



ISSUE 110

BOARD PERSPECTIVES: Risk Oversight

OVERSIGHT OF DIGITAL TRANSFORMATION

Disruptive innovation has a clear impact on the half-life of companies' business models. Industry disruption and digital transformation present a new frontier of opportunity and risk that is shaping — and speeding up — business model changes.

A recent global survey of board members and C-suite executives cited the inability to compete with “born digital” competitors, resistance to change and disruptive change to the business model as top risks for 2019.¹ These risks were not at the forefront of many senior executives' and board members' minds just a few years ago.

To gain perspective on this important area of board oversight, Protiviti met in August 2018 with 20 active directors during a dinner roundtable at a National Association of Corporate Directors (NACD) event to discuss the board's oversight of industry disruption and digital transformation. Below are some important takeaways from that discussion.

Evaluate digital readiness. Digital leadership requires a certain state of mind. It is about changing the way an organisation acts and thinks in everything it does. To be successful, executive management must prepare the organisation to compete in the digital age. They must also assess the extent of digital know-how across the company. Is the organisation a follower or a leader? If it is a beginner or a sceptic, does the board encourage management to advance its digital maturity? Can management identify and act on the strengths and weaknesses across the business in the context of the digital vision, mission and strategy?

¹ *Executive Perspectives on Top Risks 2019*, Protiviti and North Carolina State University's ERM Initiative, December 2018, available at www.protiviti.com/US-en/insights/protiviti-top-risks-survey.

Management can have the best possible strategy, but the organisation can't execute it if the business is not digital-ready. It is also difficult to formulate a viable strategy if the organisation is not digital-ready. It helps if the company benchmarks itself against the competencies at which digital leaders excel to better understand the pathway to achieving digital readiness. Protiviti offers a framework² to help organisations conduct this assessment.

Understand what transformation entails.

Digital familiarity and literacy are the keys to probing management about the company's advancement as a digital entity, particularly when augmented by digital-savvy experience. True digitalisation starts at the core. The board, therefore, must transform itself before it can offer effective oversight of the organisation's digital journey. Just as a strategy that attempts to layer technology on an analog business does not work, neither can a board consisting solely of directors who grew up in the analog age contribute effective oversight without substantive steps taken towards digital literacy and digital savviness.

One option may be to form an innovation committee, with technology, digital and transformation experts as members. Another is to include directors with the requisite technology expertise on the board to complement the directors who grew up in the analog age. Yet another option is to engage outside advisers to inform the board with relevant perspectives.

Focus on resiliency and agility. In the digital era, good governance may need to be different than even five years ago. Boards need to sharpen their focus on innovation initiatives and on changing the organisation's mindset concerning digital. People and culture are the keys to success in digital transformation. If an organisation has effective digital leadership, enhances the digital capabilities of its people, and creates a corporate culture that incents

and empowers creativity and innovation, it will become a truly digital organisation. Changing the mindset also requires effective communication by management of a compelling narrative regarding the company's focus on digital transformation and the need for change.

The board can play an important role in fostering a resilient and agile mindset by allocating sufficient agenda time to discussing the company's innovation strategy and culture and encouraging open discussion on direction and progress. This requires constructive engagement with management with broader, more diverse perspectives regarding how the organisation should embrace digital opportunities. The dialogue should be supported with appropriate innovation-specific metrics that tell the full story of how the strategy is performing, what the return on investment is, and how effective the company's innovation culture and capabilities have become.

Keep an eye on the customer experience and competitive advantage. How can directors ensure that management has its act together, has the right team and competencies in place, and is taking the organisation down the right path? A customer-centric approach to digital strategy breeds confidence that the organisation is making the right moves.

Success in executing on digital initiatives is about knowing the company's limitations and avoiding procrastination on making the difficult decisions to address those limitations. A strong focus on the customer is a powerful driver for moving forward. For example, data strategy and legacy infrastructure issues (e.g., technical debt) are examples of difficult problems that are often ignored. But with a commitment to enhancing the customer experience and commanding customer loyalty, companies can overcome this inertia and do what it takes to remain competitive.

² See <https://landing.protiviti.com/digital>.

Ensure there is a compelling plan that fits market realities. Directors need to ensure that management formulates a viable plan for managing business disruption and transformation and executes that plan. This isn't easy given the uncertainty in determining the appropriate technologies to embrace, new products and services to offer, third-party ecosystem supplier and distribution channel partners to engage with, and the changes to make in the business. Under the auspices of the board, management must measure and monitor progress. As noted earlier, a digital readiness assessment can help with this by clarifying the organisation's strengths and weaknesses so that management knows where to focus on its journey to digital maturity.

As many companies have announced significant digital investments, it is important for the board to take the long-term view in creating a platform for sustainable growth even at the

risk of a short-term drop in share price. The alternative is a steady decline over time that management is powerless to correct. Directors should be mindful that investor sentiment can shift quickly as digital capabilities become essential to compete. Over time, investors will be looking for CEOs to articulate a compelling digital vision and plan. Accordingly, no one should be waiting until it's too late to act.

Consider human(e) digital transformation.

A clear and coherent strategy is needed to address worker dislocation and displacement. That was a critical issue in the room during the NACD event, which no one took lightly. In fact, several participants continued to discuss it after the roundtable concluded. Currently, the answers are elusive.

For a more complete look at this roundtable, including key takeaways, read Protiviti's full summary of the event at www.protiviti.com/US-en/insights/insights-active-directors.

Questions for Boards

Following are some suggested questions that boards of directors may consider, based on the risks inherent in the entity's operations:

- Does the board have access to the expertise and experience needed to understand how digital disruption can affect the organisation and its business model?
- Is the board satisfied that management understands and is immersed in digital business concepts, digital ecosystems and digital hyper-scaling platforms that are ready to facilitate growth? Are there barriers to innovation and digital transformation within the organisation that require the board's and executive management's attention?
- Does the board agenda allocate time for discussing the company's innovation strategy and culture and encouraging open discussion on direction and progress? Is this dialogue supported with appropriate innovation-specific metrics?

For more questions for boards to consider, see Protiviti's full summary of the roundtable event at www.protiviti.com/US-en/insights/insights-active-directors.

How Protiviti Can Help

Digital transformations generally seek to accomplish one or more key objectives: exploring and creating new ways to build strong relations with customers; the digitisation of products or services, which involves launching new, enhancing existing, or exploring innovative business models for products or services; enhancing business analytics and decision science to improve decision-making; or creatively using technology to improve operational performance. We have experience collaborating closely with clients to help them achieve their business objectives in a variety of ways. Since each transformation is unique, we tailor the following competencies to fit your organisation's strengths and needs:

- **Digital transformation, governance, strategy and execution** — Ensuring that transformation programmes are established, well defined, set up for success and support execution.
- **Functional transformation and improvement** — Using technology to reinvent finance, information technology, business operations, procurement, risk management and audit.
- **Enabling an innovation culture** — Ensuring that the unnecessary barriers to innovation and change that exist within organisations are eliminated.
- **New technologies assessment and implementation** — Supporting organisations with decision-making as they consider whether to embrace new or emerging technologies.
- **Business analytics and decision science** — Helping organisations manage increasingly complex data architectures and transform data into information.

Is It Time for Your Board to Evaluate Its Risk Oversight Process?

The TBI Protiviti Board Risk Oversight Meter™ provides boards with an opportunity to refresh their risk oversight process to ensure it's focused sharply on the opportunities and risks that truly matter. Protiviti's commitment to facilitating continuous process improvement to enable companies to confidently face the future is why we collaborated with The Board Institute, Inc. (TBI) to offer the director community a flexible, cost-effective tool that assists boards in their periodic self-evaluation of the board's risk oversight and mirrors the way many directors prefer to conduct self-evaluations. Boards interested in using this evaluation tool should visit the TBI website at <http://theboardinstitute.com/board-risk-meter/>.

Learn more at
www.protiviti.com/boardriskoversightmeter

Protiviti is a global consulting firm that delivers deep expertise, objective insights, a tailored approach and unparalleled collaboration to help leaders confidently face the future. Protiviti and our independently owned Member Firms provide consulting solutions in finance, technology, operations, data, analytics, governance, risk and internal audit to our clients through our network of more than 75 offices in over 20 countries.

We have served more than 60 percent of *Fortune* 1000® and 35 percent of *Fortune* Global 500® companies. We also work with smaller, growing companies, including those looking to go public, as well as with government agencies. Protiviti is a wholly owned subsidiary of Robert Half (NYSE: RHI). Founded in 1948, Robert Half is a member of the S&P 500 index.

Protiviti partners with the National Association of Corporate Directors (NACD) to publish articles of interest to boardroom executives related to effective or emerging practices on the many aspects of risk oversight. As of January 2013, NACD has been publishing online contributed articles from Protiviti, with the content featured on <https://blog.nacdonline.org/authors/42/>. Twice per year, the six most recent issues of *Board Perspectives: Risk Oversight* are consolidated into a printed booklet that is co-branded with NACD. Protiviti also posts these articles at protiviti.com.