BUILDING BENCH STRENGTH

When committees work *too* independently, the board can miss opportunities to drive culture and keep the pipeline full. A panel of experienced directors shares their ideas and best practices for keeping the connections that matter. **BY C.J. PRINCE**

"If you have lived through succession planning that didn't work well, it underscores the importance of it."
—Laura Kaiser, Director, Merit Medical Systems; CEO, SSM Health

The pandemic may have sparked the seismic workplace shift that led to changing employee priorities and phenomena like the Great Resignation, but in its wake, companies across industries continue to struggle with finding and keeping great talent. Right now, boards have a unique, outsized opportunity to influence their company's trajectory by focusing on the development of future leaders. The best way to do that? Strengthen the link between leadership development, succession and compensation discussions.

Of course, that's easier said than done, agreed participants at a recent roundtable convened by *CBM* and executive compensation firm Semler Brossy. At some companies, management lacks a fundamental understanding of how critical robust talent planning is to organizational capability, or even what it is that makes an individual successful in a company, said Beth Webster, who witnessed that firsthand as head of HR for large financial firms, including TD Bank and Citi. "Even in very sophisticated companies, when it comes to succession planning, every CEO talks about how important it is, but most don't understand it," she said. "Until there's real clarity around [these questions]—what is it that makes someone successful in this organization, what are the derailers, how do we talk about those—you'll get nowhere."

Too many companies learn this the hard way, said Laura Kaiser, who serves as a director on Merit Medical Systems' board and is the CEO of SSM Health, a $9.3 billion Catholic, not-for-profit health system. "If you have lived through succession planning that didn't work well, it underscores the importance of it. [That's] where you can actually see companies lose momentum or even stall if it isn't done well and there isn't the work devoted to making sure it happens thoroughly and thoughtfully."

Holes lower down in the pipeline can derail succession planning at the top, creating a mess that boards then have to clean up. "That's the number one job that keeps us sleepless—if we haven't done consistent and rigorous planning for the CEO," said

Liane Pelletier, independent director for Frontdoor and Expeditors International of Washington, who noted that CEO tenure "has been dripping down over the last 10, 20 years."

To ensure a robust pipeline and smoother CEO succession, boards need to proactively connect the dots between leadership development, succession and compensation. The following are several best practices to help achieve that synergy.

Make sure the right processes are in place internally. An abundance of skill on the board won't help if talent strategy is being mismanaged inside the organization. "It's got to start there," said Webster, who recently served on the board of CURO Financial and worked closely with the firm's head of HR to develop robust talent development processes. "The board has to oversee the processes that are in place internally, and then when you bring them to the board, you can work through the integration of the various board committees. But those processes have to be solid within the organization."

The head of talent and head of compensation should be the CHRO's "right and left hands," she added. "Those are the roles that should be teeing up this work to the board, and then it becomes the board's responsibility, of course, to go from there. But it's got to be good inside. If it isn't, what gets to the board is useless."

Ensure talent is a chief priority. Although boards don't own culture, they are responsible for making sure the right people are in the right positions to drive it. "Oftentimes CEOs and other C-Suite executives don't understand the direct impact that their day-to-day behavior has on the development of culture or the erosion of it," said Webster. "The board has a big responsibility to ask some very specific questions around that topic and to stay abreast of what the cultural issues are within the organization."

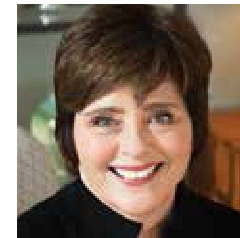
The board also has to ensure the CEO is setting the tone at the top that talent strategy is paramount, Webster said. "When it's a priority of the CEO, whether it feels bureaucratic or not, it gets done. So this is one of those things that has to start at the absolute top." There should be regular reporting out to the board, she added, "and it is incumbent upon the board to ask for it. Any good head of HR will welcome this kind of analysis and scrutiny and development."

Find a champion. "Having a supportive CEO who is interested in succession planning and talent development can make all the difference, but you may not have that in all cases," said Kathryn Neel, a managing director at Semler Brossy. "So it's important to find another person who can bring more of that to life, whether it's the lead director or chairman, or the CHRO—someone who can partner with the CEO."

The head of HR can absolutely play that role—if they're given a seat at the table, said Michele Siekerka, CEO of the New Jersey Business & Industry Association and independent director with Citizens Financial. "If the CHRO is seen in the boardroom as a partner and as someone who is highly respected across the organization, then that person really does sit a little more center than if they're playing a supporting role somewhere along the side."

Create a positive setting for discussion. It's no secret that succession planning can be a challenging topic for CEOs, which makes a healthy relationship between the board and the CEO so critical—because decisions around succession can't be personal. "We have a collective fiduciary responsibility to do it well, but there's always the opportunity when emotions are running high for things to be misinterpreted," said Kaiser. "You just need to know one another well enough to ensure that you're checking in with your sitting CEO so they can be an active and healthy part of the process. They need to be able to freely and appropriately share information, and also not feel threatened that the board is thinking, 'Well, how soon are you leaving?' Because that's not the right question. It's more about, how are we ensuring continuity for this organization that we all deeply care about?"

Kaiser recommended devoting time to succession planning on the board retreat. "It's a more relaxed setting. There's a little more time to breathe."



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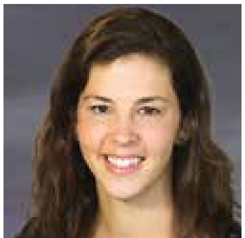

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Plan for committee overlap. One way to connect the dots between, say, talent development and compensation is to have at least one director serving on both of the relevant committees, said Barbara Higgins, who serves as an independent director at Employers Holdings, a workers' compensation insurance company. Higgins shared that her simultaneous service on both nominating-governance and human capital compensation, though not deliberate, turned out to be very helpful when the company was searching for a CEO to replace a long-time leader. “It's really hard if you have a total disconnect between those two committees.”

Which is why planning for strategic overlap between committees “is really smart,” said Neel. “It's something for nominating-governance committees to think about as they make committee assignments, to be very thoughtful about where you have strategic overlaps of board members on different committees.” For example, a pharmaceutical business Neel worked with made sure to have overlap between the compensation committee and the science and technology committee, she said. “Because you have a link to innovation targets and objectives and the compensation program, so you need that expertise from the science and technology committee.”

While committees do report out to the full board, packed agendas can limit the time allotted for that sort of information sharing. Tom Palmer, an independent director with Erie Indemnity, offered another solution. “For the principle committees, we have an overlap where the whole board is invited to one of their meetings to have a full range of in-depth discussion about issues that the committee is dealing with,” he said. “It gives us an opportunity to see people in the areas that are affected by the respective committees, so that works well.”

Dig deep into the pipeline. Palmer's executive compensation and development committee also looks well beyond the top level of the pipeline, reaching as far down as vice presidents who are in line for promotion to senior vice president. “Once they get to the SVP rank, we want to see them making some presentations to the board. We want to see the development of the people coming up.” he said.

Kaiser added that high-potentials should be exposed to the full board not only in presentation but socially as well. Her board makes a practice of inviting the “high-pos” to board dinners several times a year. “So it's not just a table of a bunch of us. We break into different tables, so there can be some meaningful conversations,” she said. “It's really helpful so that we're more informed, and it just helps to increase the depth of richness and conversation around succession planning.”

Webster cautioned that board members keep the right order of priorities as they're evaluating future candidates for senior roles. “Too often, you see ‘people, structure, strategy,’ and [board members] saying, ‘Oh, I know Joe, and he's amazing. He can do anything. So I'm going to stick him in this job’—when Joe has no connection to the strategy capabilities required in that role.” Instead, start with strategy and structure, and then look at the candidates who are right for those roles, she said.

Use compensation strategically. While compensation plans historically have been more rigid and formulaic, boards need to look at how they can use a more nuanced approach to guide talent development. One example would be to use long-term incentives to recognize not just current performance but future potential, said Higgins. “So even if you knock it out of the park, if that's as far as you're going to get, you might not get a very generous equity grant. If you've sort of had a tough year, but we know that you have lots of runway ahead of you, we might still reinforce your performance with a very strong long-term incentive grant.”

One of the big mistakes boards and management make is putting high-potentials into “stretch” roles but not compensating them for it and assuming they will stay, said Webster. “I have seen time and time again an unwillingness on the part of the executive team to properly pay a high potential that you know we've put into some stretch role. Invariably you lose them." She noted that boards are sometimes hesitant to make a change to pay structure before they're sure the new assignment will work out. "But my approach has always been, if we find that they're not doing the job and they don't have the potential we once thought, we can take other action. But that's not a reason not to pay them. You're taking a bet on them, you're developing them, you're telling them that you think they've got what it takes. You say all those things and you don't pay them? It doesn't work."

Ultimately, if the company wants to create a culture where talent development succeeds, it needs to be valued and compensated, said Higgins, who recalled the compensation strategy at her former employer, Disney. "We would actually reward people for developing individuals. We compensated people in the operations group higher than some of the people in strategy areas because they had so many people they were accountable for that they had to develop and nurture in the organization." If someone is high potential but they don't get promoted, that should impact his or her manager's compensation, and vice versa, she added.

Don't lose your runners-up. Only one of the high-potential candidates being considered for a top spot can actually get the job, which can spell trouble for your pipeline if you're not careful, said Andrew Smith, CEO of Yenkin-Majestic Paint Corporation/OPC Polymers and independent director with Core Molding Technologies, where he chairs the compensation committee. "In my 35 years of business, I would say it's more the rule that if you've got multiple people vying for a top position and they don't get it, they're going to leave," he said. "It's very hard to keep the people who really want to be CEO, [because] if they don't get it, they're going to become CEOs somewhere else. Same with a CFO or a chief operating officer."

Being intentional before, during and after the succession process can help, said Neel. For example, when selecting candidates internally, the board should examine invested outstanding equity to see how much is at stake for those individuals to stay long term. "And is there anything different we should do about those incentives? There's a lot to be planned for beyond just the individual whom you select. There are all the individuals you may not select for those positions as well; that has to be thought through."

Keep an eye on the data. Neel recalled a board she worked with that, at the end of every human capital committee meeting, looked at the turnover of specific populations within the organization, including SVPs, EVPs and anyone else in the succession pipeline. "So as a committee or as a board, they could start to see whether there was anything that seemed troubling for one reason or another, and any patterns in the departure statistics," she said. The practice began during Covid, when turnover was alarmingly high—as it was for many companies—but has continued. "It provides a lot of really interesting insights, and it leads to questions around how you plan to fill that position afterwards. And could that be an opportunity for so-and-so who presented to the board at the last meeting, and who we think has real capabilities in these areas?"

Higgins noted that doing something similar at a former company enabled the board to spot some unfortunate trends. "We looked at who was on the succession plan, and women and people of color were much more likely to be listed as high potential. But looking at who actually got the promotions, that [data] did not follow the succession plan—they were largely male and largely not people of color. Those statistics alone showed a lot of work that needed to be done.... It was shocking that we were going through the motions of having succession plans, but actually not using them at a very large percentage."

Webster and others stressed that when looking at high potentials to fill current and future roles, boards should do so with an eye toward who is going to support culture and keep it healthy. "It's really true, as Peter Drucker said, 'Culture eats strategy for breakfast,'" said Webster. "When you don't pay enough attention to culture and you are not explicit about it, it's going to bite you in the butt every single time." **CBM**

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