THE BOARD MINDSET™

The vital attribute of exceptional boards

HOW BOARD DIRECTORS CAN INTERRUPT CONFIRMATION BIAS

A well-known concept from psychology is the confirmation bias that describes people's tendency to recognize, remember, and value new information that confirms what they already believe. The idea is not difficult to understand, but it is surprisingly challenging to interrupt. Why? Because unconscious biases are more than cognitive processes, they are emotional, making it more challenging to dislodge them.

Understanding what confirmation bias is and recognizing how it can lead even intelligent, experienced people to make poor decisions is a helpful start. Few leaders take the next step even though that is precisely what is needed to reduce the likelihood that this invisible process will foil your plans. Boards need to do two things: 1. Create an environment to reduce the possibility of biases becoming decision traps. 2. Admit, first to themselves, that they are fallible.

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The first is easy to accept, but the second trickier. Why? Emotion. It's human, it's normal, but it affects thinking and decision-making more than many care to admit. The payoff, however, is terrific for the few who adopt an attitude of learning about how they think and make decisions and what influences them.

While people can't sidestep biases every time, here are three ways that can help.

Flip the Frame

Carol Tomé, CEO of United Parcel Service, served as the chief financial officer at The Home Depot for many years. In 2002, while she was CFO at The Home Depot, Sarbanes-Oxley (SOX) was passed and quickly derided by many business leaders as too costly, too complicated, and too bureaucratic. While on a panel at a governance conference, Tomé listened while every other speaker complained about the new regulation and predicted chaos, out-of-control costs of compliance, and perhaps ruin. Tomé completely flipped the frame, saying that at The Home Depot, her team of auditors were rock stars. They took up the charge not to check boxes but to be of value to the business leaders. The group was known as the "velvet hammers."

Tomé reframed the issue by reversal. She rejected the stereotypical view of auditors as nerdy, tattletales who don't understand business but are happy to take up time and resources pursuing foolish consistency.

Examine Your Assumptions

In his book, *Enterprise Risk Management: From Incentives to Controls*, James Lam details research that demonstrated the major sources of risk to 76 companies who had at least a 30 percent decline in market value. The study revealed the counterintuitive finding that 61 percent of the risk was strategic, not operational or financial, as many expect.

Lam says that one reason for this finding is that strategic risk is more difficult to evaluate than operational or financial risks because strategic risk involves assumptions that go unexamined or only lightly so. Interrogating management's assumptions can be tricky and sometimes is met with defense. Human beings tend to resist it. One thing that helps is to ask yourself questions but from the point of view of an investor. If you were investing your funds, how would you want the following questions answered?

- What business trends are relied upon in this plan?
- What do we know about customers? How do we know?
- What emerging technology will play a role and how?
- What global trends are assumed to continue or not?
- What regulatory conditions favor us?

Imagine Your Future

A process that has demonstrated value in decision-making is a pre-mortem. In this process, a group looks into the future and asks, "If we are wildly successful, what would we have done to make it so?" Conversely, "If we fail, what would we have done or not done that led to a bad outcome?" When a group allows enough time to think about the outcome they don't want and truly consider what could undermine their best efforts, it yields valuable information.

A pre-mortem is only as valuable as the changes a team makes based on the insights gleaned. Rationalization, the very human need to defend our point of view, often kicks in and derails our intentions. Asking a few questions and digging beneath conceptual answers will clarify what needs to be done and who must do it to improve the odds.

- What did we do well that exemplifies a strength we currently have? Are we capitalizing on it?
- What did we minimize because it's hard to define?
- Do we deeply understand the causes of our success when we perform well?
- What vital aspects of leadership have we defined and taught to others that led to good outcomes? What have we not taught others that we should?

Emotion is an inseparable part of being human, and quashing it impossible. Far better for boards to create a culture of openness that enables them to use their curiosity, admit what they don't know, and ask questions that allow them to govern as well as they intend.

Helping Define Your Company's Future Success

We can help you formulate a strategy that works:

- Defines the choices a company is making about who is and who is not a customer
- Doesn't serve as a rationalization for budgets
- Challenges assumptions
- Seeks to reduce risk, not avoid it
- Serves as a framework in which adjustments are expected and can be accommodated

We advise on any unaddressed issues to help the board and the company move forward. If you have any questions about The Board Mindset, visit www.theboardmindset.com or contact us.