Nasdaq | Stanton Chase

Forward-Looking Boards & Succession Planning

Aligning corporations and forward-looking governing bodies for sustainable value creation

Why Succession Planning Is Important

The context in which companies operate today has been dramatically transformed by unprecedented circumstances including, but not limited to, climate change, diversity, equity, and inclusion, as well as the impact of the COVID-19 global pandemic. Moreover, companies today have also shifted to focus on stakeholder capitalism; meaning shareholder interests are having to be balanced with those of other stakeholder groups such as customers, employees and society as a whole.[1]

Resiliency and sustainable corporate governance practices can strengthen companies and help them be prepared to successfully navigate risks and challenging scenarios. This goes hand-in-hand with a greater commitment to embracing the wider demands of people and the planet; and, ultimately, long-term sustainable value creation through alignment of strategy with the needs of a changing world.

Boards can demonstrate forward-thinking by constructing and nurturing a succession plan that authentically reflects the company's culture and strategic vision. There is no time to sit idle.

> "With the rising demand in highly-specialized skillsets – digital transformation, cybersecurity, sustainability, M&A – the war for board-ready talent is real, and fierce," she says. "Coupled with the diversity element, boards should be thinking about renewal and refreshment with at least a five-year lens."
>
> –Cathy Logue, Managing Partner, Global Leader of the CFO Practice Group, Stanton Chase Toronto

Forward-looking boards are well equipped to manage this. These boards make an ongoing commitment to understanding company risks and opportunities, culture, values, and strategic vision, and remain apprised of the latest corporate governance best practices.

A Culture of Responsibility

Amid possible global supply chain breakdowns, new and evolving regulations, cyber risks, changing political and economic climates, and concerns about sustainability, directors' tasks—and the scope of their oversight role—seem to have expanded exponentially.

More than ever before, it is crucial to have committed, forward-looking boards. Directors must continually enhance their knowledge base and be familiar with new sets of core supervision and governance capabilities including environmental, social, and governance (ESG) oversight and reporting; non-financial risk management, culture oversight; and effective, integrated succession planning.[2] Developing these capabilities and fulfilling these responsibilities will help companies to accomplish their mission of sustainable growth, in alignment with a purpose of value creation. An approach to accountability, foresight, and commitment is needed from every company, regardless of size, stage of lifecycle, or industry.

Succession planning is an integral part of effective supervision and stewardship.

> "Succession planning is no longer just a box to tick or a 'nice to have' when looking at board governance. It is an integral part of effective supervision and stewardship, indelibly linked to core board responsibilities such as oversight of strategy implementation and risk management. Having the right people around the table at the right time can add immeasurable value, whilst their absence, even temporarily, has been a key component of governance failures. The challenge for firms is in understanding who those 'right people' are and anticipating when needs may arise."
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> –James Beasley, Senior Director, Head of Board Advisory, Europe, Middle East, and Africa, Nasdaq

Maximizing Opportunities and Benefits

Embedding Succession Planning

Effective boards are strategic rather than reactive. This includes developing and actively maintaining a succession plan for both the board and management team.

The role of the company secretary here is critical: ensuring succession planning is appropriately represented on calendars and agendas as well as being linked to other processes such as effectiveness evaluations, director and management appraisals, and skills profiling.

Effective succession planning is no easy task. Today, a thorough understanding of intricate issues such as ESG, a company's non-financial risks and opportunities, stakeholder perceptions and interests, and how to develop the company's culture, values, talent, and strategic vision is requisite for high performing boards. Besides accounting for these complex and nuanced capabilities, succession plans need to align to a company's strategy and effectively tie-in with other board processes such as performance evaluations, director appraisals, maintenance of skills matrices, and appointments.

To meet these standards, boards should regularly consider their composition with respect to expertise, skillset, background, and more. This can help ensure an appropriate mix of skills and attributes uniquely suited to their companies, as well as help identify possible gaps that may need to be addressed.

Take the Long View

The appropriateness of composition can be considered through an effective evaluation process, which can in turn feedback to succession planning. However, 'moment in time' assessments of board composition are insufficient to determine whether a board is fit for purpose. Hence, for companies taking a long view, succession planning should be a continuous process and a top priority on boards' and stakeholders' agendas.

Forward-looking boards focus on long-term strategy and sustainable value creation. A robust, long-term succession plan considers the board's current skills and those it's likely to need in the future. Evaluations help identify professional and personal attributes that may be absent from the boardroom and therefore arm the board with insights to develop an effective succession plan. With this knowledge, boards are empowered to build a talent pipeline and ensure the right candidates are on deck when vacancies arise.

While board turnover is on the minds of many directors, the latest Annual Corporate Directors Survey found that few boards are making succession planning a priority.[3] Ten percent of directors reported that their board doesn't have a succession plan at all, and 33% said it is ad hoc. For boards that do have a plan, it is shared with the full board less than half the time (49%).

Taking a forward-looking approach is more important than ever.

> "There is no doubt that the socio-economic environment and overall global context in which corporations operate has altered dramatically over the past few years, and this poses a number of challenges for top management, business leaders, and entrepreneurs. In my experience, boards have faced major pressure to reassess and enlarge their function, reposition, and also become more active in the critical operations of their businesses."
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> —Panos Manolopoulos, Managing Partner, Middle East, Russia, and Greater China, Stanton Chase

Considerations When Succession Planning

External parties such as governance, proxy, and recruitment advisors are key resources in advising companies on how stakeholders will assess whether companies are taking sufficient steps to deliver sustainable performance. Many regulatory bodies also require disclosures on the board's composition, qualifications, and structure, as well as its policies and processes for succession planning.[4]

Annual reporting, such as proxy statements or governance reports, should feature succession planning assessments that set out the company's approach—including scope and influencing factors such as strategy and culture—as well as recent and planned developments of the plan.[5] This approach offers stakeholders critical insight to assess how well the board and leadership are equipped to uncover and manage potential risks and opportunities, as well as how diligently the company is being led.

A Forward-Looking Board: A Need to Have, Not a Nice to Have

A robust approach to succession planning, from the board down, can serve not only to ensure a strong leadership and talent pipeline, but also to inspire employees and other stakeholders with confidence in the board's diligent leadership.[6]

At the board level, good succession planning aims to deliver consistently relevant and impactful board composition, an important component of which is cognitive diversity. Investors are placing increased focus on board composition—including diversity—and the implementation of structured board succession planning. The tangibility of succession planning—seen through defined frameworks or policies as well as through the evolving composition of the board and leadership—makes it a feasible point of comparison between companies. Particular attention should be given to alignment of practices with company purpose and strategy, culture, talent development, and operational resilience.

Evaluating Board Diversity

Effective evaluations of board composition and succession planning should consider various elements including the company's current and future strategic goals, industry, and markets, as well as its size, nature, and complexity. But one additional constant is the need for diversity of thought and opinion around the table.[7]

"Thinking has evolved over time from diversity being a 'nice to have' to being a fundamental element of good governance," says Cathy Logue. "Legislation, quotas, and term limits won't tip the diversity scale, but influential institutional investors such as BlackRock, one notable example, have clearly articulated their expectations—from disclosure to strategy and implementation—and exercised their veto rights."

Diverse boards may find themselves more prepared for challenges that arise and leverage different perspectives to think outside of the box. Conversely, boards that are homogeneous may miss out on crucial elements of expertise that a more diverse board may offer.

> "If members of the management and/or supervisory boards are all cut from the same cloth, they share the same opinions and management styles and deliver similar solutions. Young people can bring a whole new perspective, especially in the all-important matter of innovation. People who have grown up with the Internet as a matter of course will, for instance, clearly have a different view of the requirements of the digital market than those with a purely analogue education and career background."
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> —Michael Schaumann, Global Leader of Board Services, Managing Partner, Stanton Chase Vienna

This can prove a challenge in the longer term as companies find themselves under pressure to innovate, digitalize, and globalize.

Ownership and Interconnectedness

Owning the Succession Planning Process

According to research by The Corporate Governance Institute, the task of achieving optimal board composition is primarily fulfilled by the Nomination Committee in alignment with the board chair.[8] In doing so they should review required skills, identify gaps, develop transparent appointment criteria, and inform and update succession plans.

The Nomination Committee should primarily lead the process for appointments, ensure plans are in place for orderly succession to both board and senior management positions, and oversee the development of a diverse pipeline for succession, as well as ensure the collective suitability of the board and executive management team.

The needs of a company and its board evolve over time in line with strategy implementation and ad hoc challenges or opportunities. Good practice therefore is for the Nomination Committee to re-evaluate the succession planning process by assessing periodically whether desired outcomes have been achieved and where improvements can be made.

Succession Planning Strategies

Succession plans and board appointments should utilize criteria that account for the current and future needs of the company and its stakeholders, and that promote cognitive diversity. Board evaluations can be a useful tool in testing whether this is the case, having regard to the approach taken overall as well as the contribution of individual directors, their tenure, and re-election cycles.

Effective leadership succession planning processes will be closely aligned to the talent management strategy. Doing so effectively is advantageous for filling new roles arising due to emerging business needs, providing development opportunities to talented employees whilst delivering value for the company.

Succession Planning Linked to Talent Management

Whilst allowing for external appointments where internal successors are not able to be identified, good succession plans focus on fostering the nurturing of next level talent. Initiatives to encourage this may include middle management development programs, facilitating engagement between middle management and non-executive directors, as well as partnering and mentoring schemes.

This holds true for board succession too, where potential successors for chair positions – for the board or individual committees – should be factored into planning, as well as individual director development and appraisal conversations.

Talent management is a strong motivational force for those who wish to develop their career within the company and transition to senior positions. For management responsibilities, it also provides the Nomination Committee with a referenceable pool of strong candidates to fulfill critical strategic roles in the future.

> "This close link between effective succession planning and broader talent management has inevitably elevated the relationship between the board and the Chief HR Officer / Chief People Officer. Boards are looking to the HR function to anticipate future challenges, to understand where the next generation of leaders is going to come from and, importantly, what directors can actively do to support their development."
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> –James Beasley, Senior Director, Head of Board Advisory, Europe, Middle East, and Africa, Nasdaq

Board Capabilities Matrices and Disclosures

Companies traditionally disclose the board of directors' skills and qualifications by various means, such as through election processes, annual reporting and on company websites. As a result of stakeholders' interests in director quality, diversity, experience, skills, and knowledge; practices are continuously improving. Companies are increasingly employing, and disclosing, detailed capabilities matrices to illustrate the board's capabilities profile. In more sophisticated approaches, these are explicitly linked to the strategy lifecycle, ESG considerations, industry or geographic developments, stakeholder interests, and company culture.

Such matrices can aid robust board evaluation and succession planning processes by helping to identify any gaps or overlaps in capabilities and experience. Transparency around these considerations—including a version of the capabilities matrix in proxy statements or governance report, for example—can serve to build stakeholder confidence in the board's quality, strength, independence, and ability to oversee and support management and its strategies.

Succession planning exercises can provide valuable input into boards' capabilities analysis alongside assessment of strategic objectives and other factors in order to arrive at a bespoke board capabilities profile.

The knowledge, skills, and expertise comprising a bespoke board profile should ideally be benchmarked against best practices of relevant industries and company types, related international markets, and in accordance with the latest sustainable corporate governance frameworks and guidance.

Succession Planning Advice

One of the best ways to create meaningful impact is through clearly defined board renewal strategies, according to Cathy Logue. "Great boards don't just happen," she says. "It's critical to build board renewal mechanisms such as tenure, term, and even age limits into these strategies." As for term limits, Logue suggests looking five to 10 years out so that boards aren't at risk of lacking experienced directors.

One of the worst mistakes a board can make is not looking beyond its traditional networks and unconscious biases. "The standard excuse of 'We couldn't find any qualified diverse board candidates' just doesn't fly anymore," says Logue. "Investors are putting their foot down, and boards must approach renewal and succession planning more creatively," she notes.

Given the importance of these processes for the effective leadership of every institution, partnering with experienced, objective, and independent companies has to be a priority.

Authors' Conclusion

Succession planning is imperative for a company's continuity and sustainability. Succession planning exercises begin with the company's long-term strategy and consider how the knowledge, experience, and capabilities of the board and leadership team aligns, or may need to evolve over time, to deliver against it.

Assessment outcomes can help the board articulate the strategy into a desired composition profile to deliver sustainable effectiveness. Succession planning assessment outcomes serve as a strategic tool to assess the fitness and propriety of potential candidates for nomination to the board, as well as input into other related processes, including appraisals and training and development activities. What is more, disclosures of a robust succession planning framework may positively influence stakeholders' opinions, such as proxy advisors for shareholder voting.

Finally, succession planning tied with personal performance management and the company's wider talent strategy results in a solid leadership pipeline that will embed trust among shareholders and stakeholders, engage senior leadership towards strategy, and enhance employee engagement.

About the Authors

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James Beasley is a governance and board effectiveness specialist with over 13 years' experience working with some of the world's largest and most complex organizations. He currently serves as Senior Director and Head of Board Advisory in Europe, Middle East, and Africa regions at Nasdaq. He joined Nasdaq from Deloitte where he spent nearly a decade in governance advisory, latterly as Director leading on board effectiveness and wider governance transformation activities. Throughout that time, he has supported boards not only through reviewing effectiveness and performance, but also through the design and implementation of effective governance arrangements. James holds a master's degree in Global Governance and Ethics from University College London (UCL).

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