Shoemaker's child? succession planning for the board

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With corporate boards occupied with responsibilities such as regulatory compliance, risk assessment and executive compensation and succession planning, board succession has something in common with the shoemaker's barefoot children from the old proverb; just as the shoemaker never quite has the time to make shoes for his children, boards — with so much on their plates today — do not devote the time they would like to planning for director succession.

Historically, boards had allowed the chief executive officer to take the lead in filling board seats or tended to replace a retiring director with an individual "who looks like the person who left." Today, of course, boards no longer cede responsibility for director recruitment and succession planning to the CEO, yet they typically address director succession only on an as-needed basis — that is, when facing an impending vacancy.

This approach, however, may put boards at a disadvantage in this time when growth and innovation are top priorities for most organizations. Facing new global and competitive challenges, companies are transforming themselves through new product strategies, different product mixes and expansion into new markets and geographies. In an ideal world, outside directors with relevant experience can serve as valuable advisers to the board and management about the company's market, geographic and product directions and serve as a sounding board for management on the critical issues the company is likely to encounter. Wise boards will want to foresee where the company is headed in the future and have individuals on the board with the expertise to help the company move in that direction as efficiently as possible. Boards can accomplish this by vigorously managing director succession.

A more pressing reason for being proactive in board succession is the acute scarcity of experienced and available board directors. The increased time commitment and perceived financial and reputational risks related to board service have caused many experienced directors to scale back their participation in outside boards. In particular, CEOs — among the most highly valued director candidates because of their general management experience, big-picture view and knowledge of current business challenges — have been curtailing their outside board commitments. Most CEOs simply do not have the time to serve on more than one outside board and, increasingly, boards are limiting CEOs' outside board memberships.

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External forces, too, encourage a more proactive stance on board succession planning. Investors have become a potent voice in board governance, holding directors accountable for company performance and even challenging the nominations of directors. Institutional investors, on the whole, are looking for board directors who are independent from management and possess the relevant business and financial experience.

In the United Kingdom and Europe, boards have an additional regulatory impetus for actively managing board succession. For example, governance requirements such as those limiting director terms help to promote the orderly turnover of directors and provide boards with opportunities to review their composition and bring on valuable new expertise. According to governance guidelines in the United Kingdom and Italy, a director's independence generally is considered compromised if he or she has served for more than nine years from the date of first election. In France, a director is not considered independent after 12 years (three terms) on the board. Further, U.K. governance rules directly address board composition in the recommendation that the nominations committee evaluate the balance of skills, knowledge and experience on the board, make recommendations on the appropriate board composition and prepare a specification for each director appointment.

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With all of these forces aligned in support of rigorous board succession planning, why aren't boards more proactive in this area? Boards, of course, recognize director succession as one of their key roles, yet they do not always use the opportunity of a vacancy on the board to add critical new skills and perspectives. Why is this and what can boards do to ensure board succession planning becomes a priority?

Reluctance to have the difficult conversations. Human nature being what it is, some boards can find it difficult to discuss more directly the delicate issue of the need to make changes to the composition of the board or whether additional expertise is required. Directors may be reluctant to identify the desired criteria for the board and compare them to the expertise of the current board for fear of embarrassing those board members who do not meet those criteria. While such issues can be challenging for directors, strong boards address them anyway.

Perceived lack of time and lack of process. Because director succession seems like a need for the distant future, near-term business issues take priority for boards. While most boards do have processes for anticipating upcoming vacancies, many do not use this time to evaluate the skills required on the board to support the company's strategy.

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Practical constraints. While less of an issue today than in the immediate aftermath of the wave of governance reform, some boards' recruiting efforts place priority on identifying the finance expert for the audit committee. Boards can acquire individuals with this specialized expertise, while also recruiting individuals with the deep industry or business experience in the areas in which the company is moving.

Taking a more proactive approach to board succession

In general, boards tend to be very stable organizations, with little change in membership from year to year. While this stability is valuable, too little change can limit the board's ability to provide effective guidance to management when the organization is headed in a new direction, entering new businesses or exploring new geographies.

Director departures or retirements create important and rare openings that allow the board to expand or strengthen its skills in certain areas. Boards benefit when they take advantage of this natural attrition to recruit directors who can add valuable perspectives about the company's strategy — helping to prepare boards to rise to the new challenges and opportunities the organization will face.

A board can position itself to recruit directors with the desired experience by regularly reviewing its composition. A natural platform for the full board to review its composition and discuss the expertise that it will need in the future is the annual board self-evaluation. Through the evaluation, individual directors and the board as a whole can identify the areas of knowledge the board should possess in the coming years based on the company's strategic direction and the competitive landscape. From there, the board can evaluate whether it currently includes individuals with the relevant backgrounds and, if not, what skills or experience would be valuable to seek in new directors when vacancies occur.

As a starting point, the board should stay up-to-date on the timing of anticipated vacancies, including those due to term limits and directors' plans for retirement, and the needs of individual committees for specific expertise. In many cases, director departures are well known in advance, giving the board the opportunity to plan for specific board openings. While in the past, boards might begin the search for a new board member about six months before directors' elections at the company's annual meeting, the scarcity of experienced and available directors calls for boards to take a longer view. Today, wise boards start planning for vacancies at least 12 months in advance — and in some regions as much as 18 months in advance — reviewing and confirming the desired expertise and qualifications for new directors, identifying potential director candidates and communicating the board's interest well in advance.

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It may be helpful to tap external resources at this point. For example, through their work with boards and top executives, search consultants often know on a confidential basis the plans of many senior leaders. Particularly in the case of CEOs, who often are inundated with board invitations, it is valuable to understand their restrictions and preferences for outside board service, as well as their retirement plans. A search firm often has the ability to discreetly test an executive's interest in a new board role and his or her future availability.

Boards are likely to find that regular discussions about board composition and the skills-sets the board should be building for the future will help to create an atmosphere where the topic is less taboo. Treating board succession as one of the board's regular responsibilities may help to create an atmosphere where directors themselves recognize when it may be time for them to leave to make room for individuals with much-needed experience.

Forward-looking boards will elevate the task of planning for director succession. They will engage in an ongoing review of the board's skill-sets relative to the company's strategy and direction and use director departures as opportunities to acquire the necessary capabilities and experience. As they become more proactive in this area, boards will ensure the board as a whole and directors individually have the energy, expertise and experience to guide the organization as it addresses new challenges and market opportunities.

About the authors

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