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SAY GOODBYE TO GROUPTHINK

Diverse and outspoken boards prevent passivity—and prime companies for better decision-making.

By Sarah Fister Gale

When a boardroom is little more than an echo chamber for the will of a single voice or an unwavering mission, complacency—and failure—often follow.

Take the rise-and-fall saga of blood-testing startup Theranos. Led by CEO Elizabeth Holmes, the Silicon Valley company—once valued at $9 billion—had a meteoric rise on the biotech scene, garnering an abundance of buzz and money alike. Ms. Holmes landed Theranos a high-profile partnership with Walgreens and became a darling of the business world, gracing magazine covers and landing a slot on *Time*'s Most Influential People list.

But the kingdom came crashing down when *The Wall Street Journal* published a 2015 report discrediting the validity of Theranos' technology. More than 32,000 of the company's blood tests were declared void, Walgreens filed a suit and the company's valuation bottomed out.

What went wrong? One big factor was the company's lack of transparency—its technology was never peer-reviewed or fully verified by the U.S. Food and Drug Administration. But fault has also been placed with the company's board, which was packed with big names like Henry Kissinger yet lacked expert representation from the life sciences or health care community. Without that, the board failed to fulfill key functions of its role, including pushing back on strategy and scrutinizing data.

"There are no sitting chief executives [from] other companies—a basic tenet of board best practices," wrote *Fortune* senior editor Jennifer Reingold about the company's board at the time. "There is but one still-licensed medical expert, Bill Frist ([William] Foege, age 79,

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is retired). And while it's probably useful to have a retired government official or two to teach and offer good leadership skills, when there are six with no medical or technology experience—with an average age, get this, of 80—one wonders just how plugged in they are to Theranos' day-to-day activities. Nor is there anyone with formal accounting or auditing expertise or legal expertise, which may now become an issue, based on the questions raised in the [*The Wall Street Journal*] article."

Since the scandal erupted, the board has undergone a major restructuring, but the original incarnation seemed to largely follow Ms. Holmes' lead. It succumbed to groupthink, not an uncommon board affliction. Enron, Olympus, Volkswagen and Toshiba all suffered major scandals, and in each instance their respective boards were criticized for unquestioning conformity. One powerful bulwark against groupthink: a culture that embraces cognitive diversity.

WANTED: SPRING CHICKENS

Diversity of thought starts with diversity of people. An overly homogeneous board, made up of like-minded people of a similar age, experience and ideology, is insulated from the wider world and lacks objective viewpoints, according to Fause Ersheid, an economist and senior corporate governance analyst and researcher at the Abu Dhabi Center for Corporate Governance in the United Arab Emirates.

And with such uniformity comes great peril.

"Homogeneous groups run the risk of narrow-mindedness and groupthink (i.e., premature consensus) through misplaced comfort and overconfidence," lead author Adam Galinsky and colleagues wrote in a 2015 report published by the Association for Psychological Science. "Diverse groups, in contrast, are often more innovative and make better decisions, in both cooperative and competitive contexts."

Much has been made about the business value of gender and racial diversity. A report from nonprofit Catalyst, for example, found that Fortune 500 companies with the highest representation of women board directors attained significantly higher financial performance, on average, than those with the lowest representation. But age diversity also matters in dismantling groupthink.

The average age of all S&P 500 independent directors rose to 63 between 2010 and 2015. This does not bode well for the many companies trying to appeal to young customers in a rapidly evolving, technology-driven business environment, Mr. Ersheid says.

ROCK THE BOAT

Simply establishing a diverse board guarantees nothing unless members are empowered to point out flaws and missteps. And that culture must be defined from the top.

When Jane Chwick joined the board of directors at Voya Financial, an $11 billion investment and retirement firm, in 2014, she was asked to join the finance committee. It made sense: Ms. Chwick spent 30 years at

"As a board member, it's your responsibility to take action, even if it's difficult."

—Jane Chwick, board of directors, Voya Financial

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Goldman Sachs before retiring four years ago. But the majority of her experience was based in technology, not finance. Yet she soon discovered she had among the strongest financial backgrounds of anyone on the committee. "I knew enough to ask the right questions, but I also knew we needed to add depth," she says.

So she brought her concern to Voya CEO Rodney O. Martin Jr. "He was incredibly receptive to that input," Ms. Chwick says. He immediately added two new members with deep financial experience to the board. Mr. Martin's willingness to acknowledge shortcomings not only helped plug potential holes, but also nurtured an environment where criticism is not just heard, but valued and acted on.

A board that cannot communicate dissent has a real problem, says Beth Stewart, a former board director for CarMax, General Growth Properties and AV Homes Inc. "The main thing boards need are people confident enough to be willing to speak up when it really matters," says Ms. Stewart, CEO of New York-based Trewstar Corporate Board Services, a search firm that focuses on placing qualified women on Fortune 500, mid-cap and private equity boards.

Creating an environment that encourages everyone to express opinions—which describes Voya's board—is critical. This becomes more complicated, however, when the board has a dominant leader accustomed to being in charge, Ms. Chwick says. But such pressures are not an excuse for board members to be complacent. "If the CEO won't listen to the board's advice, it's the board's job to fix the situation," she says. "If you can't make people pay attention when you see a problem, then maybe you should question your value on that board."

A critical examination of strategy and

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C-suite decisions should not be limited to times of obvious trouble. Board members must be willing to question the status quo even when things seem great. "During the global financial crisis, everyone in the financial services industry knew bundled subprime mortgages were very risky, but no one raised a flag," Mr. Ersheid says. "Because of groupthink, board members closed their eyes. No one wanted to rock the boat when everyone was making a profit."

No doubt, board members must walk a fine line.

"If a company is doing well, you don't want the board to be constantly raising alternative ideas just because they think it is part of the job description," Ms. Stewart says. "However, there needs to be a balance. Board members must be knowledgeable and willing to engage when companies are faced with critical decisions—for instance, about things like executive hiring and compensation, mergers and acquisitions or strategic operational issues."

THE LIMITS OF LIMITS

Some organizations are introducing term limits to ensure boards avoid the same old, same old syndrome. "New board members bring a fresh perspective that can break the groupthink mentality," Mr. Ersheid says.

Term limits can also help independent directors stay that way—and continue to battle groupthink by taking a more objective stance, he says.

In France, for example, directors are no longer considered independent if they have served on a company's board for more than 12 years. And in the United Kingdom, publicly traded companies must either terminate a director after nine years of service or make an argument as to why the long tenure has not compromised his or her independence. This practice is less common in the United States. Only 13 S&P 500 companies have imposed term limits for non-executive directors, according to the 2015 Spencer Stuart Board Index. However, 69 percent say they have a strategy to encourage regular board refreshment.

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Companies opposed to term limits often argue that changing the board every few years means they lose the benefits a tenured board brings to decision-making. A 2015 study from Sydney, Australia-based University of New South Wales found companies with a higher proportion of experienced directors were:

- More likely to change CEOs when performance faltered
- Less likely to misreport earnings intentionally
- Less likely to make acquisitions, which often expand a CEO's power while diminishing shareholder value

Ms. Chwick, however, argues term limits for boards are often simply "an easy way out of having tough conversations." Boards need to create an environment where everyone is comfortable calling out members not performing effectively—whether that person has been on the board for two years or 10. "As a board member," she says, "it's your responsibility to take action, even if it's difficult." **IQ**

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