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Paths and Implications for Navigating CEO Transitions

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Transitioning a CEO marks a pivotal moment in any company's trajectory and can take many forms. As boards deliberate on selecting the new CEO, they also have a choice about the outgoing CEO's role. Will they stay as a mentor to the new CEO, transition to a board role, or depart entirely? Regardless of the role, each path will affect the organization's stability and strategic direction.

Defining the organization's needs is the first priority. Factors such as how seasoned the new CEO is, potential responsibilities for the outgoing CEO (e.g., targeted employee relations, government relations), and whether the new CEO wants the old CEO around should be evaluated. Board dynamics with the former CEO and the reason for transition are another consideration, as is the prominence of the former CEO's personality.

If the outgoing CEO is to remain involved, the second question is for how long. Having the prior CEO in a prominent role for too long can create confusion about who is in charge and slow the new CEO's ability to take control. This is why transition periods are typically less than two years. Boards need to assess the requirements of the work, and if unclear, build in natural check-in points to ensure the arrangements are still working. Secondary considerations, such as when vesting milestones occur, can also come into play.

Below we share four common scenarios for CEO transitions and considerations for each, including pay implications.

SCENARIO 1

CEO transitions to Executive Chair

TYPICAL TIMEFRAME	S&P 500 PREVALENCE
6-24 months (~65% < 12 months)	48%

Transitioning to an Executive Chair role is a common strategy for planned, orderly successions and is the most prevalent in our study of S&P 500 CEO transitions covering calendar years 2022 and 2023 (n=102). The Executive Chair role offers highly valued CEOs, who may be retirement ready, the opportunity to continue contributing while reducing day-to-day responsibilities. They can also be a resource for the new CEO for coaching, questions, and back-up support as the new CEO learns the new role. Often the Executive Chair will steward strategic initiatives, but the division of labor between CEO and Executive Chair can take many forms. For example, the Executive Chair may continue as the "face" of customer and/or supplier relationships while the CEO focuses on operational excellence. Clear delineation of responsibilities and defined timelines are essential for a smooth transition.

Executive Chairs often see a reduction in cash compensation (base and bonus) following transition–often in the range of 50%. Eligibility for, and the design of, future equity grants vary considerably with timeline and role. Roles with a longer runway and more substantive responsibilities will often receive additional equity awards. In either case, continued service generally allows for continued vesting of prior grants received as CEO and, in select cases, other ancillary benefits or perquisites (e.g., office space and administrative assistant).

A slight variation on the Executive Chair role is the much less common Vice Chair role (used in only 5% of our studied S&P 500 CEO transitions). The Vice Chair designation may fulfill similar objectives as an Executive Chair when the organization's bylaws mandate that the CEO serve as board chair. In these cases, pay is usually similar to that of an Executive Chair. In other cases, the Vice Chair role may serve as an honorific title used for a founder-like or transformative leader—bestowing emeritus status and signaling the individual's profound contributions to the organization. Pay in this scenario typically mirrors that of the typical director—possibly with an additional retainer on par with a lead director if/as warranted.

SCENARIO 2

CEO transitions to Senior Advisor

TYPICAL TIMEFRAME	S&P 500 PREVALENCE
3-12 months (or longer)	28%

A senior advisor transition offers many organizational benefits of an Executive Chair transition but with greater flexibility for the incoming CEO to define the desired level of support on a more ad hoc and/or as-needed basis. It also means an immediate (or at least quicker) transition of the outgoing CEO from the board—particularly valuable for an experienced, externally-hired CEO looking to create a clearer demarcation of the organization's past and future state visions.

Pay is typically structured as a consulting agreement with either a defined hourly, weekly, or monthly rate payable in cash. Eligibility for an annual bonus or future long-term incentive grants are very rare, but continuous service typically allows for continued vesting of prior grants received as CEO.

SCENARIO 3

CEO transitions to Board Member

TYPICAL TIMEFRAME	S&P 500 PREVALENCE
6-18 months (anchored to annual meeting dates)	4%

Remaining on the board as a director offers another avenue for ensuring strategic continuity when day-to-day transition support is unnecessary. For example, there is no mandate for a change in strategic direction when a long-time lieutenant ascends to the top job during a period of strength. Alternatively, there may be urgent investor or other stakeholder issues to be resolved that someone with experience on the board would be better positioned to navigate. Of course, boards should be mindful of corporate governance implications (the outgoing CEO will not be deemed independent) and should be careful that the former CEO does not overstay his/her welcome to the point that interferes with the evolution of priorities.

Compensation for the transitioning CEO will almost universally follow the standard program for board pay during the individual's tenure and, again, offers the opportunity for continued vesting in outstanding equity awards.

SCENARIO 4

CEO has no affiliation with the company

TYPICAL TIMEFRAME	S&P 500 PREVALENCE
n/a	20%

The outgoing CEO may have no formal, continuing role at all—the case for approximately one-in-five S&P 500 CEO transitions in our study. Reasons for this may include redirecting change due to underperformance, avoiding overshadowing the new CEO, or enabling the former CEO to pursue other interests. Such transitions often lack future pay considerations and require careful messaging to shareholders to avoid misinterpretation.

Conclusion

Succession planning is a critical responsibility of the board. As transitions occur, the role of the outgoing CEO must be carefully considered to ensure a smooth handover and preserve the organization's stability and strategic direction. By evaluating various scenarios and their implications, boards can navigate CEO transitions effectively, setting the stage for continued success and growth. ■

For more information, visit us at SEMLERBROSSY.COM, *or reach us at 310.481.0180.*

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