Innovation starts in the boardroom

If fostering innovation is one of the board's objectives, a good place to begin is with the board itself.

By Beverly Behan

Innovation is one of the hottest topics in global business today. Everyone and every company is striving to be "more innovative." The role and focus of the board in innovation can vary dramatically with the nature of the company it oversees:

• In high-growth entrepreneurial companies, boards often view their role as guiding innovation. Typically they are seeking to enforce more accountability and discipline in a highly entrepreneurial company — without dampening the innovative spirit that lies at the heart of the corporate culture.

BOARD ENTRENCHMENT IS A NATURAL ENEMY OF INNOVATION.

• In more-established companies, boards sometimes seek to stimulate greater innovation. While the board's choice of CEO has the most direct bearing on these efforts, many directors wonder what more they can do to reinforce and sustain a tone of greater innovation at the company they oversee.

It is not board's job to drive innovation. This is the job of management once the board has given the CEO that mandate. The role of the board is to facilitate innovation — by creating and supporting a corporate environment that fosters innovation, ensuring that the board is comprised of directors who can knowledgeably advise and question the company about the impact and risks of innovative strategies, and by developing a boardroom culture consistent with a tone of innovation.

Accountability vs. risk tolerance: A boardroom balancing act

When it comes to fostering an innovative corporate environment, the board plays a critical role in striking an appropriate balance between accountability and risk tolerance.

In entrepreneurial companies, one of the most productive ways for a board to inject greater accountability is often by working with the CEO to establish clear performance goals. The most meaningful goals address the "must-win battles" — what the company has to do in order to either stay alive or get to the next stage of growth. Once agreed upon, if the goals are not achieved the board needs to ask why: Is the company too scattered, with too many things on the go? Have resources been diverted? Should the strategy be modified? Should chang-

Beverly Behan is the author of *Great Companies Deserve Great Boards* (Palgrave MacMillan, 2011). She has worked with more than 130 boards over the past 18 years through her consulting firm, Board Advisor LLC in New York (www.boardadvisor.net), and recently designed a program on "The Role of the Board in Innovation" for the Malaysian Directors' Academy.

es be made in executive roles or new management talent recruited?

In traditional companies, the issue is typically one of risk tolerance. Often, the board is more comfortable allowing the CEO to take a few "small bets" on innovative ideas or projects considered less risky because of their size and scope. Victories achieved with these smaller ini-

Private companies need boards focused on innovation, too

Proposal: An innovation subcommittee of the board.

By Tracy Warren

Innovation is the lifeblood of high-growth, private companies. With a three-to-five-year time horizon to major growth inflection points, these companies must aggressively pursue strategies in all aspects of business. Boards must support innovation efforts not only in product development but also in sales and marketing (e.g., the implementation of social media engagement to reach and retain customers), finance, and all other areas across an organization.

While boards of emerging companies tend to be small in number, experience shows that creating a science and technology (S&T) subcommittee — or an innovation subcommittee — of the board is highly effective in providing insight and accountability to such efforts.

The S&T subcommittee should also be small in number, nimble and full of diverse skill sets. Ideally, the subcommittee is led by an independent director with knowledge of the company's market sector who not only can provide insight on product development innovation but also has the historical knowledge of the workings of a market sector necessary to evaluate sales strategy and even finance. In many cases, the model profile is that of a former C-level executive of a major player in the company's space who can dedicate ample time to engaging and building rapport with the executive committee.

The S&T subcommittee might also include an investor-director who has made investments in adjacent or complementary sectors and can provide a unique perspective in how other companies in the value chain for a particular market are evolving.

Given the variations in sizes of private company boards, it is recommended that 20% of the directors serve on the S&T subcommittee, recognizing the diverse and far-reaching elements of innovation and its role in defining a company's future.

While the S&T subcommittee may not have voting power, its influence is in acting as a sounding board to management in its quest for innovation and market superiority. Incentives, processes and implementation strategies for innovation can be challenging for emerging private companies, as they are under pressure from stakeholders to execute against particular business plans. However, the pace of high-growth industries requires innovation to remain a critical component of a company's research, development and even sales efforts.

An S&T subcommittee can also step outside an organization's existing business (technology/initiative) and address barriers or roadblocks within the organization, including culture, process or technological limitations. Consistent with good board practices, the S&T subcommittee itself should have term limits to maintain its relevance and continue to offer fresh insights into the marketplace and technology areas.

The S&T subcommittee should have access through management to customer feedback at varying points of a company's life cycle to confirm innovation effort results; provide new direction, as necessary; and demand accountability. Innovation should engage customers more fully, open new markets, or expand a company's reach into an existing space. The S&T subcommittee is motivated to support the company's efforts to demonstrate market leadership and/or technical acumen where necessary in a given sector.

For emerging, high-growth companies, a high-quality innovation effort supported at the most senior level of the organization can determine success or failure. A board's role is to evaluate management's strategy, provide insights on market forces, and assist in assessment of opportunity costs in innovation within the organization. Establishing an S&T or innovation subcommittee of the board elevates innovation to a top priority of management and the company as a whole.

Tracy Warren *is a general partner of Battelle Ventures and its affiliate fund, Innovation Valley Partners, for which she focuses on investments in health and life sciences as well as emerging energy technologies. She has co-founded and serves as a board member of several life sciences companies, advises on new company formation, mentors female entrepreneurs, and provides other early stage leadership to private growth companies.*

tiatives can then be used to "move the needle" on innovation within the larger organization — and with the board itself.

If something new or innovative is attempted that doesn't succeed, the reaction from the board is critical. Is it: "Fire those responsible" or "OK, you messed up, so try again"? Unless some tolerance for failure begins to permeate the culture, all those corporate screen-savers flashing the word "Innovate" will achieve little more than eye rolling. And those culture-forming decisions are often discussed — if not made — in the boardroom.

Quick fixes intended to stimulate innovation can sometimes have significant drawbacks. One board approved a new compensation scheme designed to provide financial incentives for "innovation"; 25% of the strategic goals involved investments in non-core business lines. In response, executives began proposing ideas to get the money and make their "quotas" — ideas that were neither well considered nor financially viable.

Is board composition designed for innovation?

The board's role in both fostering and guiding innovation involves asking the right questions of management rather than dictating "what's to be done." This can only be accomplished with the right team of directors at the board table.

Some key questions to ask about board composition are: Does the board have the capability to really advise the company as it makes changes to its strategy or business model? And to see and understand the key risks inherent in these sorts of changes? Is board composition sufficiently diverse that directors will be able to offer perspectives on a broad range of issues that will need to be addressed for these changes to be successful?

Traditional companies that aspire to be more innovative should consider the benefits of specifically recruiting one or two directors who have run or served on the boards of highly innovative companies and understand their issues and operating environments. These types of directors can bring an entirely different point of view and tangible experience to boardroom conversations about innovation. This background is even more crucial at the board tables of high-growth companies; entrepreneurial CEOs and CFOs understand the trajectory and issues that these companies will be grappling with and can make significant contributions in addressing them.

Does the board set a tone of innovation?

The board's choice of chief executive officer — and the tone which that leader sets at the top of the company — clearly has the most significant impact in creating a climate of innovation. But the board environment, itself, is also a factor in setting the "tone at the top," one that is far too often ignored.

> MANY BOARDS PROUDLY DESCRIBE THEIR CULTURE AS "COLLEGIAL"; VERY FEW INNOVATIVE COMPANIES WOULD DESCRIBE THEIR CULTURE THAT WAY.

Innovative companies are typically characterized by vibrancy and passion. Yet many board meetings are so structured and formal that the boardroom climate appears disconnected from the rest of the organization: Directors occupy the same seats, the agenda goes relatively unchanged, and "death by PowerPoint" hangs in the air. Many boards describe their culture as "collegial" — and often that's said with pride. But very few innovative companies would describe *their* culture that way.

If fostering innovation is one of the board's objectives, a good place to begin is with the board itself. What changes would stimulate a more innovative and vibrant board culture — one that reflects the innovative tone the board wants to see throughout the company? Boards of highly innovative companies who are trying to instill accountability might consider some of their board practices through a similar lens. For example, are directors renominated year after year, even if their contributions are marginal? Entitlement and entrenchment are the natural enemies of innovation.

Every day, boards make decisions that can either cultivate or suppress innovation in the companies they govern. These range from major decisions, such as the choice of a more innovative or entrepreneurial chief executive officer, to smaller ones, such as tolerating repetitive board agendas largely focused on compliance issues. While the board's focus may differ with the nature of the company it governs, the tone and pace of the innovation in any organization truly begins in the boardroom. ■

The author can be contacted at beverly.behan@boardadvisor.net.