



Disruption and Innovation: How Does the Board Adapt?

September 12, 2016

The Chicago NACD's 2016-2017 season began with a lunch presentation by Sam Yagan, CEO of e-commerce competitor ShopRunner. Named to TIME Magazine's 2013 list of the "100 Most Influential People in the World, Yagan has significant entrepreneurial experience; he co-founded SparkNotes in 1999 during his senior year at Harvard and co-founded OkCupid in 2003. He also served as CEO of Match.com.

Yagan discussed the critical importance of innovation and disruption in creating strategic models for today's fast-changing business environment. Using his development of SparkNotes as an example, Yagan noted that his experience as a student, combined with the burgeoning powers of the Internet, led him to correctly identify key vulnerabilities in the antiquated CliffsNotes print model so prevalent on college campuses at the time. SparkNotes' strategy of immediate on-line availability very effectively disrupted CliffsNotes' 80% share of the study guide market, and Yagan and his business partners sold SparkNotes to Barnes & Noble one year later. Yagan's lesson for board members is to be just as watchful for "sins of omission" as "sins of commission;" CliffsNotes' downfall was its failure to recognize how a new, innovative business model could decimate its own long-term strategic path. Yagan noted that Barnes & Noble's board also eventually committed its own sins of omission by neglecting to recognize the e-book trends successfully pursued by its competitors. As a board member, continually ask management, "What are we not doing? What are we missing?"

Yagan talked next about what he called the "birth" of Tinder. Post SparkNotes, Yagan and his colleagues founded OkCupid, another disruptive category entry, this time as a free offering in the on-line dating space. Yagan ultimately sold OkCupid to Match.com, became CEO of Match, and founded Tinder, an innovation he calls his biggest accomplishment. Yagan opened "labs" throughout Match to develop Tinder, describing a standard line-iteming budgeting process to fund this start-up. What he didn't "budget" for was the startling, disruptive success of Tinder. While business model disrupters like SparkNotes, OkCupid and Tinder typically provide category expansion over the long-term, they almost always cannibalize share from market leaders in the short term. Tinder grew faster and took more share than anyone expected, its success and its resource needs far outpacing its original profit and loss budgets. While the board understood and agreed with Yagan's plans to grow Tinder, Yagan discussed the intense pushback he received from long-term employees dismayed by the cultural and management disruption caused by Tinder's success. Yagan cautioned attendees to anticipate internal as well as external concerns when funding and supporting disruptive, albeit innovative, products and services.

Yagan next offered observations from his various board experiences, advising directors to take their role as potential disrupters seriously. As a member of the Advisory Council at the Stanford Graduate School of Business, for example, Yagan and his fellow directors have debated whether the MBA is "going away," and what role Stanford should have in the degree's long-term continuation. Yagan discussed the importance of "dogfooding," making sure that board members and senior executives remain very familiar with their company's products and services; Yagan is a board member of SpotHero, and he describes himself as the company's second largest customer. He recommends board members accompany management on sales

calls as appropriate, noting that experiences in the field have transformed his ability to give counsel. Board members ultimately must do whatever necessary to remain active and innovative company participants; Yagan officially offers his resignation at the end of each board term, for example, in order to avoid complacency and to ensure that his participation is an active decision by all involved.

The question and answer period returned to several themes developed by Yagan during his remarks. When asked how directors should balance offering innovative ideas versus meddling, Yagan recommended that directors focus on questions requiring management output rather than interference involving board input. Yagan also advised nominating committees to search a little harder for younger, accomplished members to add to their boards. Yagan strongly advised directors to help companies create cultures in which failures are not only tolerated, but encouraged; he referenced the recent rocket launch failure at SpaceX by suggesting that management be encouraged to ask "what's your rocket?" at all employee performance reviews. Lastly, when choosing to join a board, consider the relationship between the CEO and directors and among the board members themselves; make sure board members are encouraged to meet with executives, ask questions and really understand the company and its strategies.