Navigating disruptive risk: The lead director lens

By Dennis T. Whalen

Envisioning a company's future is hard and imprecise work. But it's increasingly clear that dedicating time to think about the future is vital to navigating the disruptive risks that are shaking up industries and upending business models.

During the NACD Lead Director Symposium, sponsored by the KPMG Board Leadership Center, we explored the topic of disruptive risks—such as technological innovation, the Internet of Things, the digital economy, demographic changes, and ecosystem changes—that may threaten the core assumptions underlying a company's strategy and business model. Approaching the topic from their perspective as board leaders, some 80 lead directors and independent chairs discussed the challenges they face as they lead their boards in helping the company identify and assess disruptive risks and as they prepare to calibrate strategy and change course as needed in an increasingly disruptive business and risk environment.

One of the important insights we heard was an articulation of the key challenge that these disruptive risks pose for boards today: obtaining a view or picture of the future and how that future may impact the company's strategy. What will the business or industry look like one, three, five, or more years from now? What will be the impact of these disruptive forces on the business or industry, and what risks will these forces pose to the company's strategy? By gaining a better understanding of the future of the business—the risks and opportunities—boards are better positioned to provide oversight and guidance on the company's key governance activities: setting and calibrating strategy, monitoring execution, and managing strategic risks.

Our dialogue with the lead directors generated a number of practical suggestions—echoing several of the recommendations made by the *Report of the NACD Blue Ribbon Commission on Adaptive Governance: Board Oversight of Disruptive Risks:*

Encourage the board, CEO, and senior management to develop an understanding of the disruptive risks that threaten the continuing viability of the assumptions underlying the company's strategy and business model. What are the most critical assumptions underlying our strategy? What disruptive forces have impacted our industry or adjacent industries, and what lessons can we learn?

Make clear that it is management's job to educate the board about these disruptive forces and the risks they pose to the company's business model and strategy. What information does the board receive from management about disruptive risks? Do their reports provide a forward-looking view of changing business conditions and potential risks? Who takes part in the discussions about disruptive risks? Are outside perspectives being heard?

Insist on an assessment of the company's ERM (enterprise risk management) processes, with a particular focus on how these processes help the company to detect and assess early-warning signals that may indicate disruptive risks on the horizon.

— Does management have regular, systemic mechanisms in place to accelerate the pace of detection of early-warning signals? Do we have people from outside, who bring very different experiences and perspectives, involved in the process?

— Do we engage expert partners to scan for subtle indicators of change, and to provide trend analyses?

— How can we enhance our risk prediction and scenario-planning capabilities?

— Do management and leadership have the talent, skills, and training to manage disruptive risks?

With committee chairs, reassess board and committee structure and processes for overseeing disruptive risks.

— While the full board has responsibility for overseeing strategic risks—and disruptive risks are generally strategic risks—board committees have important oversight responsibilities as well. And committees can bring increased focus and attention where required. Which board committee has responsibility for overseeing each of the disruptive risks management and the board have identified as posing a threat to core strategic assumptions?

— Which committee should oversee management's ERM processes generally—and particularly the adequacy of ERM processes to help the company detect and assess early-warning signals that may indicate disruptive risks on the horizon?

— Is ample committee and board agenda time devoted to disruptive risks?

— How does the board stay abreast of company and industry developments between board meetings?

As part of the board evaluation, assess whether the board has the "right" composition and culture (in addition to the "right" structure and processes) to provide effective oversight of disruptive risks.

Gaining a better understanding of the future—and the potential impact of disruptive forces on the business and industry—won't enable the board and management to predict or prevent all disruptive risks, but it will provide greater agility and help position the organization to effectively manage and respond to disruptive risks that do arise.

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