TOMORROW'S CHALLENGES

THERANOS FOUNDER FOOLED INVESTORS WITH THE PROMISE TO REVOLUTIONISE HEALTHCARE – IT OFFERS THREE BIG LESSONS FOR COMPANIES

ELIZABETH HOLMES HAS BEEN CHARGED WITH 'MASSIVE FRAUD'. SHE MAINTAINS HER INNOCENCE BUT WHAT LESSONS CAN BOARDS TAKE AWAY FROM THE WHOLE AFFAIR?

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Less than three months after being charged by the US Securities and Exchange Commission(SEC) with "massive fraud" and barred from being the CEO of a public company for ten years, entrepreneur Elizabeth Holmes is reportedly on the hunt for investors for a new company.

She is still allowed to be the CEO of a privately held company – but would-be investors should heed the lessons from Holmes' last venture, Theranos.

In 2003, 19-year-old Holmes dropped out of Stanford and founded the health tech firm, Theranos. It worked in "stealth mode" for a decade while developing new technology to perform many standard medical tests using only a single drop of blood. After unveiling the company's device and its plans to revolutionise the healthcare industry, Holmes was heavily profiled in the media and embraced the role of guru.

Holmes had a US$4.5 billion share of the company, which was valued at US$9 billion at its peak in 2014. But, in March 2018 the SEC charged Holmes and Theranos "with raising more than US$700m from investors through an elaborate, years-long fraud in which they exaggerated or made false statements about the company's technology, business, and financial performance."

Neither Holmes nor the company admitted (or denied any wrongdoing) but agreed to a settlement that effectively stripped Holmes of control of her company and she was fined US$500,000.

Holmes was compared to Apple's Steve Jobs. EPA/John G. Mabanglo

There are lessons that we can learn from this spectacular fall. At first glance, it raises concerns about the role of board members in carrying out their clear fiduciary duties. For a US corporation this includes, but is not limited to, "the duty of care": to exercise one's independent judgement with skill and diligence.

Theranos' board seemingly overlooked a systemic and long-term fraud. And yet its members were preeminent public figures – three former cabinet secretaries, two former senators, as well as retired high-ranking military officials. While Theranos' board has been criticised for not including industry experts, its members were highly knowledgeable about governance, and would have been aware of their fiduciary responsibilities.

There are three insights from Theranos' failure, which apply to any new company – and would-be board members of Holmes' next venture.

1. The danger of sticking to what you know

We know from the study of group dynamics that groups talk about what they know. Members of any group – including boards – discuss topics such as what they accomplished together, the good old days, common friends and the familiar. The dark side of this underlying, subconscious force is that groups do not talk about what they do not know.

So, while the Theranos board members could add value to Theranos – they were knowledgeable and competent in their fields – they, too, were subject to the forces of group dynamics and we can speculate on whether they might have avoided discussions of the unknown. Did they, for example, deeply interrogate Holmes' technological tool box to understand the company's main product? You simply cannot talk about what you do not have the knowledge base for.

2. Watch out for fairy tales

Theranos was a Silicon Valley fairy tale. A young, charismatic CEO proposes a revolutionary, industry changing idea that will heap rewards on all involved. These seductive, too-good-to-be-true stories do become real in Silicon Valley – think Facebook, Google, Apple.

But Theranos had the elements of a modern Rumpelstiltskin – with the false promise of gold being spun from nothing. Holmes – a college dropout, visionary and charismatic entrepreneur – claimed Theranos would revolutionise the healthcare industry with its ability to perform 240 common blood diagnostic tests with a single drop of blood. It's the role of the board to truly understand their company's product and ask the difficult questions – we therefore have to question whether Theranos' board might have enabled or failed to stop the creation of this particular fairy tale.

3. Spot self-deception

Finally, as CEO, surely Holmes knew that her company's technology did not perform as promised. Yet she repeatedly, convincingly and passionately maintained that it did. This begs the question: at what level was she deceiving herself?

It also raises the issue of how our culture likes to create heroes so much that some become completely invested in their own hype. Still, neither Holmes nor Theranos admits any wrongdoing. Holmes' behaviour as CEO of Theranos is similar to that of disgraced cyclist Lance Armstrong in that they both were unshaken in their belief in themselves despite being exposed to the public.

Ultimately, all groups – boards, teams, families – are subject to unconscious processes. The decisions that boards make are the outcome of just such group processes. Therefore, members need to build their awareness of unconscious dynamics within their group.

Developing this kind of insight takes work, and is extremely uncomfortable. But doing so can help the board carry out its fiduciary

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