What's the board's role in strategy development?: Engaging the board in corporate strategy

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A dynamic tension is emerging in the evolving relationships between CEOs and their boards. As legal requirements surrounding corporate governance increase, directors are taking a more active, independent role in their corporate oversight responsibilities. Consequently, chief executives must determine how to engage their newly empowered boards in real, hands-on work that provides value to the company but doesn't result in directors usurping essential management functions. While simple in theory, the challenge is for management to develop processes that engage their boards in the right kinds of work – and in the right way.

If a CEO is sincere about finding a level of board engagement that goes beyond mere window dressing, he or she should consider involving the board in the development of corporate strategy. A recent survey confirms, ''There is little doubt that board members want to be involved in strategy''. Directors ''want to understand the strategy of the business and want to have opportunities to shape and influence it[1]''. Yet, while some directors are both eager and equipped to contribute to strategy development, they are likely to become frustrated because many corporations do not have a process to involve them in a substantive way.

From their perspective, CEOs report that strategic planning is one of the most important issues that their boards should address[2]. A study of CEOs conducted by the National Association of Corporate Directors reveals that the board's participation in ''strategic planning ranked number two in importance to their companies, yet only number 11 in their board's effectiveness[3]''. So if CEOs place such importance on their boards' contributions to strategy development and directors express a desire to participate, why aren't more boards integrally involved in developing their companies' business strategies?

The reasons vary, but a primary one springs from CEOs' reluctance to involve their boards too heavily in running the company (management) and deflecting their attention from ensuring that the company is well run (governance). Similarly, many companies lack a clear process – the

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Definitions of strategic activity

We use the term ''corporate strategy'' to encompass four different types of activity:

(1) **Strategic thinking.** The first step in strategy development involves the collection, analysis, and discussion of information about the environment of the firm, the nature of competition, and business design alternatives. Business design includes the customer value proposition, the scope of offerings, profit-capture mechanisms, and sources of competitive differentiation[4]. In multibusiness firms, strategic thinking also involves core questions about the shape of the business portfolio.

(2) **Strategic decision-making.** Ultimately, strategy requires a set of core directional decisions. In the context of strategic thinking, there are fundamental choices concerning the business portfolio and the business design, which serve as the platform for the future allocation of limited resources and capabilities.

(3) **Strategic planning.** Once key strategic decisions have been made, priorities are identified, objectives set, and resources configured to execute the decisions. This typically results in a plan and a set of budgets, though the plan evolves over time as consequences of the firm's actions are seen, the environment changes, and new information is obtained.

(4) **Strategic execution.** Reaching this phase, the company focuses on implementation, monitoring results, and appropriate corrective action. This phase of strategy development can involve the allocation of funds, acquisitions, and divestitures.

The Board's role can differ dramatically in these four development phases (see Exhibit 1).

education, necessary steps, definition of roles and responsibilities, for example – that enables directors to constructively participate in strategy development. However, there are distinct benefits for companies that systematically and effectively involve their boards in setting strategic direction. Not the least of these is enhanced board-management collaboration, which can carry over to other board-management interactions. Additionally, a board engaged in strategy development becomes better educated about the company and more committed to its chosen direction.

We offer an action plan for CEOs who want to constructively engage their boards in the strategy process that:

- details five key elements of value-added engagement of the board in strategy;
- provides a framework for board-management strategic decision-making; and
- identifies requirements for an effective participative strategy process.

The plan outlines the step-by-step actions that management can take to effectively involve their boards in the strategy process.

Ideally, a board that is engaged constructively in strategy is:

- an active participant in strategic thinking;
- involved substantively in strategic decision-making and the ultimate approval of major decisions affecting the portfolio or significant investments;
- providing input to the process required to implement the strategic plan, including measures and milestones necessary for strategic decisions to be turned into action within the desired timeframe; and
- apprised of strategic execution as part of its normal review of company performance.

Engaging the board in strategy

Many CEOs, for a variety of reasons, are concerned about the board's involvement in corporate strategy development[5]. At one extreme, many CEOs believe that board involvement is an all-or-nothing proposition. At the other extreme are CEOs who worry that board involvement will be merely a cursory review, a common practice where the board reviews the strategic work that has been done by the executive team, usually after that work has been completed. Theoretically, this cursory appraisal provides an opportunity for the board to review

Exhibit 1 Corporate strategy tasks and roles

Description of task	*Role of the board*	*Role of senior management*
Strategic thinking Collecting, analyzing, and discussing information about the environment of the firm, the nature of competition, and broad business design alternatives – different views of customer value proposition, scope, competitive advantage, and profit capture	■ Be an active participant in the strategic thinking process ■ Bring an outside perspective and accumulated wisdom ■ Test the consistency of management's thinking ■ Collaborate with management	■ Initiate the process of strategic thinking ■ Set the agendapose the questions and issues ■ Provide rich and meaningful information ■ Actively participate with the board in the discussions ■ Summarize the output of board and management working together
Strategic decision-making Making the fundamental set of decisions about the business portfolio and business design	■ Provide input for management's decision-making ■ Provide ultimate review and approval on major decisions (resource allocation, initiatives, portfolio changes, etc.)	■ Make critical decisions ■ Develop proposals to the board for critical directional decisions and major resource allocation ■ Engage with the board in its review of decisions
Strategic planning Translating the critical strategic decisions into a set of priorities, objectives, and resource allocation actions to execute the strategy	■ Review core strategic plans presented by management ■ Ensure understanding of the plans and their potential risks and consequences ■ Comment and make suggestions on plans, as appropriate ■ Approve plans	■ Develop plans, working with staff support and operating management ■ Review plans to ensure consistency with corporate objectives and strategy ■ Present plans to the board for review
Strategic execution Undertaking the various initiatives and actions consistent with the strategic plan, including adjustments over time to account for environmental changes and different outcomes	■ Review the process and progress of implementation of key initiatives *vis-á-vis* established milestones and objectives	■ Ensure resources and leadership for execution are in place ■ Monitor progress of execution ■ Make changes in either the execution or the plan, depending on outcomes

management's strategic decisions and directions, but in practice, it is usually done with the expectation that approval will be given. In such cases, the board has few options – either accept, reject, or postpone – and it has very little basis on which to evaluate or shape the strategy. A possible alternative is to have the board lead strategy development, which many CEOs see as an infringement upon their – and management's – responsibility and role.

An alternative approach

There is, however, a middle position, one that we call value-added engagement. In this approach, the board participates in the strategic thinking and strategic decision-making processes, adding value but not infringing on the CEO's and executive team's fundamental responsibilities. More specifically, in value-added engagement, the CEO and management lead and develop the strategic plan with directors' input, and the board generally approves the strategy and the metrics to assess progress. We've seen this approach, which is both possible and desirable, employed in a variety of different settings.

At one company, the CEO and executive team decided to engage the board in making a critical choice about the company's business portfolio and future strategic direction. The ultimate decision involved whether to divest several business units and become a communications equipment pure-play, or, alternatively, to concentrate resources on and ''turbo-charge'' a small portfolio of complementary businesses. This was a difficult choice to make in an era when the communications industry was booming and seemed poised for continued future growth. But, in their work together, management and the board recognized the perils of putting all their eggs in a single basket. They resisted the allure of a seemingly sure thing and chose instead to pursue a balanced strategy of diversified but related businesses. The decision would turn out to be a pivotal one. By early 2001, the communications sector was in a rapid decline, and the choice to pursue a balanced portfolio strategy was directly responsible for the ongoing viability of the company.

While board participation in strategy doesn't always produce such significant results, engagement can yield substantial dividends. It helps to:

- Create deeper understanding. As the board participates in strategic thinking, directors learn about the company and its strategic environment. Their expanded knowledge better prepares them to contribute to future strategic discussions and decisions.
- Build ownership. By participating in the process, the strategy becomes "our" strategy as opposed to "their" strategy. With increased ownership comes increased commitment to help the strategy succeed and to defend it when under attack.
- Improve the quality of decisions. Directors bring new perspectives, different points of view, and wisdom that can lead to better strategic decisions.
- Define a more collaborative dynamic between the board and management. The board and management's collaboration on a mutual strategy enhances their ability to work as a team on other initiatives and decisions.
- Increase board satisfaction. Board members feel that their time, knowledge, and experience have been used constructively.
- Prompt board members to become external company advocates. When directors are an integral part of strategy development, they are more likely to champion and appropriately defend the company's strategy to external audiences, including analysts, customers, suppliers, and media.

While the benefits can be significant, broader board participation in strategy development also has costs. First, board members need a comprehensive understanding of the company, and that takes time and commitment. As the Conference Board suggests, "In approving strategies, boards need to understand, among other things, the corporation's capital allocation, debt levels, risks and vulnerabilities, compensation strategy, and growth opportunities. Importantly, they must engage management on the central issues facing the company and have a firm grasp on the trade-offs that lie at the heart of a corporate enterprise[6]". Increased board participation can also result in less management control over the outcome. Real participation means influence, and influence means the ability to change outcomes. However, a well-designed and well-facilitated process can yield the benefits of participation while limiting the amount of time and potential loss of control.

The key elements of a value-added engagement process

The challenge is to construct a process that can produce value-added engagement. Five key elements are critical to successful engagement of the board in strategy development:

(1) View strategy as a process, not an event. Successful board-level strategy work usually involves a process that occurs over months. Frequently, discussions with the board about strategy may begin at a strategy offsite, but following this, significant time is required to digest information, perform analysis, and develop insight. CEOs can develop and present to directors an overview of the strategy process at an initial "special" meeting, after which their involvement in developing the company's strategy becomes the focus of both regular board meetings and offsites for the ensuing six to nine months.

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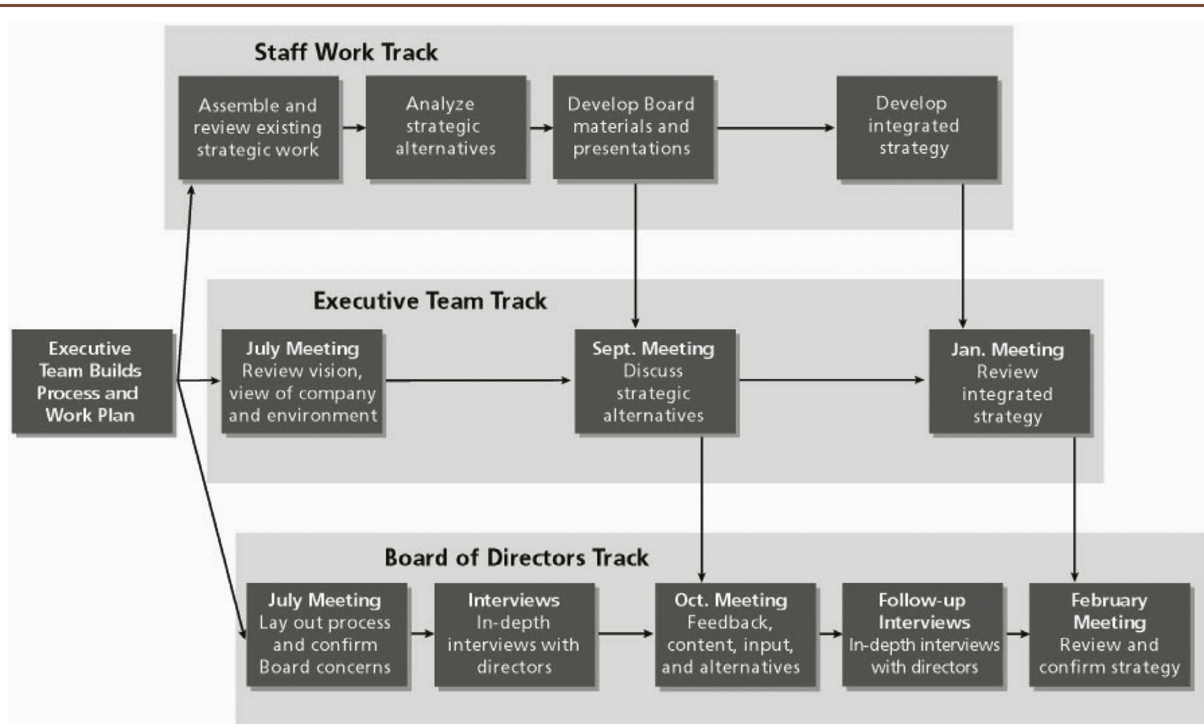
(2) Design parallel but lagged processes. The executive team – not just the board – should be a part of the strategy development process. Parallel processes should be created, with the executive team going through the same steps and asking the same questions as the board but in more depth and detail. Usually, the executive team is somewhat ahead of the board (or the board-level process is lagged). This allows the CEO and executive team to pose the most pertinent questions to the board, rather than just throwing open strategy development for unguided discussion. At the same time, the team cannot get so far ahead of the board that it already has answers it is committed to and, consequently, is not open to input from or influence by the board. The board is engaged in a process of discovery as it works strategic issues, but it is a guided discovery, bounded by the work that the executive team has already done but also informing that work. Exhibit 2 illustrates the parallel but lagged workflow process developed for one client's staff, executive team, and board.

(3) Inform and educate the board. In order for independent directors to engage in strategy in a value-added manner, they need access to appropriate information, such as company financials, industry and competitor developments, and broader economic trends. And, frequently, they also need to develop a much deeper understanding of the business, which can be done through briefings, training sessions, site visits, and product/offering demonstrations. One board, for example, participated in a day-long working seminar on emerging technologies at one of their company's research and development centers. Others visited manufacturing, operational, or retail sites. Immersion in a company's day-to-day operations is a critical component of the board's education and it should include familiarizing members with the various lines of business, their customers, and their strategic options.

(4) Collect and analyze director input. True engagement requires the opportunity to provide input. This implies finding ways for individual directors to ensure that their perspectives, questions, and recommendations find their way into the process and are seriously considered. Episodic board meetings, which tend to be infrequent and driven by set agendas, are not the most productive time to get such input. Collecting several rounds of

Exhibit 2 Strategic choice framework



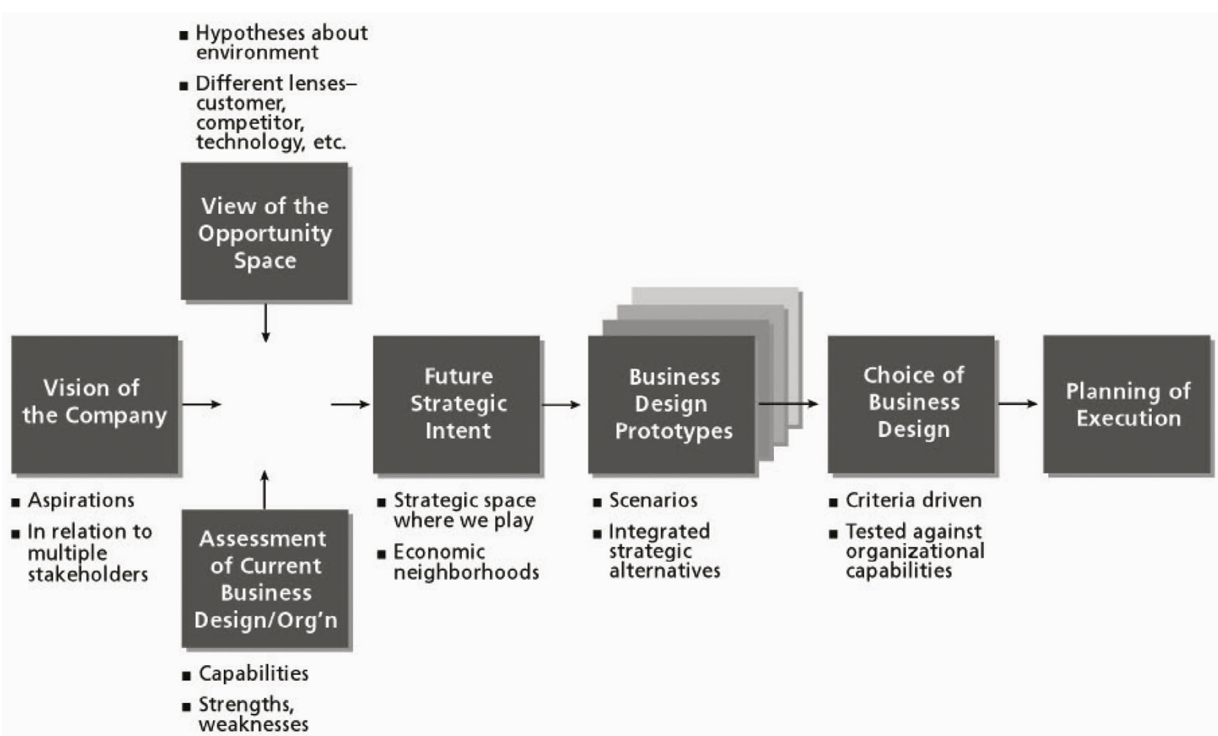
data – over time – from each director is critical but time consuming. One effective approach is to interview directors individually (and, in some cases, supplement these interviews with surveys), at their own offices, using a set of questions and issues related to where in the strategy process the board is. Then, as a means of starting and focusing discussion at the next board work session, information from the interviews is analyzed and feedback is presented to the board as a whole. In a one-on-one setting, directors are frequently willing to share concerns, observations, and questions that they might not feel free to raise in a group setting. The interview/feedback cycle helps make the in-room board time more productive and ensures that the right issues are on the table.

(5) Generate strategic alternatives. Real involvement comes from informed choice and the opportunity to develop commitment to decisions that the group makes. Informed choice is difficult when the only alternatives possible are to accept or reject. The best practice is for executive teams to develop and present to their boards a set of viable strategic alternatives – distinctly different courses of action. The management of the high-technology company we described earlier presented its board with several variations on two themes: pure-play or balanced portfolio. Neither limiting directors to a single yes/no response, nor overwhelming them with infinite possibilities, the executive team offered the board several distinct business design alternatives, allowing them to compare the advantages and disadvantages of each. Directors had a real choice and were engaged with the process. And while their role was not to select the strategic direction, they were able to identify and discuss the pitfalls and opportunities they saw with each strategic alternative and work with management to make the best choice.

A framework for strategic thinking and decision-making

A framework can help to organize the discussions and decisions that the board will undertake and is helpful when implementing the key elements of this process (see Exhibit 3). Both the executive team and the board can use it to sequence activities, although each situation will have

Exhibit 3 Parallel, lagged workflow process



its own specific requirements. This framework, which we call the ''strategic choice process'', involves six key steps:

(1) agreeing on the company vision;

(2) viewing the opportunity space;

(3) assessing the company's business design and internal capabilities;

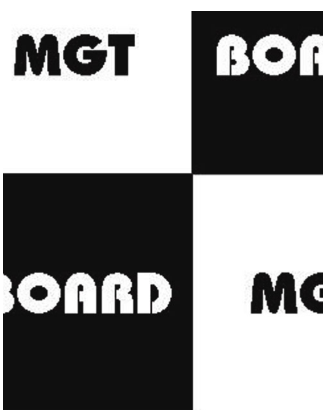
(4) determining the company's future strategic intent;

(5) developing a set of business design prototypes; and

(6) choosing the business design alternative that is deemed best.

Agreeing on the company vision. The work typically begins with a restatement (or confirmation) of the company vision – a description of its aspirations in relation to multiple stakeholders, including investors, customers, suppliers, employees, legislative and regulatory institutions, and communities. The vision statement should answer this question: ''What are we striving to become in terms of our role in the larger environment in which we function?'' If the vision is not clear, significant work may need to be done before moving ahead.

Some companies like to use vision statements born in the marketing or public relations department and intended for a variety of external purposes. A better practice is to develop vision statements intended as an internal guide for strategy development. In this context, a vision statement is aspirational and gives a picture of what the company hopes to accomplish and hopes to be, in the context of stakeholders, but in tangible and measurable terms. Good vision statements talk about measures of growth, relative positions in markets or industries, or returns to shareholders. They provide a benchmark against which to assess strategic alternatives.



Viewing the opportunity space. The second step in the strategic choice process is to consider the potential opportunity space in which the company might function successfully. Strategy makers first describe the environments in which the company operates, and then develop points of view, or hypotheses, about those environments. In the pure-play/balanced portfolio case mentioned earlier, the ability of management and the board to forecast the risks of a singular focus on communications was not just a stroke of good luck. It came from a thorough understanding of the company's business environments and a disciplined, collaborative approach to developing well-grounded hypotheses about how those environments were likely to change. The analysis of environments can be done from different perspectives. One might consider different emerging markets, the range of available technologies to meet a customer need, the potential set of customers, or the constellation of competitors. Each of these presents a different set of ''lenses'' through which to look at the environment. Obviously, in different companies and industries, different lenses will be appropriate.

Assessing the company's business design and internal capabilities. The next step is to look inward, making an assessment of the company itself, including its current business design and organization. The objective during this phase is to understand current and potential capabilities of the company in the context of the opportunity space. This assessment focuses on the relative strengths and weaknesses of the firm, including its human capital, technologies, financial situation, work processes, etc. Different tools and models can be used to do this assessment[7].

Determining the company's future strategic intent. The fourth step is to bring together the vision, the view of the opportunity space, and the assessment of the current business/ organization to identify a future strategic intent. The purpose is to identify a strategic space where the company's capabilities and the hypothesized environment come together in places where the potential for profit is present – what can be called attractive ''economic neighborhoods''. In other words, it involves determining the most attractive opportunities for the company to pursue the development of business, given their vision and their capabilities. At this point, the executive team and board can begin to identify the key criteria for evaluating a potential business design that would reflect that strategic intent. These key criteria will be used later on to make critical choices.

Developing a set of business design prototypes. Having identified a strategic intent, the next step is to develop prototypes for each business design. Again, it is important to have a number of distinct, viable options to stretch the thinking of the group and to provide the opportunity for real comparison, contrasting approaches, and true choice. Ultimately, one business prototype must be selected. That decision is best made against a set of criteria developed in the strategic intent stage, and the benefits of having engaged the board at that earlier stage becomes quickly apparent at this point. The leading choices should also be tested against current organizational capabilities to understand the nature of the challenges inherent in executing each strategy. When this choice is made, initial planning of execution is complete.

The ''strategic choice'' work process usually is done over a period of months, with numerous meetings, work sessions, and rounds of data collection and feedback. This strategic choice process provides a way of building board engagement. Perhaps more importantly, management will benefit from the board's informed point of view.

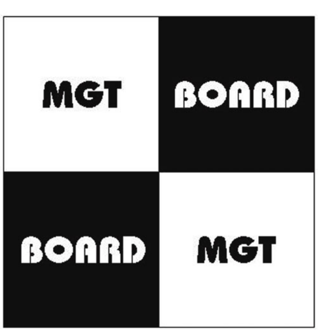
Requirements for effective board engagement in strategy

While the elements of a value-added engagement and the framework for strategic thinking and decision-making can help to effectively engage the board, not every board is prepared to participate. In our experience, addressing a set of prerequisites will set the stage for value-added participation:

1. **Balanced but diverse board composition.** The quality of the board's contributions will depend on the quality of its members, and several characteristics are particularly important. First, of course, is independence. When directors are not independent – either financially or psychologically – they may not be able to raise the difficult or challenging questions that are part and parcel of strategic thinking and decision-making. A second major requirement is specific knowledge. At least some directors need to have sufficient knowledge about the technologies, markets, competitors, or processes of the company so that they can make informed contributions to strategy development.

Corporations are waking up to the benefits of a good board mix and diversifying their boards by recruiting specific director talent, structuring new director compensation packages (to ensure independence), and increasing director pay for growing (and increasingly specific) board responsibilities[8]. Of course, board members should also possess a general wisdom, or the perspective and judgment that a director can bring as the result of his/her accumulated business experience. Finally, it helps to have some directors who have a long-term view of the business and a deep understanding of the company history, and others who bring fresh insight and new perspectives.

2. **An engaged executive team.** Strategic thinking and decision-making requires a commitment to creative teamwork by both the board and the company executives who will be responsible for leading and managing the implementation of the strategy. Effective implementation of the strategy depends on the full understanding, ownership, and personal commitment of a company's managers. Participating with the team provides the board with a tremendous opportunity to hear the leadership's multiple perspectives and also to gain insight into their capabilities as a management team.



3. **The CEO as a process leader.** For this approach to succeed, the CEO needs to be experienced, open to input, and receptive to different ideas. While the CEO can demonstrate this openness by serving as the leader of the strategic process with the board and by playing an active role in soliciting the directors' input, some CEOs use an outside facilitator to help guide the group through the process. This frees them to think about content and substance – without undermining the needed role of impartial and fair facilitator.

4. **An open and constructive board culture.** It's important for the board to have a culture – that is, a set of norms and expectations – that support constructive contention and the importance of different points of view. A board that is characterized by conformity, excessive politeness, and aversion to conflict will have a difficult time engaging in true strategic thinking and strategic decision-making. On the other hand, a CEO who seeks to move the board culture

towards more openness and constructive contention can use the strategy process as a catalyst to help make that happen.

5. **Board accountability.** The board needs to feel that it has something at stake in relation to the development and successful implementation of strategy. The increasing focus on board accountability and visibility helps. Other actions that can increase accountability include shaping the way the board is rewarded, using board and director assessment to motivate individuals to participate actively and constructively, and increasing the visibility of the board as spokespeople for the strategic direction.

The benefits of strategic engagement

In the strategic choice process, a CEO should not turn over strategy development to the board; on the contrary, the CEO and his/her executive team should lead the process – while engaging the board at every step. The underlying message here, and one that we've seen proved true time and again, is that this can be done, and it can be accomplished without management giving up its prerogative to manage and run the company. In the strategic choice process and steps we outlined for value-added board engagement, the CEO and his/her team lead the way.

We have observed a number of benefits to this approach. First, the process yields better strategic decisions that contribute to a more robust strategy than would have been developed otherwise. Second, the satisfaction of the participating directors increases significantly. They feel that they have made a contribution; they feel that their capabilities have been utilized; they feel that they have been listened to; and, ultimately, they feel that they've been able to add value. Third, the process results in an understanding of the company that will improve the quality of the board's work in the future. Specific proposals for investments, capital, acquisitions, etc. will now be considered in the context of a strategy that everyone around the table owns, rather than as isolated, one-off transactions. This typically results in more thoughtful discussion of and stronger support for proposals that are consistent with the strategic direction. Finally, the process results in strong ownership and support, which is particularly useful when the company hits a difficult period or a crisis. The board that has been engaged is much more likely to support management in times of dire need because it understands that its support is truly deserved.

Notes

1. Conger, J.A., Lawler, III, E.E. and Finegold, D.L. (2001), *Corporate Boards: Strategies for Adding Value at the Top*, Jossey-Bass, San Francisco, CA.
2. National Association of Corporate Directors and the Center for Board Leadership (2000), *1999-2000 Public Company Governance Survey*.
3. National Association of Corporate Directors Blue Ribbon Commission (2000), *The Role of the Board in Corporate Strategy*.
4. Slywotzky, A.J. and Morrison, D.J. (1999), ''Profit patterns'', *Times Business*, New York, NY.
5. We assume for this discussion the dominant US governance model, where one person holds the chairman and CEO positions.
6. The Conference Board Commission on Public Trust and Private Enterprise, 2003.
7. Nadler, D.A. (1998), *Champions of Change*, Jossey-Bass, San Francisco, CA.
8. The Wall Street Journal Reports: Corporate Governance, ''Ready and able?'' (R3, R5), and ''More work, more pay'' (R4, R5), 24 February, 2003.