WHY BOARDS MAKE BAD DECISIONS

BY MARTIN COYNE

It was a multibillion-dollar multinational manufacturer, and I had been on the board for less than a year. The company's performance was already pretty poor when, finally, the board replaced the CEO and brought in an "industry expert." Instead of a more conservative growth strategy, the new CEO promptly proposed a major acquisition to capture market share in new customer segments, many of which were in high-risk technology. The acquisition was supposed to be based on his apparent industry knowledge and relationships. In reality, this was a "bet the company" deal.

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From there, the CEO convinced the board chair of the deal's value and together they set out to convince the remaining board members. The CEO presented only facts that supported the deal. He had based the deal on his expert knowledge and made the business case based on older assumptions of market growth that the board had already reviewed nine months earlier. Basically, his approach was: "Trust me because I'm the expert and I know more than you do." He identified some obvious risks, but patiently assured the board that he understood those risks and would have them all under control and well monitored.

This experience taught me a lesson in how boards ought not to behave.

The board chair called individual directors to "gather questions and concerns" but actually used the conversations to convince directors individually of the value of the deal. At the next board meeting, where the vote would be taken, there was little discussion, and the chair called first on those directors who supported the acquisition. He placed non-supportive or skeptical directors in the position of bucking the crowd. To vote against the deal meant not being a team player.

Ultimately, the deal was a disaster, missed all of the revenue and earnings projections, and distracted management and the board. After a major decline in market capitalization over several years, a competitor acquired the company for a fraction of its previous value. This experience taught me a lesson in how boards ought not to behave.

Bluntly speaking, boards make bad decisions because directors are not doing their jobs, individually and collectively. The bad decision gets all of the press, but what precedes the faulty assessment is the real root cause.

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In my experience on boards, poor corporate performance over an extended period of time creates the pressure that leads to notable bad decisions. When company performance lags behind the competition and does not create sufficient value for shareholders, management and the board feel they must increase risk to make up for lost time and value. To that end, they do dumb things. They make poor choices and take unnecessary risks all because they didn't properly execute their oversight role over an extended period of time.

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Most board members will say this would never happen to their board or their company. But given the notable board failures in recent years, we can't ignore what happens to major corporations when growth slows and the pressure is amped up.

In the late 1990s, for example, the Hewlett-Packard board brought in Carly Fiorina to turn around poor performance. Reputed to be a marketing and sales guru and people person, she bought Compaq Computer to offset HP's slowing computer and printer business and market-share losses. The $25 billion deal failed, and Fiorina eventually was fired. Later, when HP faced another crisis with the personal-conduct issues surrounding their new CEO, Mark Hurd, the board replaced him with Leo Apotheker from SAP. When Apotheker was hired as CEO, many of the board members had never met him. He performed so poorly he was dismissed 11 months later. He was the third consecutive outside CEO hired by HP—all failures. The board had never put in place any serious CEO succession plans.

I witnessed similarly bad decisions when I worked at Kodak, an iconic brand that failed to recognize and embrace the digital photography revolution. Management

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made bad choices, but the board did little to push the company in the right direction.

The list of really bad decisions, reviewed and approved by each respective board, is long and varied, but there are some important commonalities. In every case, business performance had been lagging for several years, and the pressure to perform increased quarterly. CEOs were not held accountable for their performance and for developing qualified successors. Finally, the directors postponed making the difficult decisions that had to be made regarding people and performance. Delaying these decisions only made them harder, not easier.

Because the directors on these boards did not mandate strong operational performance, did not ensure there was a valid and sustainable long-term growth strategy, and did not have the right leadership team in place, business performance stagnated and began to deteriorate. If they had done their jobs well when things were not so dire, these risky decisions could have been avoided, or at least the risk reduced.

As directors, we need to ask ourselves: Are we doing the right things to continuously increase value or are we just being collegial by not making waves? Boards must have an effective decision-making process in place that negates the personal biases that affect how decisions are made. Collectively, these biases can lead a board to decisions that may appear logical but are in fact destructive. Boards need to ask the right questions, anticipate the consequences, and define specific milestones and checkpoints to evaluate executional performance for any key decision.

Boards that avoid the due diligence and deep analysis required of them will inevitably make bad, and sometimes catastrophic, decisions.

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