



Part Two:

# Culture as Governance and the Link With Performance

# The Evolving Role of the Corporate Board:

Culture as Governance and the Link With Performance

## Key Summary Points

1.

One of the most powerful insights drawn from my experience in business leadership is that if you are going to run your business like most businesses are run, it is only reasonable to expect you'll end up like most businesses – underperforming, and very likely failing. It is just a matter of how severe the setbacks will be and when they will show up. The best corporate boards will acknowledge these realities and look beyond the conventional management practices of their peers and competitors. They will seek advanced understanding and engage in practices that few others embrace.

2.

The rarity of sustained superior performance is the most challenging issue directors face. Working with this challenge and moving the needle in the direction of superior performance isn't a matter of additional compliance-based governance, as some governance advocates argue. It has little to do with director demographics, terms, recruiting processes or even diversity, although these factors are all important in different ways. The answers lie elsewhere. Governance and the role of the board must be grounded in the

reality that our authorities implicitly reflect a responsibility for performance. Governance must be reconceptualized to encompass all systems of control that drive performance.

3.

One central system of control and influence that links with performance is the culture of the board and the organization. The challenge for directors is to deeply understand the dynamics of how to create and sustain great culture. Unfortunately, most of us resist the necessary learning and justify our disinterest with some version of the view that culture has little to do with results. This is understandable given the invisible and intangible nature of culture. However, these leaders today are arguably being left behind. There is now a vast body of empirical research that clearly evidences the ways in which culture is a key driver of performance. If we embrace performance as an imperative we will be drawn to understand that "strength of culture" must be a strategic priority. This is in fact a mark of advanced leadership.



Mac Van Wielingen

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## 4.

The culture of a board of directors can be seen as an informal system of governance that directs and controls the material fundamentals of an organization. It's a system of social control that encourages desired behaviour, while simultaneously discouraging undesired behaviour. These behaviours and underlying attitudes, beliefs, and values are present all the time in all our interactions and have powerful links to performance. The direct link with performance is primarily through quality decision-making. However, to appreciate this requires something of a wakeup call! We need to start with a clear understanding of director responsibilities.

## 5.

We can talk until we are blue in the face about the separation of board and managerial responsibilities, but the reality remains that directors have the authority and thus the responsibility to approve all decisions relating to the most material fundamentals of the company. The most notable are the level of acceptable financial risk, which involves the balance sheet and all material commitments that may create liabilities, as well as all significant capital allocation decisions. Strategic risk and value creation (or loss) are the critical factors that make or break a company. My contention is that board of director decision-making is almost always a causal factor behind an underperforming or failing company. It is hard to imagine otherwise.

## 6.

High-quality decision-making requires a robust, healthy social environment in which clarity and truth-seeking are ever present. The critical ingredient that must exist is a passionate search for unbiased objective understanding. Otherwise perceptual and cognitive biases, along with shallow understanding based on intuition and hunches, will rule the day. These biases and perceptual traps are beyond the "self-interest bias" upon which much compliance-based governance is focused. They encompass the "optimism bias," the

"confirmation bias," the "hindsight bias," and "groupthink" to name a few. These biases are always operating and create perceptual distortions that work against clarity and objective understanding. A great culture will root out such obscurations and impediments, thereby significantly improving the quality of decision-making, which in turn will translate into reduced risk and a higher probability of sustainable positive results.

## 7.

In addition to quality decision-making, there are other critical ways in which a board can have a positive value-creating impact. One is through active diligence, which entails continuously stress-testing assumptions and beliefs that underlie director or executive leader perspectives. This is one of the principal functions of the board. We are responsible not to passively accept and rubberstamp, but to challenge the espoused knowledge upon which decisions are being based and actions are being justified. Another fundamental link with performance relates to the "tone at the top," as it's often described. This involves living, and thereby modelling, the values and attitudes that support success within an organization. Ethics is a critical part of this, but it shouldn't stop there. The tone at the top should pertain to all the essential values and attitudes that are part of the culture that is needed to support enduring success.

## 8.

One of the most important questions we can ask is, "What does our culture need to deliver to support and sustain success?" What are the deliverables of great culture? One essential must have deliverable of great culture is a high level of collaboration, or what could be described as engaged partnering. Secondly, a performance-focused culture must also deliver a strong sense of ownership of responsibility and accountability for progress and impact. The third must have deliverable is what I call adaptive intelligence. This shows up as discernment and responsiveness to what is most important, and reflects an attunement to change. The fourth essential deliverable is commitment to a shared vision and

purpose. This is demonstrated through discipline and persistence, particularly in the face of adversity. There is an ample body of empirical research evidencing the importance of each of these must have deliverables of culture.

## 9.

When we're clear on the qualities of culture that are essential and must exist, the deficiencies will show up in glaring form and can be dealt with proactively, sometimes with just a nudge or some supportive feedback. Other times more drastic change has to occur. Left unattended, boards and organizations will drift into dysfunction that becomes so familiar as to feel normal. When serious underperformance or the realities of failure strike, it's usually painfully clear that "we made some bad decisions." But if we were unclear on the culture we needed, we will probably also be unclear as to what went wrong at the level of culture. Given the prevalence of underperformance and failure, and based on my experience and studies, it's hard to disagree with the "widespread sense that underperforming boards are the norm, not the exception."<sup>1</sup>

## 10.

The quality of experience among the directors and within the organization, and "strength of culture," must be a strategic priority. Developing and sustaining a great culture requires both explicitness and an unrelenting commitment among the directors and executive leaders. Otherwise our fate will be sealed. We will become like most others, eventually stumbling and falling, underperforming or failing, and the shareholders and all others impacted will rightfully ask, "Where were the directors?" Specific practices such as monitoring strength of culture are important, but where we are in relation to our responsibilities, and how we view and embrace our responsibilities, is the most important fundamental that will determine whether a board is adding value. If we understand our responsibility for quality decision-making and performance, we will be drawn to understand the importance of culture.

<sup>1</sup> Ryan, Chait, and Taylor, "Problem boards or board problem."

## Role of the Corporate Board and Performance

In my previous article, “The Evolving Role of the Corporate Board: Governance, Strategy, and the Imperative of Performance,”<sup>2</sup> I examined the role of the board from the perspective of its relationship to performance. The question asked was how the concept of board governance can be expanded in the direction of performance while honouring long-standing boundaries between director and management responsibilities.

Four broad systems of structures, authorities, and processes that direct and control a corporation were identified and examined. These consisted of compliance-based governance, which represents most current board processes and activities, serving the need for fairness and creating legitimacy; social-based governance or culture, which can be seen as a process of social control that links to performance through quality decision-making; strategy-based governance, which organizes and directs the commitment of an organization’s resources and is central to

value creation and risk management; and performance-based governance, which is a system of monitoring and accountability that encourages responsiveness and adaptability.

These systems of governance combine to offer a framework within which to explore the role and influence of the corporate board. Each system of governance can be seen as serving a specific purpose, based on a unique control mechanism, and each has a direct link with performance. This way of looking at governance is summarized in Exhibit 1.



## EXHIBIT 1

### Board Governance: Structures, Authorities, and Processes That Direct and Control

Focus	External Stakeholder Focus	Internal Focus with Direct Links to Performance		
Type	Compliance-Based	Social-Based	Strategy-Based	Performance-Based
Purpose	Fairness and Legitimacy	Stability, Cohesion, and Predictability	Directional Alignment, Consistency, and Integration	Accountability Over Drivers of Performance
Mechanism	Compliance and Disclosure	Adherence to Values and Norms, Social Acceptance, or Rejection	Strategic Risk and Capital Allocation Approval	Monitoring and Reporting of Progress
Performance Link	Antecedent Condition to Access Capital	Quality Decision-Making/ Influence and Modelling	Competitive Advantage, Effectiveness, and Efficiency	Responsiveness and Corrective Action
Summary Description	Compliance-based governance is concerned with structures, processes, and rules that are generally focused on minimizing the adverse impact of management and director self-interest. Compliance and disclosure confirm fairness to all stakeholders and create the legitimacy needed to access capital. The links with organizational outcomes and performance are minimal.	Culture creates an informal system of control that both limits undesirable behaviour and encourages desirable behaviour. The control mechanism is social acceptance, belonging, or rejection. The link with outcomes and performance is primarily through the quality of decisions made relating to the material fundamentals of the company. Active diligence and modelling also have a powerful impact.	Comprehensive system of control which creates coherence and a rationale for the commitment of an organization’s resources. The control mechanism is the approval of ‘strategic risk’ – primarily financial risk through the balance sheet. An additional control lever is through the approval of the capital budget. The quality and effectiveness of strategy links directly with performance.	A system of accountability that allows for clear monitoring of progress of the key drivers of performance. It is most powerful when the drivers are determinative of results versus actual reported results. The board can interpose its authority if necessary to request corrective action. This supports learning and adaptability, which links with performance.

<sup>2</sup> Van Wielingen, “The evolving role of the corporate board: Governance, strategy and the imperative of performance.”

The focus of the present article is on culture at the board level and the link with performance. This is being defined as social-based governance. The social environment, or what can be described as culture, can be thought of as an informal system of governance. Importantly, the dynamics involved must be considered in the context of the total organization, as the board is but a subset of the organization.

This system of governance, at the board level and through the organization, is comprised of shared values (what's important), shared norms (what's acceptable), and shared expectations (what's needed). Together, these represent a system within social experience – a “shared knowing” that guides, limits, encourages, or “directs and controls” behaviour and actions. Stanford professor Jesper Sørensen points to these realities based on decades of research: “Organizational culture defines a normative order that serves as a source of consistent behavior within the organization. In this sense, organizational culture is a social control mechanism.”<sup>3</sup>

Corporate governance, as it's currently understood and practiced, needs to expand to consider culture as governance – that culture itself may be seen by the board of directors as a system of governance that has far more powerful links with performance than conventional compliance-based governance. Although there is minimal research focused specifically on the culture of the board and performance, extensive research supports the link between organizational culture and performance.

A classic example of such research is that of Kotter and Heskett, who conducted a study of the strength of corporate culture

and performance over a ten-year period.<sup>4</sup> Their findings revealed that firms across various industries perceived as having strong cultures had greater average levels of return on investment, net income growth, and change in share price.

A more recent study is that of Keller and Price, who found a strong correlation between organizational health and organizational performance: “Companies in the top quartile of organizational health are 2.2 times more likely than low quartile companies to have an above median EBITDA<sup>5</sup> margin, 2 times more likely to have above median growth in enterprise value to book value, and 1.5 times more likely to have above median growth in net income to sales.”<sup>6</sup>

At ARC Financial, based on investing in over 170 businesses, we have also seen a strong relationship between performance and what we call “a culture of health and effectiveness.” Our success at ARC Financial is predicated on investing in quality leaders and leadership teams. We must have the knowledge to understand what drives effective leadership and organizational success. Through our own studies at ARC Financial, we have confirmed that all our top-performing CEOs share certain leadership and cultural fundamentals. Ethical leadership, humility, and a learning orientation are among the fundamentals most strongly correlated with performance.

Evidence of the relationship between strong culture and strong organizational performance is now incontrovertible. It is forcing many of us out of the darkness into a more progressive reality. The implications for corporate directors are profound. Why have we been – and why do so many of us remain – resistant to embracing culture as a strategic priority?

## Does Our Board of Directors Have the Culture Our Organization Needs?

There are many misconceptions and much partial understanding with respect to organizational culture. Some directors and executive leaders discuss it almost as if it's an indulgence and has nothing to do with getting results. They talk about culture as if it means simply being “nice to each other.” This view fails to appreciate that drive and an orientation toward results are aspects of culture.

Another common view is that culture is the “soft stuff,” and this is often expressed in a diminishing or derisive manner. Some will openly say that they struggle with the lack of concreteness and abstractness of culture, preferring the more tangible nature of numbers, physical assets, and business plans. This is understandable, but I often wonder whether these same people are uncomfortable on a personal level in dealing with behaviour and emotions, or what they refer to as the “touchy feely stuff.” Is it possible they are simply declaring that they don't have the confidence in their own knowledge and skills to take on what Edgar H. Schein describes as “the essence and ultimate challenge of leadership”?<sup>7</sup>

A common refrain from within the executive suite is that “we leave culture and all the human resources stuff to our human resources department,” implying that the development of culture can be delegated. I believe there is a subtle arrogance in this view, suggesting that it's perhaps beneath us as senior executives to get directly involved – “We have more important things to do.” The irony is, again as Schein states in describing the importance of culture, that “if we don't understand the operation of these forces, we become victim to them.”<sup>8</sup>

3 Sørensen, “The strength of corporate culture and the reliability of firm performance,” 72.

4 Kotter and Heskett, *Corporate culture and performance*.

5 Earnings before interest, taxes, depreciation, and amortization.

6 Keller and Price, “Organizational health: The ultimate competitive advantage,” 3.

7 Schein, *Organizational culture and leadership*, 2.

8 Ibid., 3.



## Most corporate directors spend most of their time on compliance-based governance, yet there is minimal evidence that this form of director involvement contributes to performance.

The perspective that culture is something that can be delegated is also common among directors: “Yes, I know that culture is important, but this is management’s job.” Interestingly, if this is management’s job, most boards nevertheless fail to adequately monitor management’s effectiveness in discharging this responsibility. This is despite the large and growing body of evidence linking organizational culture with performance.

Making matters worse, the majority of directors rarely look at the culture of the board as an explicit driver of performance. There are discussions about how the board operates but, in my opinion, there is a void when it comes to understanding board culture and the link with organizational performance. There certainly is a lack of explicitness as to what is needed from board culture to support performance.

Whatever one’s view of the importance of culture or how culture is developed, the fact is that there will always be a culture within your organization. There is no escaping this truth. As the over-used expression goes, “You can run but you cannot hide.” There’s a way of treating each other and a way of doing things within all organizations and social groups. Just as every organization has a culture, every board of directors has a culture that limits or constrains certain undesirable behaviour and supports or encourages other behaviour.

If we know that culture always exists, and if we know its relationship with performance, why not be explicit about the culture we want and need? How do we justify not being deliberate and explicit regarding developing a culture that’s critical to our long-term success? If we truly embrace our responsibilities as leaders in business,

I believe we have no choice. If we don’t develop and manage the culture we need, the culture that develops will manage us and we will become its victims.

It should be emphasized that the culture needed at the board level and within the organization is drawn from the same set of qualities. Indeed, the real power lies in the synergy and consistency of cultural conditions among the board and executive leaders, and more broadly throughout the organization. This isn’t a we-they thing. Whether or not our organization has the culture we need is an important issue. Equally important is the question of whether our board of directors has the culture the organization needs. This is a transformative question, and one that directors must ask themselves.

### Compliance-Based Governance Is Essential but Doesn’t Drive Performance

Compliance-based governance is essential. It creates a degree of certainty that self-serving behaviour will be kept in check, with decisions made on the basis of fairness to shareholders and all stakeholders. However, there is a problem. Most corporate directors spend most of their time on compliance-based governance, yet there is minimal evidence that this form of director involvement contributes to performance. In fact, I agree with the view of some researchers that this type of governance is more of “a qualifier rather than a differentiator.”<sup>9</sup> It’s what we have to do to be “in the game,” to raise capital, and receive the support of our capital providers and stakeholders.

The difficulty is that while directors are preoccupied with compliance-based activities, opportunities may be missed –

or worse, the insidious forces of decline may take hold. This sounds bleak, but it’s an empirical reality that most businesses, whether small or large, eventually underperform and fail.<sup>10</sup> It’s merely a matter of when, and what the resulting damage will look like.

You may be a director of a company in which all the compliance-based boxes are checked and the company is receiving moderate or high ratings for its level of governance. Yet the probability is that decisions are being made – or not being made – that will prove to be adverse to the long-term outlook of the business. In due course the inevitable happens. Performance starts to deteriorate, and the board is faced with the decision to replace the CEO, restructure, merge, or pursue a sale transaction. Such situations invariably involve a loss of wealth through either chronic underperformance or a colossal wipe-out often seen in near or outright failures.

Is there a risk that corporate directors may be (unconsciously) hiding out in compliance-based process which, in a way, may feel quite comfortable and safe? After all, this is what the regulators and so many major investors appear to be requesting – more and better compliance-based governance. This type of work is concrete and straightforward. We make changes to the composition of our board to ensure more independence. We review all disclosure materials and ask verifying questions. This all feels very hands-on, which creates a sense of doing something important. It is important, but it’s just a small part of what is truly important for all stakeholders of the company.

<sup>9</sup> Heracleous, “What is the impact of corporate governance on organisational performance?” 168.

<sup>10</sup> Shane, *The illusions of entrepreneurship*, 98.

## Compliance-Based Processes Are Indirectly Supportive

It should be acknowledged that some compliance-based processes are indeed supportive of developing a well-functioning social environment at the board level. In this sense, compliance-based governance is potentially indirectly related to company performance.

For example, in my experience, in-camera sessions, excluding management before and after meetings, create an opportunity for candid fulsome dialogue that might not otherwise occur among directors. Another example is the separation of the chair and CEO, which creates the opportunity for the board to act as a more autonomous body that sets its own agenda. A third important example is the increasing demand for more disclosure around executive compensation, and the necessity of linking compensation to performance. This makes it easier to have the sometimes difficult conversations with the CEO on compensation matters.

These are a few examples of how compliance-based processes support the possibility of healthy director and executive relationships. However, although they are helpful, they relate to performance in an indirect, and therefore limited way. The real link with performance emanates more directly from the quality of decisions made by the directors, along with setting expectations for the quality and rigour of work underlying management's recommendations, and through modelling the values and norms necessary for organizational success.

The worrisome factor in compliance-based governance is that it can give us a false sense that we are being both

responsible and effective. Indeed, a compelling argument can be made that unless we are embracing a performance-based orientation in all our director involvements, we are being neither responsible nor effective.

## Board Culture and the Link With Performance

Understanding the importance of board culture requires firstly understanding the realities of the role and function of the board. Yes, our role involves compliance, oversight, monitoring, and providing advisory support, but these are all weak if not passive descriptors given our actual authority. Whether we like it or not, we are first and foremost a strategic decision-making body, and we have control over the corporation. When I say "like it or not," I have in mind the comments of a lawyer friend who has often said to me that "if directors really understood their responsibilities, many of them may not want to continue to serve."

Do we really understand our responsibilities? I think we do. But do we embrace our responsibilities and are we prepared to be answerable for our decisions? This is where I feel there is a gap. It is a fact based in law that we are responsible for all material matters of the company and must approve all related actions. Each and every approval is a decision. We all know this. Yet there seems to be a tendency toward what I would describe as passive neglect. The common tendency is to go along with things, keep our heads down, and then when challenges and threats arise, we point an accusatory finger at management or each other, or simply whitewash bad results by blaming the (predictable) unpredictability of turbulent

markets. The decisions we make are the most important decisions made within a company, but are our actions grounded in this understanding?

It's often said that the most important decision a board can make is the hiring of the CEO,<sup>11</sup> together with the potential replacement of the CEO if performance is poor. There is considerable but limited truth in this. In fact, I sometimes think the emphasis on this perspective is a distraction from a broader reality. On a normal course basis, the most important decisions a board of directors makes relate to changes in the capital structure of the company and the allocation of financial surpluses to capital spending, repayments to creditors, or distributions to shareholders. All board of director terms of reference include these areas as key responsibilities of the board. The authority to make these decisions, together with related fundamentals, is integral to value creation and risk management. Such decisions set the stage for performance and absolutely fall within the responsibility of directors. See Exhibit 2 for a description of decisions corporate directors make that cannot be delegated to management or a board committee. These have been excerpted from ARC Resources 2016 annual information circular.<sup>12</sup>

<sup>11</sup> Larcher and Tayan, "Corporate governance according to Charles T. Munger."

<sup>12</sup> ARC Resources Ltd. 2016 Information Circular – Proxy Statement, 24.



## EXHIBIT 2

### Examples of Decisions Required by Corporate Directors

Establishment of credit facilities

Issuance of additional common shares

Approval of capital expenditure budgets

Determination of the amount of dividends paid on common shares

Acquisition and disposition of properties for a purchase price or proceeds in excess of an amount established by the board of directors

Long-term marketing, transportation, and hedging arrangements in excess of an amount established by the board of directors

Source: ARC Resources  
2016 Information Circular

In this light, let's revisit the 2008-09 market crisis. Surely we don't require extensive research to demonstrate that compliance-based governance wasn't a relevant factor in determining survivability. However, this research exists, and the conclusions are clear. Gupta, Krishnamurti, and Tourani-Rad studied governance and performance during the 2008-09 crisis. Based on a comprehensive cross sample of 4,046 publicly traded, non-financial firms from various countries, they found that well-governed firms failed to outperform poorly governed firms.<sup>13</sup> What then, was at the root of the problem for so many companies?

In a pragmatic sense, the critical factor behind most corporate meltdowns is almost always balance sheet weakness. At a deeper level, certainly for many Wall Street firms, it's correct to point to self-interest and irresponsible risk-taking as the source of the problem. Yet in financial terms, the meltdowns all showed in the same way – declining asset values and excessive leverage. The focus on the need for changing culture for many of the investment banks was on point but too late, as these companies were already imploding.

The same is true within the energy sector today, which is struggling through a major decline. Almost all of today's failing companies are victims of declining asset values and weak or over-leveraged balance sheets.<sup>14</sup> We have looked at the relationship between performance, corporate governance ratings, and balance sheet strength, and conclude that governance ratings were irrelevant in predicting downside, whereas excessive balance sheet leverage was highly predictive.

More to the point, the most relevant factor in corporate failures is often the decision the directors made as to how much financial

leverage was acceptable. Yes, management may have made recommendations. But who approved the recommendations? Is it too obvious to state that, for a failing company with a wrecked balance sheet, it's the directors who failed?

Similarly, if capital is allocated poorly with a consequent loss of value, it must be recognized that we as directors approved all of this spending. We will sometimes blame "poor strategy," failing to appreciate that when we approve capital spending we are implicitly approving strategy. As directors, we normally don't lead the development of strategy or its implementation, but so what? Does this relieve us of our responsibility to ensure that capital spending is approved in the context of a clear, comprehensive, and internally consistent strategy? For an underperforming company with chronic confiscatory losses, again, what is the role of the board?

As directors, we also approve all material acquisitions, restructuring, and corporate transactions, which often have a powerful impact – positive or negative. Indeed, the directors have the authority to decide whether a company should remain as a going concern or be sold. Ongoing performance-monitoring can be seen as real-time due diligence with respect to whether the executive team is performing and whether the company deserves to exist in its current form. This question is always in the background, and the responsibility for an answer rests with the board.

When we acknowledge the reality of our authority and related responsibilities, and the importance of the decisions we make, we are then set to explore how the right culture can enhance the quality of decision-making and the probability of sustained superior performance.

<sup>13</sup> Gupta, Krishnamurti, and Tourani-Rad, "Is corporate governance relevant during the financial crisis?"

<sup>14</sup> Domanski, Kearns, Lombardi, and Shin, "Oil and debt."



## Is it too obvious to state that, for a failing company with a wrecked balance sheet, it's the directors who failed?

### How and Why Boards of Directors Fail

My focus on the importance of culture is in no way meant to diminish the importance of deep, relevant knowledge and expertise. Competence is essential. But so is the social environment within which decisions are made. In fact, the history of business is littered with failures where directors were clearly highly knowledgeable, experienced, and had outstanding track records.

How and why do such companies fail?<sup>15</sup> The related question is how and why do boards of directors fail? They fail because they make bad decisions, and bad decisions are often rooted in culture.

There's a good reason Harvard's Jeffrey Sonnenfeld observes that "what distinguishes exemplary boards is that they are robust effective social systems."<sup>16</sup> It's in this type of environment that directors freely challenge one another's views – not for the sake of challenging, but for the purpose of surfacing increased clarity and deeper understanding to support better decisions. This certainly includes understanding related to ethical sensitivities.

But there's more. A culture that supports a passionate search for the "real and the true" is essential to avoid the sometimes disastrous impact of a lack of clear seeing of relevant and material fundamentals. Sometimes poor outcomes are the result of decisions made with limited knowledge or a lack of competence. Often, though, the root of the problem is a failure to see clearly as a result of perceptual or cognitive biases.

If compliance-based governance is primarily directed toward avoiding or mitigating the impact of director

and executive leader self-interest, social-based governance, involving the social system of the board, serves to mitigate other problematic biases. These are the ever-present perceptual and cognitive hindrances or limitations that obscure clear seeing and can misdirect our attention, leading to suboptimal decisions.

### The Burden of Ever-Present Perceptual and Cognitive Biases

A fascinating and confronting example of a perceptual bias is captured in the research of Christopher Chabris and Daniel Simons in the now-famous "invisible gorilla test."<sup>17</sup> This is a short video of two groups wearing white and black shirts as they pass a basketball among themselves. Observers are asked to count the number of passes made by the group wearing white shirts. Meanwhile, a person in a full gorilla suit walks across the stage, stops and pounds his chest, then walks off. Since observers are busy concentrating on completing the counting task, about 50 per cent of people fail to see the gorilla.<sup>18</sup> This is known as inattentive blindness,<sup>19</sup> where we fail to recognize an unexpected stimulus despite the fact that it's in plain sight. I confess that I failed to see the gorilla when I watched the video! This is confronting, as it forces you to ask yourself what else you may not be seeing as you concentrate on all the detail in front of you.

I have often thought that "counting the passes" is analogous to compliance-based governance. While we are absorbed in reviewing detailed historical results, assessing new complex accounting standards, and debating various regulatory requirements, the

fundamentals of our business may be changing in significantly adverse ways. Yet, we may not see these realities even though they are in plain sight. When making important decisions at ARC Financial, we sometimes ask, "Did anybody see the gorilla that just walked through our boardroom?" Put differently, is there anything obvious here that we could be overlooking?

I have reached the conclusion that a certain set of biases exist and will always exist in corporate boardrooms. This is based on insights drawn from my own board experience and from years of advising corporate boards in major transactions, combined with the experience of investing in over 170 entrepreneurial businesses in which we usually had a control position (at ARC Financial). The question isn't whether the biases exist; they always exist. The issue is the extent of these problematic perceptual biases and whether there are structures, processes, and a culture in place to offset and mitigate them (See Exhibit 3 "Ten Perceptual and Cognitive Biases that Operate in Decision-Making and All Interactions.").

<sup>15</sup> Van Wielingen, "The evolving role of the corporate board: Governance, strategy and the imperative of performance," 5-6.

<sup>16</sup> Sonnenfeld, "What makes great boards great," 5.

<sup>17</sup> Chabris and Simons, *The invisible gorilla: And other ways our intuitions deceive us*.

<sup>18</sup> Ibid.

<sup>19</sup> Simons and Chabris, "Gorillas in our midst: Sustained inattentive blindness for dynamic events."



## EXHIBIT 3

### Ten Perceptual and Cognitive Biases that Operate in Decision-Making and All Interactions

1. We tend to see expected outcomes that are insupportably skewed to the positive. (Optimism Bias)
2. We tend to see what we want to see. (Confirmation Bias)
3. We tend not to see what we don't expect. (Inattentional Blindness)
4. We tend to see more of what was just seen. (Recency Effect)
5. We tend to see past events as easily predictable. (Hindsight Bias)
6. We tend to see what others are claiming to see. (Groupthink)
7. We tend to see what serves our interest. (Self-interest Bias)
8. We tend to see what supports our self-image. (Self-confirmation Bias)
9. We tend to relax and take comfort in our existing knowledge. (Complacency)
10. We tend to defend our knowledge as superior. (Arrogance)

There is also a tendency to cling to partial or limited truths drawn from experience-based understanding, but which don't necessarily represent a comprehensive and complete depiction of what is really happening.

One highly prevalent bias is intractable optimism and the associated discomfort with contemplating what might seem to be negative or pessimistic possibilities. The consequence is often a lack of energy and commitment to build a sufficient cushion for risk, margins for error, optionality, off-ramps, and contingency plans. Even when we commit to solid risk management structures and strategies, all too often we find ourselves lured onto the rocks by the siren song of a good deal, a new strategic initiative, the upside associated with ramped-up capital spending, or in recent years the apparent attractiveness of low-cost debt.

However the temptation shows up, the optimism bias inhibits the clear seeing of risk, thereby dampening the creative energy and drive required to fully explore possible action to avoid or at least mitigate risk. If you think you are immune to the impenetrable bias of optimism, consider researcher Tali Sharot's work, which shows that "a growing body of scientific evidence ... [concludes] that optimism may be hardwired by evolution into the human brain."<sup>20</sup> In my experience, what isn't hardwired is thoughtful contingency planning to deal with the possibility that optimism may prove to be misplaced.

I recall many board meetings in which a director with views that were perceived as being negative was ignored, or quite frankly stonewalled. More often than not this difficult director was me! I have heard every sort of rationale for why downside possibilities don't need to be explored. The most frequent are "It's slowing us down," "We don't have the time to explore hypotheticals," or "Don't you understand? We need to drive our business forward." I have also heard many different versions of "this feels negative – I want to keep

things positive around here." This last defence is particularly interesting given the reality that most businesses eventually underperform and fail.<sup>21, 22</sup> For myself, I would rather feel the discomfort of contemplating possible failure than the agony of actual failure.

The virulence of the optimism bias is often reinforced by the recency bias. This is the tendency to place more weight on recent positive developments or evidence that "all is well." Related to this is the confirmation bias, which is the tendency to see only that which confirms our viewpoint and position. In a strong market with growing revenues and high margins, although we may feel a measure of caution, it seems almost impossible to forecast and plan on a collapse of sales or the deterioration of margins. Further, our positive results confirm what we perceive as a reflection of the quality of our past decisions. These fundamentals become intoxicating, to the point that we more or less live for the moment, with little incentive to look realistically into changing dynamics. This is an aspect of the psychology of short-termism, and it creates a dangerous sense of complacency.

Lastly, we all tend to buy into consensus views, which are the basis of groupthink. It occurs in market cycles over and over, and often in new and emerging companies. Although we may talk about downside, few have the conviction to really push for decisive action to protect ourselves, including thoroughly developing alternative strategies to survive and prevail through unexpected adversity.

The above set of dynamics sounds so facile and simplistic that it may seem too improbable to be believed. This is why most decision-makers often kick themselves for not acting sooner to

20 Sharot, *The optimism bias: A tour of the irrationally positive brain*.

21 Shane, *The illusions of entrepreneurship*, 98.

22 United States Department of Labor, Bureau of Labor Statistics, *Business Employment Dynamics*.

deal with risks that were obvious and that prove to be material, if not fatal. What is the solution? Unfortunately, being aware of our biases is insufficient. As researchers Daniel Kahneman, Dan Lovallo, and Olivier Sibony point out in a 2011 Harvard Business Review piece, "Awareness of the effects of biases has done little to improve the quality of business decisions at either the individual or the organizational level. Though there may now be far more talk of biases among managers, talk alone will not eliminate them."<sup>23</sup> The solution lies in structures and processes, and in developing a culture where seeing what's real and true is valued more than seeing what we wish to see, or failing to see what we don't want to see. This is a culture in which humility and a passionate search for clarity and objectivity combine to create the intelligence to support consistent, high-quality decisions.

Although the above discussion is focused on biases that obscure one's ability to clearly see and understand the realities of risk and other threats, the mirror image of the same dynamics applies to not seeing upside and opportunity. Even the optimism bias can have a blinding effect relating to opportunity. There are many examples of companies that failed to see the true impact of emerging technologies, holding on to an "optimistic" view that the status quo would prevail. A current example of this is in the oil and gas upstream sector where many boards of directors and executive teams failed to see the extraordinary impact of combining hydraulic fracking and horizontal drilling. Consequently, most of these companies failed to adapt their strategies quickly enough to capture the potential upside of this technology.

## Active Diligence, "Tone at the Top," and Performance

A culture that supports quality decision-making is a clear causal factor in organizational performance. But there are other profoundly important ways in which the social environment of the board drives performance. Based on the authority vested in directors to make certain decisions, there is implicit authority to request additional relevant information and to expect a certain standard of diligence, depth, and thoroughness. A critical part of the role of directors is to continuously stress-test management's beliefs, assumptions, and the thoroughness of analysis that underlies recommendations. This is how we as directors gain the confidence to exercise our decision-making authority. More generally, this process of active diligence on the part of directors has the powerful, indirect benefit of encouraging, if not compelling, the executive team to higher standards of excellence in its own internal processes.

Another critical link between board culture and organizational performance relates to the attitudes and behaviour modelled by the directors toward the executive leaders and others deeper in the organization. During recent years, the importance of the tone at the top, as it's often described, has been widely accepted. Researchers agree that the tone at the top is central to the overall ethical environment in a firm<sup>24</sup> and to performance. Indeed, even as early as the 1970s, researchers were studying the increased effectiveness of ethically led organizations due to a strengthened culture characterized by low turnover and increased employee effort.<sup>25, 26</sup>

This perspective can be thought of in a much broader way. Tone at the top – the attitudes and values actualized and

visible among directors – is also critical to inspiring and supporting other essential conditions of culture. The directors can model a collaborative attitude, where trust is implicit. They can demonstrate through their behaviour and words an open acceptance of accountability. They can model curiosity and an evidence-based search for understanding. They can also model an ever-present commitment to the interests of the organization. A healthy and well-functioning board of directors is critical to the creation of a strong culture within the organization itself. A dysfunctional board of directors will not only make poor decisions, but a toxic tone at the top can also become a source of contamination for the rest of the organization. In my experience, a dysfunctional board can certainly be demoralizing for management and will ultimately become part of the story of underperformance and failure.

Any discussion on the culture of a board of directors and tone at the top would be incomplete without a reference to the importance of the chair. I will share an anecdote to get to the heart of the matter. I was recently asked at a large conference on board leadership, "How can we make the board of directors more accountable?" I later discovered that my response seemed to surprise a number of attendees. My response and advice to my fellow directors was to be prepared to "fire the chair." As directors, we talk easily, if not casually, about hiring and firing the CEO. Given the unquestionable, critical role of the chair in ascertaining priorities, facilitating discussion to seek clarity, and modelling the attitudes and behaviours needed to develop great culture, if there's evidence of dysfunctionality or poor decision-making at the board level, it behooves the directors to intervene with feedback to the chair and potentially take corrective action.

<sup>23</sup> Kahneman, Lovallo, and Sibony, "Before you make that big decision..." 51.

<sup>24</sup> Schwartz, Dunfee, and Kline, "Tone at the top: An ethics code for directors?" 79.

<sup>25</sup> Mowday, Porter, and Steers, "Employee-organization linkages: The psychology of commitment, absenteeism, and turnover."

<sup>26</sup> Steers, "Antecedents and outcomes of organizational commitment."



# Organizational culture ... feels obscure, vague, and intangible. This explains why most directors and executive leaders resist the subject of culture, often avoiding it altogether. ■■

## What Does Our Culture Need to Deliver to Support Success?

Organizational culture is both complex and lacks concreteness. It feels obscure, vague, and intangible. This explains why most directors and executive leaders resist the subject of culture, often avoiding it altogether. They feel more comfortable focusing on operations or the concreteness of products and services. For many directors, it's perhaps more comfortable to focus on the specifics of compliance-based governance, versus what can feel like the "mush" of culture.

This leads to one of the most important questions that can be asked by directors and executive leaders – a question that cuts through the inherent obscurity of culture. Simply put, the question is, "What does our culture need to deliver to support and sustain success? What values, norms, and behaviour need to be actualized and lived at the board level and within our organization?" Asked in this way, the question changes our perspective with respect to values. By shifting us away from a focus on values that are personal to you and me, it leads us instead to the needs of the board and the organization as social groups working to achieve a vision. What's the best objective view in terms of what our culture must deliver to support the long-term performance of our organization?

Looking at culture and asking questions in this way invites a broad search for objective understanding and relevant empirical evidence. What's the evidence that certain conditions within team or group culture support superior performance? You and I will have a variety of opinions. These tend to be based on intuition, hunches, and often nothing more than a vague understanding drawn

from experience. Given that sustained superior performance is more rare than common, the truth is that most of us haven't even seen cultures that support sustained great results. If we haven't seen it, how can we recognize it? Therefore, why not explore all available empirical evidence to surface greater clarity to support or enhance the views we hold based on our experience?

The fact is that there is now ample research evidencing the relationship between the various fundamentals of culture and performance. The research relates primarily to teams, groups of people, and organizations, though not necessarily to corporate boards. However, the dynamics are the same and are therefore directly applicable. Boards of directors are just another social group – a defined team of individuals working together with a common purpose.

## The "Must Have" Deliverables of Great Culture

Based on a few decades of building businesses and supported by empirical research, I believe there are four essential conditions that must exist within culture to sustain superior performance. What is somewhat unusual about my views is that I believe there is a certain universality to these requirements. They are relevant to all boards and organizations, particularly those engaged in competitive environments where the risk of underperformance and failure is high.

The essential conditions that are required in varying degrees within any board of directors and any organization are the following: collaboration, accountability, a discerning and adaptable intelligence, and commitment. I chose these because they

are concrete and practical. If we start with these four conditions and think of them as must have deliverables from our culture, we can then potentially organize all other values and qualities of culture in a way that fosters coherence and offers insight into how great culture can be created.

The following summary discussion of must have deliverables is offered to elucidate how these values or conditions interrelate, and also to evidence the link with performance based on selected empirical research. These comments offer but a taste of the interconnectedness of the many aspects of culture, and the selection of research is a small fraction of what's available and relevant.

## COLLABORATION

Few directors would debate the assertion that collaboration is a critical condition that must exist for the board to be healthy and productive. We can easily see that this implies a high level of inter-reliance. Directors, by necessity, have to rely on the quality, depth, and correctness of each other's work in committees, and certainly the veracity of information provided by management. This inter-reliance requires a high level of trust in the competence of our fellow directors and executive leaders, as well as in their integrity and ethics.

Integrity rests on the perception and reality of positive ethics and honesty. The high level of trust needed will lack a sound basis if there is any question that others aren't being honest. Trust also requires a high level of psychological safety with others.<sup>27</sup> It's critically important to know that we can explore and be vulnerable without other people attacking or attempting to diminish us. Psychological safety also creates an environment that enables individuals to engage in learning.<sup>28</sup>

<sup>27</sup> Edmondson, "Psychological safety and learning behavior in work teams."

<sup>28</sup> Ibid.

**COLLABORATION**

**Embraced Shared Goals  
Engaged Partnering  
Team Commitment**

**COOPERATION**  
Passive Support  
Reciprocal Support  
Inter-Reliance

**TRUST**  
Psychological Safety  
Predictability  
Transparency

**INTEGRITY**  
Wholeness  
Consistency  
Authenticity

**POSITIVITY**  
Ethics/Honesty  
Humility  
Benevolence

**AFFIRMATIVE VALUES**  
Respect  
Care  
Fairness  
Personalness

**“I AM”**

It has become clear to me that the foundation for collaboration and trust is a set of interpersonal values – notably fairness, respect, care, and the capacity to recognize each other’s uniqueness, which I refer to as “personalness.” There is implicit positivity in these values that is affirming for all participants – directors, executive leaders, and all who are connected with the enterprise. These values have to be lived and cannot be merely aspirational. “I AM” is the feeling or attitude that represents the embodiment of these values. This is what creates the experience of authenticity, which in turn supports the perception of integrity – the sense that something is real and pure, without falseness or contaminants.

One might think it is intuitive, perhaps even obvious, that fundamentals such as trust, honesty, and integrity are critical to performance. However, I have been surprised over the years by the number of times the question has been asked, “Are you sure about the relationship with performance?” People also comment, “If we build this type of culture, maybe we’ll all feel good, but will we get better results?”

It bears repeating that there is now ample research evidencing the relationship between the various fundamentals of culture and performance. Although, as previously noted, the research relates primarily to teams, groups of people, and organizations, and not necessarily to corporate boards, the dynamics are the same and are therefore directly applicable. It is worth stating once more that boards of directors are just another social group – a defined team of individuals working together with a common purpose.

Trust within culture and the relationship with performance has been extensively researched in recent years, and the

relationship with collaboration has been clearly identified. Specifically notable is the work of Interaction Associates and Human Capital Institute, which reported in 2013 that employees at high-performing organizations have a greater degree of trust in their leaders and colleagues; exhibit greater levels of respect for leadership; and report a stronger degree of collaboration inside their organizations than do employees in low-performing organizations.<sup>29</sup>

Closely related to trust is the quality of honesty. Based on 25 years of research, James Kouzes and Barry Posner have found that the single most important factor in the leader-constituent relationship is honesty. “What people most look for in a leader... has been constant over time. And our research documents this consistent pattern across countries, cultures, ethnicities, organizational functions and hierarchies, gender, educational, and age groups.”<sup>30</sup>

It’s hard to imagine sustained high levels of collaboration and inter-reliance based on trust and integrity in the absence of honesty. If we are committed to sustaining superior performance within our businesses, we have to be committed to sustaining relationships of superior quality with each other, along with all others we are dealing with or in some way impact. This is an imperative that is sometimes glossed over in the rush of meetings and decisions, and in the pursuit of financial gains that are often short-term in nature.

29 Interaction Associates and Human Capital Institute, “Building trust 2013: Workforce trends defining high performance,” 14.  
30 Kouzes and Posner, *The leadership challenge*, 29.

## ACCOUNTABILITY

All organizations are built on a wide dispersion of responsibilities. Accountability is the acceptance of responsibility and the willingness to be answerable for progress toward a desired outcome within a particular domain of responsibility. In this sense, accountability can be seen as a process in which behaviour and actions are aligned with performance. For this reason, I sometimes think of accountability as a proxy for performance.

There is clearly a vulnerability in being answerable for progress. It requires brutal honesty and humility to explain exactly where you are in satisfying your responsibilities. This can't happen in a full and complete way without a sense of psychological safety. Certain conditions of trust are necessary. You can be honest and you can fully disclose – including your mistakes and setbacks – and know you'll be received constructively and in no way find yourself personally diminished. This is the interplay of accountability and trust.

The foundation for accountability is self-efficacy, which I would describe simply as the attitude that "I CAN." If you have this attitude, and if the expectations are clear with respect to your role and responsibilities, as well as the tasks that need to be accomplished, you then have the basis for accountability. My perception of directors and executive leaders is that those who are uncomfortable with the vulnerability of accountability often lack confidence, usually because of inadequate knowledge and experience. Such confidence is another way of describing self-efficacy. If you sense that you might not be able to do something effectively, you will be reluctant to be fully exposed as you go about managing your responsibilities.

An extraordinary body of research supports the emphasis on learning versus the attainment of results, revealing that the performance of those focused on learning is far superior to that of those who focus only on results (e.g., Yeager et al., 2013). In 1986, Stanford psychologist Carol Dweck developed the construct known as "learning goal orientation" for the purpose of distinguishing between people with a learning or growth orientation. Such individuals believe knowledge and skills can be improved and developed with concentrated effort, versus people with a performance orientation or fixed mindset who believe their knowledge and skills can neither be changed nor further developed.<sup>31</sup> This dynamic underlies the power of accountability.

Many have come to equate accountability with the threat of punishment for underperformance or a negative outcome. Some directors and business leaders seem to hold the view that accountability means "confronting and tearing down" a wrongdoer. This is the regressive mindset of yesteryear managers. Great accountability processes provide feedback, support, learning, and motivation, and are indeed fundamental to sustaining great performance.

## ADAPTIVE INTELLIGENCE

A third critical deliverable of culture is an adaptive learning intelligence. A board of directors needs much more than technical skills, know-how, and IQ-based "smarts." It requires an intelligence that's alive and responsive; an intelligence that's discerning and can see the issues, large and small; an intelligence that has a natural capacity for analysis and synthesis, for both incisive discrimination and seeing the big picture. An all-important function of this intelligence is to see through our ever-present cognitive biases. This includes



# ACCOUNTABILITY

**Modelling for Others  
Inspiration  
Progress & Performance**



### ANSWERABLE

Objectivity  
Disclosure  
Transparency



### REALISM

Honesty  
Humility  
Vulnerability



### MOTIVATION

Learning-Centred  
Affirmative Feedback  
Progress Visibility



### RESOURCES & CLARITY

Knowledge/Support  
Authority/Control  
Expectations



### RESPONSIBLE

Ownership  
Acceptance  
Self-Efficacy

# "I CAN"

<sup>31</sup> Dweck, "Motivational processes affecting learning."



# Without discerning intelligence in the boardroom, trust can become blind, and we can end up following the CEO or our fellow directors without asking the tough and sometimes confrontational questions. //

the trap of believing that awareness alone is a sufficient solution to our biases<sup>32</sup> and precludes the need for mediating or corrective structures and processes.

The aliveness of a discerning adaptive intelligence ultimately rests on a passion to know. "I WANT" to know and understand is experienced as a passion for and love of what's real and true. Since our circumstances are dynamic and evolving, our passion for knowing must be ever present. The driving energy is a deep curiosity that's creative and always open to fresh perspectives and new realities. These may relate to consumer trends, technology, political and regulatory developments, organizational change, and issues of human resources. Seeing multiple possibilities, as well as change when it's arising, requires openness and an exploratory mindset.

Adaptive intelligence can be described as a continuous, ever-present search for new knowledge, understanding, and insight. If you want to understand you will be naturally inclined to ask questions and listen carefully to others. You will be inclined to help others clarify and strengthen their views and you will be comfortably willing to surrender your views if you sense a clearer truth in what is being expressed. Active listening is not a construct of great effort as some people think; it arises naturally as the product of seeking understanding. Research supports listening and seeking new ideas and understanding as behaviours that are clearly associated with team learning and effectiveness (e.g., Edmondson, 1999).

As new knowledge is on the frontier of change, the mindset of adaptive intelligence is anticipatory and naturally oriented toward change. A preparedness to change is implicit in this intelligence. It reflects a foreseeing, coupled with a willingness to surrender outdated understanding, which

requires humility and a willingness to be vulnerable to uncertainty and change.

Without discerning intelligence in the boardroom, trust can become blind, and we can end up following the CEO or our fellow directors without asking the tough and sometimes confrontational questions. Without discerning, adaptive intelligence, commitment to accountability may collapse into self-blame. This is the proverbial "falling on one's sword." The problem with this is that it can create a blanket of obscurity. Almost always mistakes involve a number of individuals and a variety of factors. The key is clarity in our learning and concreteness in our response. Without a penetrating, discerning intelligence, we may not be aware of when we are using "learning" as a rationalization for not taking responsibility for change and appropriate action. When we are making mistakes and creating problems, we can only say we are "learning" so many times. Further, some mistakes may be fatal, rendering our learning experience after the fact irrelevant to our shareholders.

Without a discerning intelligence, actions, projects, and operations can take on a life of their own and become ends in themselves. This can be seen over and over in buoyant and rising markets and is a cause of boom and bust cycles. Managers with the support of compliant directors lose their learning mindset and discernment. They overcapitalize business segments or projects, usually of course at or near the top of market cycles, and also correspondingly often over borrow with disastrous and irreparable consequences.

While the literature has established the relationship between financial outcomes and corporate culture, more recently some researchers have focused specifically on understanding an organization's cultural adaptability and its effects over the long-term, suggesting that survival is the

ultimate organizational criterion.<sup>33,34</sup> In 2015, the Journal of Business Psychology published a study that looked at 95 organizations founded before 1940. The research concluded that an adaptive culture is predictive of organizational survival.<sup>35</sup>

**ADAPTIVE INTELLIGENCE**

**Continuous Renewal Innovation & Change Responsiveness/Aliveness**

- INTELLIGENCE**
  - Discernment & Materiality
  - Depth & Detail
  - Comprehensiveness
- OBJECTIVITY**
  - Evidence-Based
  - Unbiased
  - Clear-Seeing
- LEARNING**
  - Anticipatory
  - Insight
  - Listening
- SURRENDER**
  - Letting-Go
  - Humility
  - Vulnerability
- TRUTH**
  - Multi-Perspective Curiosity
  - Creative Curiosity (What if?)
  - Passionate Curiosity

**"I WANT"**

32 Kahneman, Lovallo, and Sibony, "Before you make that big decision..." 51.

33 Aldrich and Martin, *Organizations evolving*.

34 Schein, *Organizational culture and leadership*.

35 Costanza, Blacksmith, Coats, Severt, and DeCostanza, "The effect of adaptive organizational culture on long-term survival."

## COMMITMENT

The essential condition of commitment allows me to offer an additional broad perspective. This relates to the question of how board culture fits with other central fundamentals of organizational success – notably vision, purpose, and the interests of all stakeholders.

Commitment reflects a choice and causality. We have decided to let go of other possibilities in order to focus on one particular possibility, one future. It's within the scope of this one path forward that we will create our desired future. The singularity of our choice requires a sense of closure with respect to other possibilities. This facilitates the kind of strong commitment that will support persistence and tenacity in overcoming adversity, along with the "bounce back" of resilience. Commitment also requires restraint and discipline.

One of the most impactful pieces of research on the benefits of restraint is the "marshmallow test." Led by Walter Mischel and involving many other researchers over time, it was published in 2010 as "'Willpower' over the life span: Decomposing self-regulation."<sup>36</sup> The conclusion was that "resisting temptation in favour of long-term goals is an essential component of social, cognitive and mental health over the course of a lifetime."<sup>37</sup> Those who had more self-restraint were more successful in life generally. I have often thought that short-termism and the sometimes reckless and impulsive nature of decisions within businesses looks like self-indulgence and poor self-regulation.

The value of discipline is clearly evidenced in other studies. Duckworth and Seligman concluded that self-discipline outdoes IQ in predicting academic performance.<sup>38</sup>

This certainly conforms with my experience of working with a wide range of business leaders.

Another powerful research-based conclusion related to commitment is that of Jim Collins. In his study of successful leaders, he identifies fierce resolve and discipline as key determinants of success. Interestingly, he pairs this with humility. In fact, he posits that the unique combination of will and humility represents the highest level of great leadership.<sup>39</sup>

It is critical that commitment is aligned with what's most important. This is at the heart of governance and executive leadership. It speaks to the materiality of purpose. Why do we as an organization exist? Are we aligned with our central purpose? A large part of the answer to this question relates to another question: Is there not a common purpose for all businesses that in aggregate represents the central purpose of business in society?

I believe business leaders today are somewhat lost in understanding our role and the interconnection of the interests of our businesses and the interests of society. The prudent, responsible, and profitable management of capital – of society's savings, no less – has to be a central purpose. This involves a deep commitment, not just to value creation and profit, but to maximize the predictability of value creation. This can be understood as creating certainty or reducing uncertainty or risk. Indeed, for boards of directors, both value creation and predictability or risk management need to be seen as strategic priorities.

Further, our businesses and society need a long-term orientation from us that encompasses a commitment to sustainability – of our organizations, our relationships, our communities, and the



## COMMITMENT

**Shared Vision**  
**Shared Commitment**  
**Shared Purpose**

▼ **DISCIPLINE**  
Controlled March  
Order  
Restraint & Control

▼ **PERSISTENCE**  
Steadfast  
Tenacious  
Resilient

▼ **SINGULARITY**  
One-Way  
Focus  
Confidence

▼ **RESOLVE**  
Solution  
Conclusion  
Conviction

▼ **WILL**  
Choice  
Deliberate  
Causality

# "I WILL"

<sup>36</sup> Mischel, Ayduk, Berman, Casey, Gotlib, Jonides, and Shoda, "Willpower" over the life span: Decomposing self-regulation."

<sup>37</sup> Ibid, 252.

<sup>38</sup> Duckworth and Seligman, "Self-discipline outdoes IQ in predicting academic performance of adolescents."

<sup>39</sup> Collins, *Level 5 leadership: The triumph of humility and fierce resolve*.

environment in which we operate. Again, as directors and business leaders, we need to view sustainability as a strategic priority. It's also in the interest of our businesses and society that we view the quality of human experience within our organizations and all who we impact as a strategic priority, right up alongside profit, risk, and sustainability. This means creating social environments that are ethical and oriented to support human development.

These strategic priorities serve to create relevance and purpose, and together represent a powerful force for both the development of great strategy and creating legitimacy and support within society. Risk management versus recklessness, disciplined long-termism versus impulsivity, and the embrace of human experience must all be understood as strategic imperatives that are in the interests of our businesses and society, and thus necessitate an unwavering commitment from directors and executives.

As directors we stand in the middle of an intersection of interests, involving responsibilities in a number of directions. We are stewards of a set of resources and interests that in aggregate are of great importance to society. My experience is that if a board of directors can become attuned to and aligned with these broader interests, it will be tapping into a resolve – and ultimately a strength – that can serve as a profound guiding force within the culture of the board and the organization as a whole. This sense of stewardship becomes part of an intrinsic motivation that is actualized in culture to sustain a great business.

## Putting It All Together: Great Culture, Great Boards, and Great Performance

If we don't understand the importance of the role of the board, we will never understand the importance of board culture. We will never be motivated to develop an incisive understanding of the fundamentals of the culture needed to support our responsibilities, nor will we create the board composition and leadership functionality that is imperative for success.

I previously noted that the primary function of the board is strategic decision-making first and foremost. I use the word "strategic" deliberately. One criterion as to whether an issue is strategic is whether it is truly material, and there should be no doubt that director authority relates to the most material fundamentals of the organization. A further clarifying perspective regarding the role of the board is to recognize the blunt reality that the board of directors is in control. We exercise "choice" in assessing alternatives relating



### EXHIBIT 4

#### Selected Practices to Surface Unbiased Evidence-Based Understandings of Culture

- Annual strength of culture or engagement surveys done anonymously but by department or business segment, with roll-ups prepared for review by the board of directors. These should include qualitative notes and comments from survey participants, which will form part of the material to be reviewed by the board.
- Annual 360 reviews of communication and leadership capabilities of executives, and the same for managers at least every two years, with summary detail presented to the board. The 360 review of the CEO should be part of his or her annual performance review.
- Periodic "pulse" surveys that peer deeply into parts of the organization or which have a specific cultural focus, with results presented to the board.
- Periodic red-flag surveys and assessments that identify problematic behaviour to watch for and that likely already exists, with a summary going to the board.
- Periodic educational sessions on the link between culture and performance for all employees and directors, to continually reinforce a commitment to the importance of culture.
- Specific to the board itself, annual "culture and operations reviews" managed internally and periodically supported by an independent expert.



## Absent this active ingredient – the relentless search for what is real and true – the biases and partial truths, and the complacency and arrogance, will rule the day with predictable consequences. ■■

to strategic risk and the capital allocation process. Indeed, we have the authority to choose whether the business should even exist as a going concern. This was all emphasized above, but bears repeating.

How then should we define the role of the board relative to management? The board and management should be seen as partners, but with different roles. The board is best understood as the control partner, and management as the executive partner, which reflects their respective authorities. This doesn't take anything away from the view that the executive team is in a leadership role and must act to create the desired future of the organization; it must make it happen, which is the essence of leadership. But nevertheless, the board of directors is in control, and to think otherwise is hard to fathom. Indeed, it is going in the wrong direction.

Once grounded in the realities of our decision-making authority and the importance of our responsibilities, it's easier to contemplate the question, "What must exist within culture to support the effective exercise of our responsibilities?" Expressed in more concrete terms, "What culture must exist to support consistent, high-quality decision-making?"

Can you imagine consistent, high-quality decision-making without collaboration, inter-reliance, and a high level of trust? Unfortunately, many of us can imagine this, as we have seen it often. If we are skeptical of each other's motives and intentions, or if there is a fear of expressing our views, how do we engage wholeheartedly in the requisite discussions to overcome partial understanding and biases? How do we surface the clearest objective understanding?

Can you imagine consistent, high-quality decision-making absent a high level of accountability? Again, unfortunately this may be too easy to imagine. What does it look like? Call it rubberstamping, which is the common criticism of boards of directors, but I see this as an expression of complacency. It's easier to just go with the flow and not probe more deeply, particularly if the questions that need to be asked are implicitly contrary to management's view or the consensus of the board.

How can we make consistent, high-quality decisions without a discerning and adaptive intelligence to allow new understanding to surface? If we lack the humility to let go of "old truths and old positions," how do we respond to the dynamism of change, both in the business environment and internally within our organizations? My own experience is that most of us are stuck in the past. I know I have this tendency, which is why I place so much value on engaged inquiry and debate with my fellow directors and management.

How can we make consistent, high-quality decisions without an unwavering commitment to uncover what is real and true? My experience is that decisions may be difficult simply because the reality of circumstances is unclear. It requires persistence and tenacity to turn toward the discomfort of uncertainty and stay in an exploratory mindset in order to surface the needed clarity.

Consistent, high-quality decision-making cannot take hold without a deep commitment to the interests of the organization, which includes all stakeholders. Otherwise, to what and to whom are we committed? Unfortunately, most of us can provide many examples in

response to this question that evidence a diffusion of our commitment if not an actual compromising of integrity. Groupthink and complacency can be a much easier environment to hang out in than the discomfort of challenging what may be bias or partial truth.

The fundamentals required within culture to fulfill our responsibilities all point to the need for the same active ingredient – the passionate, if not fearless search for unbiased objective understanding, and the willingness to act on this understanding. Acting on our understanding is manifested in our decisions. Absent this active ingredient – the relentless search for what is real and true – the biases and partial truths, and the complacency and arrogance, will rule the day with predictable consequences.

Nowhere is it more important to source unbiased objective understanding than with respect to culture itself. Certain practices can be helpful in generating evidence-based understanding of the culture within our organizations (See Exhibit 4 "Selected Practices to Surface Unbiased Evidence-Based Understandings of Culture."). It is critically important that the directors receive this information and review the results as a regular agenda item. Directors, executive leaders, managers, and all employees need to know that a healthy, strong, and effective culture is a strategic priority, and that certain must-have qualities within culture must exist.

## Processes and Practices Versus Understandings and Convictions

A constant theme I hear from managers and business leaders is, “Just tell us how to do it. We don’t need theory and we don’t need depth; just give us the ‘how-to’s.’”

There are many practices and processes to create great culture, some of which I referenced above, such as the monitoring and measuring of culture, and the role of the chair. I could focus on certain practices which you may wish to pursue and implement, but what happens in the boardroom when you are met with predictable resistance from fellow directors?

What good are practices without deep understanding as to what purpose is being served? Without these deep understandings, what are your chances of presenting a compelling argument that will overcome the ‘naysayers?’ Further, how much resolve will you have in pursuing change without a firm anchoring in your responsibilities? There is no shortage of possible practices. The shortage is of clarity and knowledge, deep convictions, and the willingness to own responsibility.

For example, 360 performance reviews are a basic practice but I’ve been amazed throughout my career how much resistance there is from executive leaders to do this on a regular basis and how relatively disinterested many directors are in receiving this information (until they receive it and get a few surprises). With deep understanding based on sound theory and empirical evidence, I’ve found that I can usually encourage the adoption of this practice, but it’s almost always a big push to make this happen.

Another example of resistance relates to the issue of short-termism. As corporate directors these days, we are all engaged in a discussion about the importance of thinking and acting with a long-term focus. Yet I understand from compensation consultants that something like 80 to 90 per cent of executive compensation is earned within three years. The balance is often just pension benefits. At ARC Resources we developed a compensation plan that extends out roughly ten years. We were able to overcome resistance because of the conviction of a number of directors who understood that unless we are long-term oriented, we will not be appropriately strategic in developing our business and our organization.

There are many other examples of how resistance surfaces in response to progressive and potentially important advancements in board and organizational practices. Knowledge of these practices is important but insufficient. A depth of understanding, supported by evidence and robust reasoning, is necessary to overcome the resistance to advanced practices, but in my experience, even more is needed.

When we firmly understand and embrace the unique role of the board relating to performance – which does not in any way diminish management’s responsibilities – everything changes. When the inevitable resistance to progress and advancement arises, those who understand and embrace their responsibilities will dig deep for insight and understanding. They may adjust their views or change their minds as new perspectives and knowledge arise, but the resolve to make quality decisions and exercise influence in a meaningful way will remain

constant. Those of us who want to create sustainable positive change will not let go easily. The benefit is for the organization, all stakeholders, and members of society who are seeking a higher level of leadership from corporate directors.

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