IN TOUCH WITH THE BOARD

One in a series of communications from the Russell Reynolds Associates' CEO/Board Services Practice, ***In Touch with the Board*** addresses best practices in board composition, assessment, succession planning and other critical corporate governance issues.

A Russell Reynolds Associates' Series: Issue 4, 2008

A Practical Guide to CEO Succession Planning

In this issue, Clarke Murphy and the CEO/Board Services Practice discuss the specific elements and timeline of a successful CEO succession plan, as well as the steps necessary to ensure a smooth transition.

The transition from one CEO to another is a critical moment in a company's history. A smooth transition is essential to maintain the confidence of investors, business partners, customers and employees and provides the incoming CEO with a solid platform from which to move the company forward. A properly designed and executed succession plan is at the center of any successful transition.

CEO vacancies can be planned or unplanned; in either scenario, by the time a succession plan is needed it is far too late to start building one. Because of this, it is the responsibility of the board to make succession planning a priority, even in the face of more immediate and tangible issues. In addition to being necessary for risk mitigation, succession planning brings with it several beneficial byproducts:

- It provides a framework that drives senior executive development, aligning leadership at the top of the enterprise with the strategic needs of the firm.
- It gives the CEO, through an ongoing analysis of the job requirements, the opportunity to adjust his or her role in light of changing business conditions and strategic imperatives.
- It strengthens the relationship and information flow between the board and the senior management team through the regular contact that is part of the board's review of candidates.

Russell Reynolds Associates regularly advises boards and CEOs on chief executive officer succession planning, and from this experience we have developed the following practical guide to the succession planning process.

Establishing the Foundation

Succession planning is usually directed by the governance or compensation committee, or occasionally a special ad hoc committee. The current CEO's involvement varies (depending on whether the succession is planned or unexpected) with primary responsibility being the development of internal candidates. The lead director often acts as the single point of contact between the board and the sitting CEO on succession matters.

Create a written succession plan.

This document should detail how the company's officers are elected and replaced, how successors are to be chosen, and the respective roles of the CEO, the board and the various board committees in the succession process. Emergency succession procedures, in the case of sudden death or vacancy, are also included. Agreeing on these elements before there is a need to implement them helps ensure an orderly, deliberate transition while avoiding uncertainty and destabilizing political maneuvering.

Conduct regular, in-depth reviews.

The entire board, together with a senior human resources executive, should review the succession plan twice a year, including an examination of the relevant bylaws and succession procedures and a review of the baseline capabilities requirements for the next CEO—a working document that summarizes what these requirements would be if the search for a new CEO were held today.

To determine those prerequisites, the board should begin by examining company direction and strategy over a five- to ten-year time period, factoring in the impact of various scenarios such as how the business will be affected by challenges including the continuing globalization of supply chains, customers, competitors and investors, or the risks and opportunities brought by changing climate and global health conditions. Looking at the impact of broad trends such as these helps ensure that the company's next leader will have the capabilities and experience necessary to respond to unfolding complex events across numerous fronts. The board should also use this opportunity to observe successful CEOs from both inside and outside the industry and identify traits that have contributed to particular successes.

The board then distills these considerations into a set of required capabilities. The Russell Reynolds Associates' Assessment Framework offers one model for implementation. Based on the company's situation and strategic direction, some capabilities will be deemed essential and others of secondary or little importance.

Compare the resulting list of capabilities against the firm's senior talent pipeline.

While human resources manages the day-to-day aspects of measuring development, the board should be briefed annually and have regular exposure to internal candidates through board presentations, field observations and site visits. Revise the leadership development plan of each candidate as needed to address progress and shortcomings.

Boards can decide to bolster this talent pipeline by recruiting from outside. This necessitates significant advance planning; bringing in a senior executive who could potentially go on to fill the CEO role typically requires a three-year lead time so that the candidate will have fully been absorbed into the firm's culture by the time that the elevation takes place.

Narrow the field to two or three finalists.

This typically occurs two to three years from the planned date of CEO transition, with input from the full board and the CEO. The final round of professional development for the candidates should be designed so that they are exposed to multiple aspects of the business and are given responsibility for key initiatives—such as overseeing entry into a new geographic region or the integration of an acquisition—that will mirror the sorts of complex challenges they would have as CEO while giving the board an opportunity to evaluate their performance.

Although there will be plenty of internal and external speculation at this point in the succession process, it is important to defuse any aura of competition that may develop; finalists should not be pitted against each other, but given separate domains in which to lead and the opportunity to build programs that will contribute to the company's profitability over a sustained period.

Implementing the Plan

Assess the finalist candidates.

Approximately one year before the planned transition, the full board should meet to implement the succession plan. The CEO competency list should be given a final review and revised as necessary. The board should then implement a thorough assessment of the finalist candidates, including:

- **In-depth competency-focused interviews** that probe for the skills and talents essential for the role;
- **360° referencing** that provides added insight from superiors, industry peers, colleagues and direct reports; and
- **Online psychometric testing**, interpreted by an Executive Assessment psychologist, which gives shape to intangible qualities.

CEO Competencies and Success Factors

Vision and Strategy

- Agile and able to integrate material from a wide range of learning and thinking, operates effectively in complexity and ambiguity
- Develops a "core" understanding of issues that challenges assumptions and the superfluous, distills the complex
- Both optimistic (expects success, frequently identifies potential and opportunity, never feels a victim and takes calculated risks) and realistic (practical, assertive, evaluates the situation and clearly identifies problems)
- Anticipates problems and opportunities, both reflective (considers multiple "angles," considers the short- and long-term ramifications of decisions and actions) and decisive

Ensuring Tactical Success

- Can be hands off or hands on, depending on the situation
- High standards for self and others, competes with self
- Active manager of performance/drives execution by clarifying priorities, confronts problems and problem performers
- Hires, develops and retains truly excellent talent

Relationships and Communication

- Insightful regarding others
- Capable of empathy and effective listening
- Can communicate effectively with different internal and external constituencies

Motivation

- Interested in being/motivated to be CEO, willing to put in time and effort

Business

- Created and maximized success in more than one business entity
- Demonstrated ability to sustain commercial value in a business
- Raised the profile of his/her previous business entity
- Overall experience leads to credibility with board and investors/owners

Fit to Situation

- Fit to current and upcoming business stage/scope/scale
- Fit to current and upcoming business strategies and tactics
- Fit to current and aspired organizational culture
- Fit to and/or actual experience in industry/market

Measure internal candidates against their peers at other firms.
This will ensure the company is choosing the best CEO available, rather than merely the best choice from within its own ranks. The customary approach is to turn to independent senior search consultants, who then identify the most appropriate candidates in the marketplace. This list often includes not only candidates from within the industry in question but those from adjacent industries as well, to ensure that all of the best candidates are being considered.

On the basis of this information and the many other data points which have been amassed during the assessment period, internal candidates and the external benchmark candidates are given numerical rankings across the various required competencies, as illustrated on the following page. The board's governance committee, usually with the assistance of outside consultants, also produces a detailed written evaluation.

The board deliberates and makes its final decision.
If the board cannot come to an agreement on an internal candidate, it will need to conduct an external search to widen the pool. However, the foundation for an external search, including identified CEO competencies and the list of external benchmark candidates, is already in place.

The Successful Transition

Once a final candidate has been selected, it is critical that a thorough transition plan be developed so the new CEO has the benefit of a strong start. A solid transition spans a full year and contains five phases, which we have developed in conjunction with Jack O'Kelley of Katzenbach Partners:

1. **Begin intensive knowledge sharing.**
   The outgoing and incoming CEO meet frequently for in-depth discussions regarding the operating styles, histories and expectations of board members and senior management, as well as other stakeholder constituencies, including investors, creditors, customers, analysts and regulators. At various points, individual members of the senior management team are included in these discussions. Third-party interviews can help prevent the biasing of information.

2. **Communicate with stakeholders.**
   Following this briefing period, the incoming CEO should be introduced to the company's stakeholders in a series of information-gathering sessions. This allows the outgoing CEO to gracefully pass the baton and for the incoming CEO to build support and goodwill with various key players, especially those he or she has not dealt with before.

3. **Develop a written transition plan.**
   With the involvement and support of the senior management team, a detailed timeline is then developed to provide the orderly transition of roles and responsibilities. If the appointment is an internal promotion, this includes the elevation of the executive who takes over the new CEO's former position. If the outgoing CEO is remaining as Chairman, that role needs to be clearly defined so as to not interfere with the new CEO.

Assessment Report

	Vision and Strategy	Ensuring Tactical Success	Relationships and Communication	Motivation	Business	Fit to Situation	Personal Average
Dunn, Denis	3	4	3	2	3	2	**2.8**
Foss, Darren	3	4	1	2	3	2	**2.5**
Hatcher, Allan	5	5	5	4	5	4	**4.7**
Mass, Barham	4	5	3	3	4	5	**4.0**
Melon, Patrick	4	4	4	4	3	2	**3.5**
Schmidt, Kevin	3	2	3	4	4	3	**3.2**
Schneider, Joyce	4	3	3	2	5	2	**3.2**
Sharp, Jeff	5	4	2	2	5	3	**3.5**
Smart, Kelly	3	4	2	3	4	2	**3.0**
Sully, Clenton	3	2	4	4	3	3	**3.2**
Overall Group	**3.7**	**3.7**	**3.0**	**3.0**	**3.9**	**2.8**	**3.4**

Competitive Benchmarking

TIER 1 Best candidate available in the market for this position	**TIER 1** Hatcher, Allan
TIER 2 Would present as candidate without reservations	**TIER 2** Mass, Barham Melon, Patrick Sharp, Jeff
TIER 3 Would be presented as a candidate with reservations	**TIER 3** Schmidt, Kevin Schneider, Joyce Sully, Clenton
TIER 4 Would definitely not be presented as a candidate for the position	**TIER 4** Smart, Kelly Dunn, Denis Foss, Darren

4. **Share the transition plan.**
The plan needs to be effectively communicated internally and externally to project a sense of stability and positive perspective. Appropriate recognition of the outgoing CEO is an important component; failing to show appreciation for an outgoing leader's legitimate accomplishments risks alienating his or her supporters in the company and on the board.

5. **Strengthen relationships with the board.**
Even if the new CEO is known to the board, it is important that they begin to relate to him or her in the new role through one-on-one meetings. If the new CEO is appointed from within, he or she can begin to be phased into board meetings over a period of time. To the extent possible, the lead director should provide coaching and feedback to his or her successor throughout the process.

The Board's Ultimate Responsibility

Managing the CEO succession process is a board's ultimate responsibility. A regularly reviewed and closely followed succession plan is essential to successfully exercise that responsibility. The costs of shortchanging this process are easy to see when companies are caught off guard by events; the payoff is reflected in the company's momentum as it moves from one leader to the next. In addition, ongoing succession planning helps the board to be better informed and aligns the development of the senior management team with the strategic needs of the company. Beyond its usefulness in risk mitigation, CEO succession planning contributes to the successful governance and management of the firm long before a successor is needed.

Author

Clarke Murphy is a Managing Director at Russell Reynolds Associates. Clarke has more than 18 years of experience in recruiting for board of director, CEO and senior-level executive positions for leading global corporations.

About Russell Reynolds Associates

Leadership. In today's ever-changing global business environment, success is driven by the talent, vision and leadership capabilities of senior executives.

Russell Reynolds Associates is a leading global executive search and assessment firm with more than 300 consultants based in 39 offices worldwide. Our consultants work closely with public and private organizations to identify, assess and recruit senior executives and board members to drive long-term growth and success. We value teamwork, serving our clients with a collaborative approach that spans our international network of sector and functional experts.

Our in-depth knowledge of major industries and our clients' specific business challenges, combined with our understanding of who and what makes an effective leader ensure that our clients secure the best leadership teams for the ongoing success of their businesses. For more information, please visit us at www.russellreynolds.com.

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