

Director Recruiting

2008 NATIONAL DIRECTORS INSTITUTE



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INTRODUCTION

Pete Underwood, a Partner at Foley & Lardner LLP, moderated “Director Recruiting,” a panel presentation at Foley & Lardner LLP’s seventh annual National Directors Institute, held on March 6, 2008, in Chicago. Other panelists included Charles King, Managing Director of Korn/Ferry International; Christine Marx, General Counsel and Corporate Secretary of The St. Joe Company; Adam Ross, Associate Vice President of NASDAQ; and Stephanie Streeter, Director of Kohl’s Corporation. The presentation focused on the issues and challenges associated with the recruitment of qualified candidates for membership on a corporation’s board of directors. Among the issues discussed were the various processes generally followed in recruiting a new director, including the particular skill sets commonly desired in director candidates; the obstacles and impediments frequently faced by corporations in the recruiting process, including the effects of the Sarbanes-Oxley Act on director recruiting and the increased time commitment typically required of directors in carrying out their duties; and the definition and desirability of diversity in the board room.

PRELIMINARY STEPS

The program began with the panelists discussing the preliminary steps of the recruiting process. The panelists stressed the importance of creating a plan before initiating the recruitment process. While currently there may be only one opening on the board, other directors may be nearing retirement age or giving indications of a desire to leave the board. Corporations and boards of directors need to be cognizant of this and should plan and conduct their director searches accordingly. The search process is ordinarily a lengthy one, so it is important that future board vacancies be considered. Once management and the board have determined the desired number of directors to be recruited, together they must determine what skill sets the ideal candidate(s) will possess. This is generally done by evaluating the skills and experiences of the current board members. Corporations should look for candidates with skills and experiences that add to and complement — rather than duplicate — those already represented on the board.

The panelists noted that the next step is typically to determine who within the corporation will be primarily responsible for the director search. Traditionally, the CEO may have played a significant role in this process. However, the current trend involves a search orchestrated by the nominating committee or board equivalent. In addition, the panelists noted that those in charge of the director search should decide upon the search method that will be used. In the past, the recruiting process often involved members of the board and management simply pulling out their Rolodexes and making phone calls to those individuals who they thought would make a positive addition to the board. Although this “Rolodex method” is still used today, and may complement a



more formal search process, the current trend is to engage a professional executive search firm. Search firms have a much larger Rolodex and possess both the capabilities and the time to perform personality and competence evaluations as well as background checks. In addition, using a search firm can eliminate some of the politics from the recruiting process and is usually seen as much more effective in diversifying the board of directors. A third alternative that has recently been introduced is the Web-based search program. NASDAQ has created a program that matches corporations with potential suitors from a database of director candidates, based on the skills and experiences sought by the corporation.

QUALITIES TO LOOK FOR

The panelists and audience members noted that a good way to summarize the qualities that corporations should look for in a director is to remember the “four Cs” — competence, commitment, chemistry, and character. The search should focus on *what* the candidates know, not *whom* they know. The ideal candidate will have expertise that strengthens the board. Although industry experience is always a plus, the panelists’ view is that it is no longer a prerequisite. A candidate can be extremely competent without having worked in the company’s particular industry. This is especially true in the post-Sarbanes-Oxley era, in which financial experts are in high demand. Next, the ideal candidate must be committed. Sarbanes-Oxley and a litigious corporate environment require that directors devote substantially more time to their duties than had been expected of them in the past. For this reason, corporations must fully inform candidates of the type of time commitment involved and must look for only those candidates who are willing and able to commit the time required. Perhaps most important of the four Cs is chemistry. One new director can negatively affect the dynamic of the entire board. Corporations should consider looking for candidates with personalities that mesh well with those of existing board members in order to avoid conflicts based on personal chemistry. The final C, character, ties in with chemistry to some degree but also encompasses a candidate’s moral turpitude. It is important to weed out candidates who walk the line between what is legal and ethical and what is not.

INTERVIEWING

Traditionally, corporations would interview one or maybe two candidates before making a decision. This seems to have changed in recent years. The panelists discussed a common practice that is developing: A list is created of five to 10 “suspects” for membership on the board and is then narrowed to three to five “prospects” through a more in-depth evaluation of each candidate’s skills and experiences and the performance of a personality evaluation and background check. Oftentimes corporations will interview as many as four of these prospects via telephone. Based on the telephone interviews, a smaller number of candidates are brought in to meet management and the board of directors. These candidates will be given one or more face-to-face interviews with members of the nominating committee and, in some cases, the CEO or other senior management. The plus of interviewing a number of candidates is the rapport that is built with those who are not



selected. The next time there is an opening on the board, the search may be much easier if a strong candidate interviewed during the previous search is still available.

OBSTACLES AND IMPEDIMENTS

The panelists uniformly believe that recruiting qualified individuals to serve on the board of directors is not as easy as it once was. As mentioned above, the enactment of the Sarbanes-Oxley Act and an increasingly litigious corporate environment have vastly increased the amount of time required of board members. Many qualified candidates simply don't have the time or are unwilling to devote such a large amount of time. In addition, Sarbanes-Oxley has increased the risks of serving on a board. Although the majority of individuals would never engage in conduct that would warrant a lawsuit, the well-documented cases in which personal liability has been imposed on board members present a very scary scenario for many individuals. A final obstacle created by the Sarbanes-Oxley Act is the high demand that currently exists for financial professionals. All public corporations must have at least one financial expert on their audit committees, and many corporations would prefer that the entire audit committee comprise individuals with financial experience. This creates a competitive environment for the recruitment of financial experts. However, this obstacle is somewhat mitigated by the fact that, prior to Sarbanes-Oxley, financial experts (including CFOs) were not sought-after director candidates. Consequently, there is a still a large pool of financial experts to draw from.

DIVERSITY IN THE BOARD ROOM

The recruiting methodologies of the past have left many boards with members all of the same age, sex, race, and experience. Over the past 10 years, corporations have made a concentrated effort to diversify their boards. Diversity in the corporate world means more than just race and gender diversity; it also means diversity of experience and skill. Corporations seek individuals whose past experiences have provided them with the technical business skills and industry knowledge required to fully understand the intricacies of the company's business. Notwithstanding this broad definition of diversity, corporations still feel pressure and desire to add a gender, racial, and ethnic mix to their boards. However, the panelists stated that they generally believe corporations should resist the urge to employ a quota system. In their view, a better way to diversify the board of directors is to follow the steps outlined above: identify the desired skills, engage a professional search firm, and look for the four Cs. If, following this process, diversity candidates are presented, interview these candidates.



MORE INFORMATION

For more information on the topics discussed by the panel on “Director Recruiting”, please feel free to contact the panelists directly.

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