

The Big Three Questions for Boards

By Ken Taylor

As boards complete their adjustment to the many detailed regulatory compliance requirements that corporate governance reforms have imposed on them in recent years, it may be appropriate for them to step back and address the big three questions they fundamentally must answer for the company's shareholders.

- ◆ Who owns the company?
- ◆ Who runs the company?
- ◆ Where is the company going?

It's easy to lose sight of these inextricably related questions as boards immerse themselves in oversight responsibilities centered on the three principal committees of audit, compensation, and nominating/governance. Indeed, when one considers the ever increasing velocity of mergers/acquisitions, hedge fund activities, and the continually decreasing length of CEO tenure, the evidence would suggest that Boards need to get out of the "committee weeds" and function more as a group, on a regular basis, around the three big questions that might be summarized as Outcomes, Succession, and Strategy.

With respect to the first question, boards generally assume "no change" and often adopt a "poison pill" and a classified board to help ensure that ownership is difficult to change. However, with the increased pace of global competition, industry consolidation, and the growing scrutiny and investments of private equity firms and hedge funds, boards regularly should be discussing the company's relative position in the industry and the absolute performance of the company and its units. Capital movement is unemotional, efficient, and drawn rapidly to opportunities where existing oversight and management are deemed to be ineffective, under-performing, or non-competitive. Thorough and regular discussions by the board *as a whole* around possible outcomes, given the performance, direction, and timelines of the company, would prevent purely reactive stances to unexpected events that may trigger Change in Control clauses. A regular outcomes agenda item at board meetings also would help keep the board focused on the fundamental reason for the company's existence and help prevent its demise. Consider the fact that only 186 of the companies that comprised the *Fortune 500* in 1980 are in existence today. Think about this – during



the last 25 years, 63% of the *Fortune 500* companies have ceased to exist as independent companies. Our bet is that research would show that, in almost every case, the boards of these 314 companies were thrust into a reactive mode as a result of an unexpected suitor at their door. Had there been regular, earnest discussions of outcomes by the board prior to the occurrence of such an unexpected event, the directors might better have anticipated, or even controlled, the eventual fate of the company. At the very least, a regular discussion of outcomes by the board would have led the directors to consider the next two questions – who runs the company and where is it going?

With respect to the question of who is running the company, evidence would suggest that the traditional decision making process on CEO succession planning and recruitment is flawed. It can't be that just because more people are "watching" and being more "demanding", CEOs live shorter lives, akin to an NFL or other professional athlete. Why has the average tenure of a CEO dropped to a range of three to five years? If directors are the institutional memory of a company and supposed to provide somewhat constant oversight and direction over expected director tenures of ten to fifteen years, do they really want to replace a CEO three or four times during their terms? This frequency of leadership change may be indicative of a board that is not appropriately focused on outcomes or strategy – or does not understand the inextricable linkages between outcomes, succession, and strategy.

"Getting it right" with respect to the CEO is really hard work. When done correctly, the board may focus its time and energy on the principal issues of outcomes and strategy. More often than not, however, the board is forced into a reactive mode on the issue of CEO succession, as often is evidenced by the formation of an Ad Hoc CEO Selection Committee. We'd like to submit that if the board is simultaneously and regularly considering outcomes and strategy, the directors will have a clear understanding of the competencies and experiences needed in the CEO, both now and in the future, and be able to better (i) evaluate the CEO and (ii) design and align succession planning processes to ensure it has multiple options along different points in the CEO succession timeline. This will help ensure stable leadership and the ongoing success and viability of the company – some companies, like GE, seem to have perfected this. We'd like to further submit that with respect to succession planning, boards should take on this responsibility themselves, possibly with the assistance of third-party advisors, and involve, but not rely upon, company management. *And they should do this long before the need arises to replace the CEO.* Organization design and re-design, executive development, CEO evaluation, and external benchmarking of companies and executives should be regular components of the CEO succession planning process. If a company's



performance relative to its peer group is not in the top quartile, the board has the first chance to help direct it there. Examination of what's working and who is making it happen in the competitors is worthy of a board's time – especially as it ponders the company's strategy.

Turning to the third question, where is the company going, we'd like to submit that it is impossible to select a CEO or orchestrate a succession planning process if the board does not have a clear view of the future and the implied competencies and experiences the company's CEO must therefore have to successfully and competitively lead it. While this may seem obvious, we believe that process may supplant substance in this area. Has the board ensured that the CEO has (i) directed a robust strategy development process, (ii) led an iterative process with the board to discuss and agree on a corporate strategy, and (iii) aligned the corporation's operations and people development initiatives with the board approved strategy? If a third party were to ask each director, independently, to describe the company's strategy, would each answer end up on the same point of a compass? Is the board, *as a whole*, aligned with the strategy such that the directors easily can make the human and financial capital allocation decisions of “enter, exit, fix, grow, or shrink”?

Has the board “connected” value creation with executive development and selection processes? Has the board anticipated the challenges confronting the company and taken decisions to position it competitively? What percentage of a board's decisions could be classified as being reactive?

As a board ponders these questions and assesses its preparedness and effectiveness with respect to outcomes, succession, and strategy, it may find it advisable to retain an independent advisor who is not beholden to management, emotionally or financially, and who will serve as the thought and execution partner with the board. Only through the adoption of a linked, rigorous, fact and competency-based assessment of the company, its leadership and strategy, will the board be able to properly discharge its fiduciary responsibilities to shareholders and positively impact the outcomes of the company. While the big three questions are the responsibility of the board, it may find it advisable to expand the scope of the Nominating/Governance committee and encourage it to obtain the outside counsel and support to which the Audit and Compensation committees have become accustomed.

Taylor Meyer Associates is an independent and trusted advisor to Boards on matters relating to outcomes, succession, and strategy.



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Ken Taylor is the founding partner of Taylor Meyer Associates. He is recognized as a trusted global advisor to boards, CEOs and senior leadership teams on matters relating to Board composition, Director recruitment, CEO succession planning, and senior leadership team recruitment.

During his prior 17-year career with a leading global executive search firm, Ken was a senior partner and served as one of eight Executive Committee members, the sole U.S. managing partner and the head of its Board Consulting and Director Search Practice in the Americas. His expertise and experience is best evidenced by the long-tenured relationships that he has developed with his clients, many of whom have become friends. He has lectured at IMD, Yale and Northwestern University, where he is a founding faculty member of the Kellogg School of Management's Center for Executive Women, and has served both as a corporate director and a member of the Advisory Board of Georgetown University.

Previously, Ken was a vice president and group executive for a predecessor organization to JP Morgan Chase Bank N.A. where he worked with Fortune 500 companies on matters related to their capital structure. He holds a BSBA finance degree from Georgetown University, an MBA from The University of Chicago and a CPA from the State of Illinois.

Ken and his wife, Cathy, reside in Evanston, IL and have three adult children. He is a member of the Economic Club of Chicago, The Executives' Club of Chicago, The Chicago Club, and The University Club of Chicago.