCorporateDirectors (WCD) and Bright Enterprises Inc. found that more than three-quarters (77%) of director respondents believed that their boards would make better decisions if they were more open to debate, and 94% said that when criticism is used properly, it can help bring about change.

Nevertheless, board members are often hesitant to offer criticism, especially to CEOs. The same survey found that only about half (53%) of respondents felt the CEOs of the companies on whose board they sat took criticism well. This is not surprising. As a board member it is much easier to empathize with the feelings of a CEO under pressure than it is with an abstract group of shareholders. One way to address this issue is to offer board members training in both giving and receiving constructive criticism. Board members need to understand that failing to confront difficult issues will not help the CEO. If a CEO's first indication that the board is dissatisfied is hearing they are searching for his or her replacement, then the board is not fulfilling its own responsibilities.

Challenger boards are those with the strength to put the hard questions to management and poke holes in suboptimal strategies. At the same time, they bring a diversity of perspective that can help management understand the company's vulnerabilities and how to overcome them. For companies struggling to exist in a world where disruption is rapidly becoming a business constant, challenger boards may well be one of their most important survival tools.

About the Author

Stuart Jackson is L.E.K.'s Global Managing Partner and a member of the Global Leadership Team. Stuart is responsible for directing the firm's global strategy and operations. In his leadership capacity at L.E.K., Stuart has worked with hundreds of clients in industries such as medtech, manufacturing and consumer products. These clients have enjoyed higher growth, increased their profit margins in existing businesses, added scores of new services and products, and completed more than 100 merger and acquisition transactions.

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