FOLEY & LARDNER LLP

Board Oversight of a New CEO

2007 NATIONAL DIRECTORS INSTITUTE

BOARD OVERSIGHT OF A NEW CEO

The selection of a successor to a departing CEO is arguably the most important role of the board of directors. Ultimately, the goals of the board with respect to the CEO should be to help establish a solid foundation from which the new CEO can succeed, to stay engaged with the CEO's progress by monitoring and evaluating the CEO, and to allow the CEO to do his or her job so the board can focus on its mandate of guiding the company through change.

At Foley's sixth annual National Directors Institute on March 8, 2007 in Chicago, "Board Oversight of a New CEO" was a featured breakout session topic. The panel discussion was led by Tom Hartman, a partner at Foley & Lardner, along with George Bradt, managing director at PrimeGenesis; Joe Griesedieck, vice chairman at Korn/Ferry International; Randy Hogan, chairman and CEO of Pentair, Inc.; and David Webster, former vice president and general counsel of DeVry, Inc.

The Importance of the New CEO's First 100 Days

CEO failure is on the rise. In recent years, approximately 15 percent of *Fortune* 500 companies replaced their CEOs. Finding a new CEO is very important to shareholders and institutional investors, and the selection of a successor to a departing CEO is one of the most important roles of the board of directors. Accordingly, CEO succession should be discussed at every board meeting, rather than only once a year. However, to minimize the risk of failure, the board's involvement with the new CEO cannot end upon his or her hiring.

Generally, there are seven key factors that can contribute to a new CEO's failure, including:

1. Organization: If the business lacks a winning strategy or is unable to implement its strategy effectively, the new CEO, no matter how talented, will likely fail.
2. Role: New CEOs often fail because expectations are not aligned or their role is not clearly defined. It is difficult for a new CEO to succeed when it is unclear how success is to be measured or how the organization makes decisions.
3. Personal: No matter how good a board's selection criteria and interview process is, sometimes a new CEO is just not the right fit for the organization.
4. Learning: A new CEO entering into a new industry may face a steep learning curve and may not get up to speed fast enough to be successful.
5. Relationship: The new CEO may fail because of his or her inability to establish key relationships with important employees and customers.
6. Delivery: New CEOs often fail because they are pressured to build a high performing team and deliver fast results, which may not be practical in some situations.

7. Adjustment: Even if the new CEO is the perfect person for the organization, the new CEO may still fail because he or she is not be able to adjust to a changing competitive and organizational environment fast enough.

Ideally, it is best for the board of directors to take the role and personal factors off the table before a new CEO joins the organization. The board can accomplish this by having an up to date succession plan, conducting a thorough interview process and clearly defining the role of the new CEO. The board should work quickly with the new CEO to evaluate existing strategy and determine if a new or revised strategy is appropriate. The board must also jump start the learning, relationship and delivery processes during the first 100 days with a new CEO.

A new CEO will have a difficult time succeeding if the board simply stays out of way, rather than actively seeking to help and foster his or her transition into the organization. The first 100 days are critical to a new CEO's ability to succeed in an organization. During these first few months, the board should play an active role in encouraging and enabling the new CEO to establish key relationships. Board members typically have established and personal relationships with key customers or employees, who are vital to the success of the organization. The board members should make every effort to ensure that the new CEO is able to meet with those individuals. It is also important to make sure that the board and the new CEO act as, and are perceived as, a cohesive team.

It is vital that the board of directors and the new CEO operate in a mutual and transparent environment. A great way to synchronize the board and the CEO is by having the new CEO meet with each director, one-on-one, as soon as practicable. By having individual meetings, the new CEO is able to gain valuable insight into how the organization operates and establish early relationships with the members of the board. Furthermore, it helps the new CEO determine each individual director's contribution to and visions for the organization. It is also good to start early and define the criteria upon which the new CEO's performance will be measured. The board should clearly communicate the criteria to the new CEO and evaluate the new CEO's performance often. When doing so, the new CEO should be evaluated on all aspects, rather than only the financial performance of the organization.

The General Counsel's Perspective

The general counsel is well-positioned to brief a new CEO on how the board and the organization operate. While not a member of the board of directors, the inside counsel generally participates in board meetings and can be a very valuable set of eyes and ears for a new CEO. In that role, the general counsel usually knows which board members are able to produce results and those who tend to impede the board's progress, in addition to which committees are effective and which will require extra attention. Furthermore, the general counsel can comment on compliance with the organization's code of ethics, the scope of the organization's director and officer liability insurance coverage and the importance of '34 Act filings.

The CEO's Perspective

From the CEO's perspective, there are generally five things that he or she is looking for from the board:

1. Support and confidence: It is important that the board of directors show support and confidence in a new CEO. Entering into a new organization can be very challenging, especially for individuals who have no previous experience in this role. The board can help the transition by being sensitive to the CEO's situation and tailoring the nature of the support to the circumstances. After all, the board chose the CEO to join the organization.
2. Clear objectives: Make sure the CEO and the board have clear objectives and that all are in agreement on those objectives. A new CEO will often hit the ground running and it's important that expectations are set for what is to be accomplished in the first 100 days, thus allowing the board and CEO to operate in unison.
3. An engaged, but not intrusive, board: It is important that the board of directors adopt a "nose in – hands out" attitude towards the new CEO. The board should trust the new CEO while also keeping a close watch on his or her actions. Having former executives and CEOs on the board can be distracting to both the board and the new CEO, and removing old executives and former CEOs before the new CEO arrives proves to be very helpful to the new CEO.
4. Supply useful information: The board should help the CEO with the unknown. A new CEO will often not know all of the information that is pertinent and necessary to effectively run the organization. Accordingly, there should be frequent communication between the board and the new CEO. It's often helpful to appoint a lead director to communicate with a new CEO, as having multiple directors sending communications can be distracting.
5. Let the CEO run the organization: The CEO was hired to run the organization. Letting him or her run the corporation allows for a smooth transition and a good platform.

For More Information

For more information on this session or the sixth annual National Directors Institute, visit Foley.com/ndi2007 or contact the panelists directly.

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Save the date! The 7th Annual National Directors Institute will be held on March 6, 2008 in Chicago. Learn more at Foley.com/ndi.