How to chart the course to the board of the future

EY Global Center for Board Matters

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Building a better working world

A study by EY teams finds that board directors are increasingly under pressure. We sum up the issues, imagine the future and explore potential next steps.

Executive summary

- Board directors are juggling an increasingly large, complex workload without necessarily having adequate time, the prerequisite skill sets or access to supporting technology to adapt.
- Current trends suggest they'll need to make substantial changes to their roles, operating structures and ways of working to be fit for the future.
- Establishing a clear purpose, and aligning an operating model around it, is a good place to start. Unitary operating models are not the only option.

For years, people have been fascinated by the question of what happens when an unstoppable force meets an immovable object. And as a recent EY study of board directors and observers shows, boards would be well-placed to ask the same question of themselves.

In their case, the unstoppable force is a volatile, uncertain, complex and ambiguous (VUCA) world that includes growing regulation, litigation and stakeholder expectations, including reaching net zero. And for many, the immovable object is a governance model and skill sets that's largely remained static in the face of immeasurable change.

This perfect storm of pressures was already making it increasingly challenging for board directors to continue to add strategic value at the same pace. Add the COVID-19 pandemic and it has only worsened the problem. At the same time, it's given boards a taste of the pace, responsiveness and flexibility they'll need in a VUCA world. As board veteran David Gonski put it[1], it's tested them like never before.

A local study that tells a global story

For this study, EY teams interviewed board directors and non-executive directors, along with CEOs and CFOs, from 64 publicly listed companies and 29 private companies in Australia. We also spoke to teams within the EY organization who work closely with boards and leadership.

The findings, which we published in July 2021, equally resonated with attendees from around the world at a recent virtual event for board directors[2]. The event also confirmed our hypothesis that, despite the scale of the challenge, currently most boards are holding their own.

To be fit for an uncertain future[3], though, they'll need to make fundamental changes to their governance operating models, skills, structures, ways of working and use of technology. These changes chime with those suggested in EY 2021 Global Board Risk Survey. To find out more, take a look at the results.

At EY, we've created a series of articles to support the ongoing dialogue and discussion They cover the "what is", the "what could be" and what it'll take to bridge the gap. Below is a summary of our thinking.

[1] Six business leaders predict the future for boards, Australian Financial Review website, September 2021

[2] Decision 84, Virtual event, September 2021

[3] Hitting reset, Australian Institute of Company Directors website, October 2021

The “what is”: 20th century governance models in a 21st century world

EY teams consolidated the findings from the study into four main challenges for boards:

1. Unmanageable regulatory and legal demands. Governance failures have led to a risk and compliance overload that’s preventing boards from having strategic conversations. According to EY 2021 Global Risk Survey, that includes conversations about risk.

2. An outmoded, mostly manual way of working. This overload means some management teams are operating on the basis of “if in doubt, tell them everything”. As a result, their boards are drowning in information. And there’s little evidence of boards routinely using technology to reduce the workload or unlock the value of their data.

3. Looming gaps in skills and behaviors. As point 2 suggests, most boards have a digital skills gap. And while observable diversity is improving slowly, diversity of thought and decision-making is lagging behind.

4. An identity crisis around stakeholder priority and ESG. Boards are having to balance growing public and investor expectations[4] in these key areas with the continued demand for short-term earnings.

Issues in the wider organization can compound some of these challenges. For example, EY 2021 Global Risk Survey found that boards see technology as one of two drivers of effective risk management. But fewer than one in five board directors believe their organization uses technology for risk management in a highly effective way.

[4] Boards suffer an ‘identity crisis’ as ESG demands rise, Australian Financial Review website, September 2021

Read the first article in the series:

How Australian boards have an opportunity to become future fit

The “what might be?” five trends shaping the future of boards

What might life look like for a board director in 2030? In our view, it’ll include the better use of technology such as accessing real-time updates on risk and ESG through a board portal, and using advanced soft skills to unpack issues or priorities and reach a consensus.

EY teams have identified five trends they believe will lead boards to this brave new world.

1. A stronger stakeholder voice from a more diverse group. Many (but not all) boards will exchange shareholder primacy for creating long-term value through stakeholder engagement.

2. More transparent decision-making. Investors, consumers and prospective employees increasingly want more transparency from organizations and their boards. In response, boards will base decisions around agreed, purpose-oriented criteria, and communicate these in an open and transparent way.

3. More accountability (and consequences) for boards. Arising from the first two trends, the third will see boards use AI and broader consultation to make more considered decisions that stand up to external scrutiny. This approach will give directors the ability to defend their actions – particularly useful in countries where a fear of litigation is limiting participation by talented new directors.

4. A faster, more unpredictable pace of change. In a VUCA world, the usual governance procedures don’t apply. Boards will have to reconsider everything from the timing and mode of meetings to how they gather information and so much more.

5. Complex business ecosystems that make governance more challenging. Digitalization, globalization and dispersion (of people, organizations and supply chains) have created a mind-boggling level of complexity for boards. They’ll need to find ways to manage the considerable strategic and operational risk, and in some cases, opportunities this creates.

Read the second article in the series:

Five trends that will the shape the board of the future

What it will take to get there

What your board looks like in 2030 will depends on many factors, including your current state , levels of maturity and future ambitions. These four steps will help you to understand the "what is", the "what could be" and how to bridge the two.

Four steps on the road to reform

1. Establish what "fit for purpose" means for your operating model by looking at:
   - The long-term, societal purpose of the organization, and how to support it (for example, ESG should be embedded into the business strategy and not seen as a stand-alone).
   - The board's mid-term priorities, based on the organization's strategy.
   - Your view of your responsibilities as a board - individually and as a group.

2. Have an honest conversation about what kind of governance approach will best fit your 3Ps – long term for the organization, medium-term priorities for the board and finally, the overall purpose of the board (as a group and as individuals). Should you be shareholder – or stakeholder-centric? Should you look inwards to the organization, to keep tight control? Or outwards, to understand its vulnerabilities from an external perspective?

3. Discuss and decide in concert with management who's responsible for what and how to deal with the grey space in the middle. That includes which decisions you'll own, and what you'll delegate to the management team. Having a healthy constructive continuous dialogue with executive management is a critical success factor.

4. Develop a staged plan for transforming your governance model. Success will be about adopting the right mindset, and challenging each other to adapt over a defined period of time. Aim to make incremental changes to everything from your use of technology to your board composition.

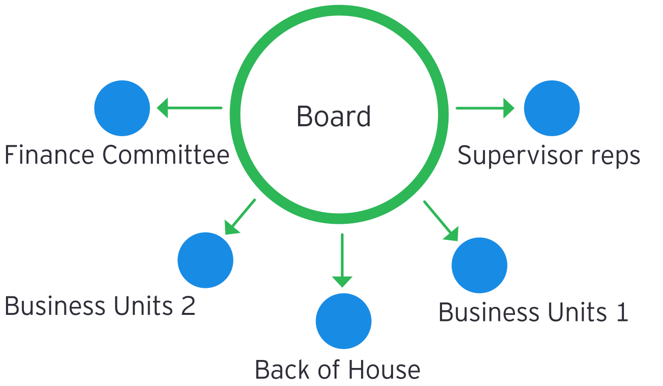
Establish a clear purpose and design a model to reflect it

EY study showed that boards recognize that in order to meet the complex demands of the future, there is a a need to review and revise their operating models.

And as the focus on purpose grows, we expect growing numbers to consider a move from the classic "unitary" model to two-tier boards and networked structures.

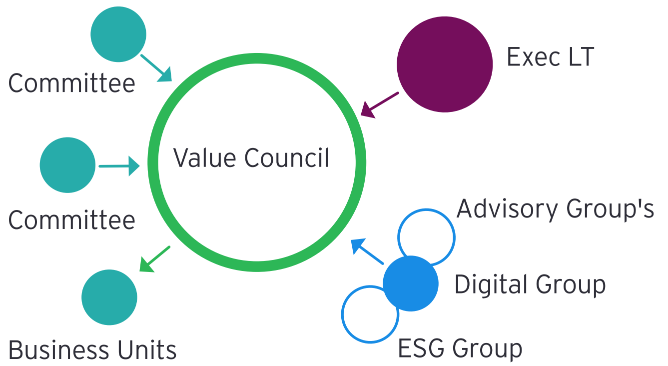
Here are three example models to explore.

Hybrid



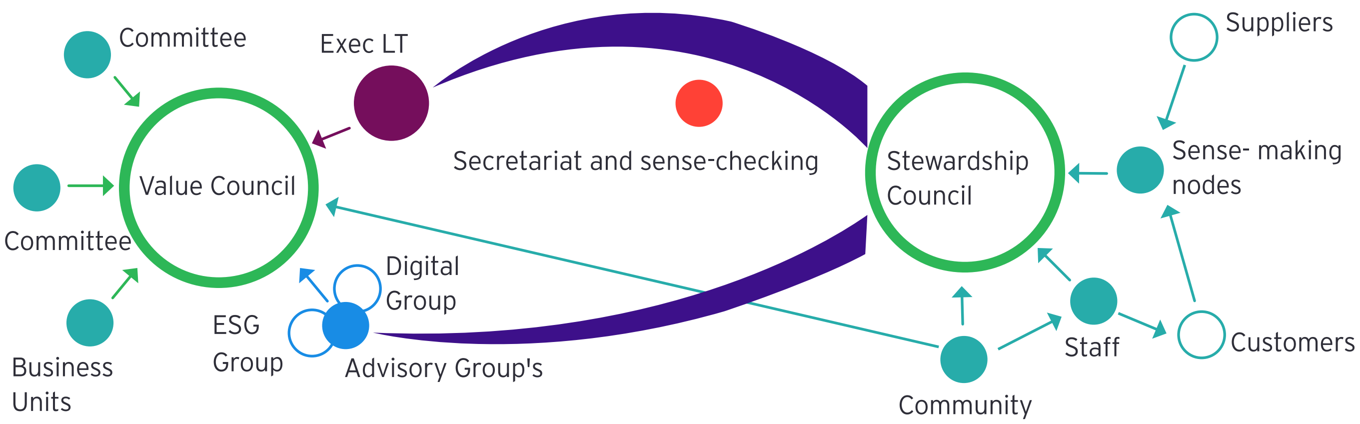
- Mixes classic and new board structures, as determined by the organization's purpose
- Aligns committees to the BU (business units) where the most value and/or biggest risks lie
- Allows input from other key stakeholders

Hub and spoke



- The board (or "value council") is still the epicenter, but shares its workload more widely
- Ideas are raised and resolved around, as well as within, the board
- Non-traditional committees support the areas creating the most value, while advisory groups help with topics such as ESG

Networked



- Instead of an omniscient epicenter, the board is a steward, responsible for monitoring and facilitating long-term value
- Satellite structures pick up stakeholder issues and feed them up to sense-making "nodes"
- The board delegates more decision-making for important responses to the nodes (which are closer to where issues emerge and the point of impact)

Read the third article in the series:

How Australian boards may look in 2030

A final thought to leave you with

If based on what you've now read, you only ask yourself one question, we suggest it's this: "If we had a clean sheet of paper, given our purpose and strategy and the way things are going in our market/industry/regulatory environment, what would we design?"

The answer may surprise you. We look forward to continuing this conversation towards 2030 and beyond.

Our thanks go to Strategy and Transformation Executive Dr Dean Blomson for collaborating with EY Global Center for Board Matters on The Board of the Future study.

Summary

A recent EY study has found that board directors are grappling with a myriad of challenges, from a static governance model to changing stakeholder expectations. To help navigate these challenges, EY teams describe the current reality (according to board directors themselves), start to paint a picture of the future that boards need to prepare for, and propose four potential ways to bridge the gap.

Want to find out more?

Download the summary findings https://www.ey.com/en_au/board-matters/board-of-the-future.

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