

Preface

Life short, art long, opportunity fleeting, experience misleading, judgment difficult.

Hippocrates, 400 BCE

In 2400 years nothing has changed in human nature, but everything else has. The first quarter of the 21st century has witnessed colliding waves of change from every direction – social, political, economic, technological, demographic, legal, environmental. The momentum of change, its mass and velocity, is accelerating exponentially. We are in an era of extreme uncertainty, complexity, and instability.

One result of all this change is that corporate life is getting much shorter. Since 1957, the average life expectancy of an S&P 500 company has declined by more than 70 percent, and it is still falling.¹ Today's organizations may have shorter life spans because conventional collective decision-making processes cannot keep pace with the external rate of change.

This manifests itself in several ways. There are numerous examples of boards (and their executives) who did not recognize and seize upon existential external opportunities, which later became existential threats. Others recognized the need for change but failed to execute the needed changes. Others failed to detect internal control weaknesses and fraud. For example, between 1999 and 2010, chief executive officers (CEOs) or chief financial officers (CFOs) were involved in 89 percent of U.S. Securities and Exchange Commission (SEC)-prosecuted fraud cases.²

This is despite numerous governance reforms over the past 50 years that have focused mainly on board structural issues, such as independence, composition, and director tenure. Those reforms, while necessary, were not sufficient, as they tended to prioritize form over substance in collective decision-making processes. The board's function is to make effective decisions. Form should follow function, not the reverse.

Conventional governance has tended to approach decision-making in isolation rather than as a system. Currently, there is no comprehensive framework for adaptive governance to enable and accelerate the board's collective decision-making functions and powers. There is no coherent and practical way of better organizing the board's most valuable and irreplaceable resource: its own time.

The nature of business and the "rules" are changing. What worked in the past may not work today and in the future. Judgment is indeed difficult. Creative destruction is alive and well. Organizations succeed by creating, delivering, capturing, and protecting value. When they cease to do so, they fail. The overarching duty of every board is to enable its organization's success despite uncertainty, complexity, and inevitable adversity.

If longevity is the measure of adaptation, many boards have failed and will likely continue to fail despite their best efforts. Directors are spending more and more time on board matters and are being inundated with more and more data. It is unlikely to help and may even exacerbate the situation.

Boards, by their nature, must make decisions collectively. Assuming the directors of failed companies were smart and well-intentioned, what went wrong? If whether to adapt or fail is the overarching governance question, then how best to adapt?

People and organizations are not perfect and cannot be perfected. Sooner or later, all will succumb. But can this be forestalled? Can more value be created, delivered, captured, and protected? Can corporate longevity be increased? What lessons can be learned from the successes and failures of others?

Will your organization adapt or fail? That is the existential governance question.

Our motivation for writing the book. While complex systems tend to fail in complex ways, a practical framework for adaptive governance to enable a board's collective decision-making need not and must not be complex itself.

This book is aimed at directors of boards of organizations large and small, complex and simple, for-profit and not-for-profit. The focus is on the board's powers and role and only indirectly on the executives' and third parties' roles. For example, when we discuss the key decisions that require board approvals, we discuss the board's role in seeing its due diligence requirements are met but not the roles of executives and others in performing such due diligence.

The book is also aimed at executives, corporate secretaries, internal auditors, and others who frequently work with the board to help improve their ability to support and enable achieving a common and synergistic understanding of reciprocal roles and expectations.

The 21st-century acceleration of change poses both greater threats and greater opportunities. Rapid adaptive choices demand situational awareness and decision discipline. Once the opportunity to adapt has passed, good choices were either made or not. Only time will tell. That is why we wrote this book.

The structure of the book. We know directors' and executives' time is extremely limited. We have tried to structure the book to make it easier for you to skim and then dive in where you are interested. Each chapter begins with a summary of Lessons Worth Learning.

Chapter 1 describes why boards and their organizations must adapt or fail and why a framework for adaptive governance is needed.

Chapter 2 ("A Framework for Practical Adaptive Governance") describes five essential powers common to every board and a practical process and principles for Adaptive Governance.

We describe five steps in systematic and deliberate adaptation:

1. Detect signals (external/internal)
2. Interpret (as threats or opportunities)
3. Respond (experiment/innovate)
4. Learn about the effectiveness of the response (better/same/worse)
5. Adapt as necessary

We then dedicate a chapter to each of the five essential powers common to all boards:

1. Conduct the business of the board.
2. Set direction and policy.
3. Approve key decisions, then prudently delegate.
4. Oversee the execution of direction within policy.
5. Verify the reliability of advice and information before trusting.

While the book proceeds linearly, all the powers are interdependent and interactive. There are feedback loops. Each power requires input and feedback from every other power and decision discipline.

Other than the conclusion, each chapter begins with a high-level summary of lessons worth learning that allows you to pinpoint your areas of greatest interest. It asks critical questions that every board should always ask of itself and others in exercising each power. The questions are intended as examples to frame the discussion and are not intended to be exhaustive. In answer to those questions, each chapter presents case examples and lessons worth learning from the successes and failures of others and practical tools for use by boards and executives.

Our goals are to help make your job easier, help you and your board become more effective, and make the highest and best use of your limited and valuable time. We offer our opinions based on our research but particularly with regard to our experience as board members, consultants, academics, and authors studying organizational governance. Our recommendations are, of course, subject to our own unavoidable biases. We don't expect anyone to adopt everything we recommend. Take what you will.

One size fits one! We believe that, if acted upon, a more disciplined exercise of a board's five essential powers combined with a systematic and deliberate process for adaptation can help drive sustainable value creation. Since we're dealing with the real world, we rarely can isolate a result and trace it back to a single factor. Instead, we suggest a hybrid approach of symmetric and asymmetric strategies to improve the chances of successful adaptation.

We provide a framework for improving collective decision-making in extreme instability. In today's highly volatile environment, how do people of good intent, with a common purpose, more quickly agree on how to make decisions collectively and then develop the discipline to carry them out in the face of inevitable adversity? Adaptive boards agree on how collective decisions will be made, stick to it, and improve it. How well does your board perform? We have provided a short Self-Assessment at the end of the book.

Of course, no one joins a board to fail. Most directors come to boards with a track record of success and no doubt wish this to continue. But success requires knowing how to learn, change, and adapt to changing conditions to drive sustainable value. If that is your goal, then this book is for you.

Extinction is the rule. Survival is the exception.
Carl Sagan, American Astronomer and Planetary Scientist