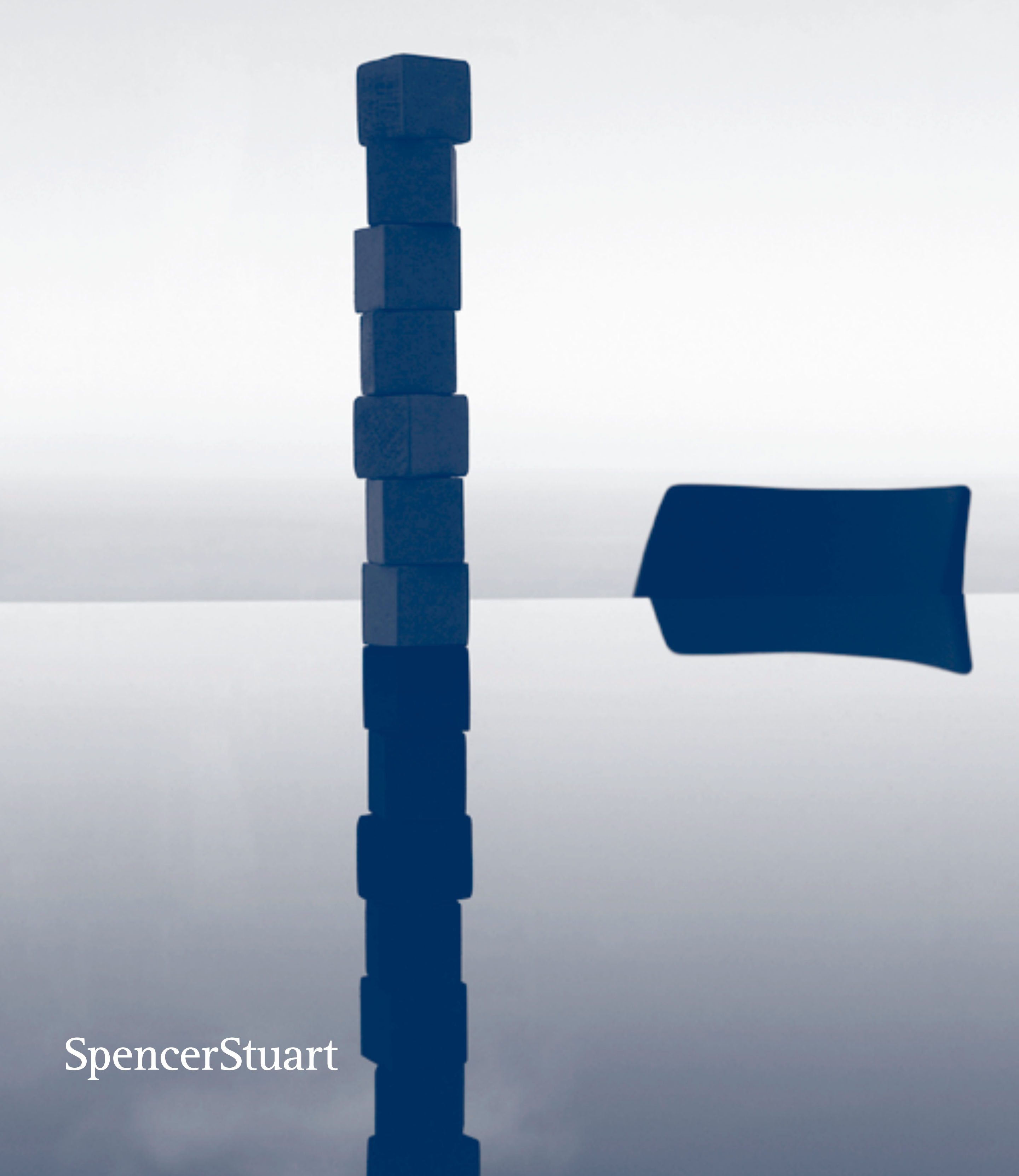
POINT OF VIEW

A SPECIAL ISSUE FOCUSING ON TODAY'S BOARD & CEO AGENDA



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About Spencer Stuart

Spencer Stuart is one of the world's leading executive search consulting firms. Privately held since 1956, Spencer Stuart applies its extensive knowledge of industries, functions and talent to advise select clients — ranging from major multinationals to emerging companies to nonprofit organizations — and address their leadership requirements. Through 51 offices in 27 countries and a broad range of practice groups, Spencer Stuart consultants focus on senior-level executive search, board director appointments, succession planning and in-depth senior executive management assessments.

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What motivates a director candidate to choose one corporate board opportunity over another? Why do directors continue to serve at all, given the scrutiny boards find themselves under today?

How is the ideal CEO profile likely to evolve in the next five years, and what should boards and CEOs be doing now to groom successor candidates able to fit the bill?

As we emerge from one of the most challenging recessions ever and look ahead to continued economic uncertainty, many of us are re-examining our priorities and plans and the skills that we as individuals and our organizations should be building for the future. In light of the activity on governance around the world and the many business and organizational challenges companies face, this special issue of *Point of View* focuses on today's board and CEO agenda.

We think the topics that we are exploring in this issue — including board priorities such as risk management and succession planning, the trends that will shape CEO profiles in 2015 and the underappreciated leadership traits that are fundamental to executive success — are especially relevant in the current business landscape. We hope you agree.

On behalf of all of us at Spencer Stuart, I hope you enjoy this special issue of *Point of View* and welcome your comments.

David S. Daniel
Chief Executive Officer
Spencer Stuart

Why they still do it

Directors' motivations for joining a board

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Despite the occasional anecdote about a director vowing never to join another public company board, experienced directors are not fleeing boards in droves. Yet, one could be forgiven for assuming that at least a few directors are asking if board service is still worth it, in light of the sky-high expectations on them, the significantly greater time demand and the challenge of keeping up with the dizzying pace of business.

Several forces have converged to make board service more complex and challenging today:

New regulatory requirements. The global financial crisis and isolated business scandals have renewed focus on board governance and, in some places, led to new governance rules and requirements. Regulations differ by country and region, but many of the new requirements center on a few areas: board composition, director qualifications, executive compensation and risk management. While it may be too soon to know the impact of regulatory changes on board composition and operations, some directors fear that the balance of the new governance rules "is tipping from substance to form, and regulation has now tipped to incompetent intrusion."

Shareholder activism. Investors are pushing for more influence on key issues, including board composition and executive compensation — and, occasionally, gaining new tools to exert their views, such as the new proxy access provision in the U.S. While many directors welcome the increased dialogue with investors, there are frustrations: the check-the-box mentality of some institutional shareholders, the vast influence of ratings agencies and the pressure for immediate and unsustainable results.

A higher degree of scrutiny. Ten years ago, the chances of a board of directors becoming front-page news were slim. Today, when a business faces a crisis or erosion in performance, the board's action — or inaction — is examined nearly as closely as the CEO's. As one director observed: "There's no hiding anymore."

A growing agenda. Boards are spending more time discussing issues such as risk, executive compensation, the environment

We spoke with many experienced chairmen and board directors, including the following, about a range of topics related to joining boards and getting the most from the director experience.

Daniel Camus, executive board member of Electricité de France and a board director of MorphoSys and Valeo

Jean-Martin Folz, retired CEO of Peugeot and a board director of Alstom, Axa, Carrefour and Société Générale

Chris Gibson-Smith, chairman of the London Stock Exchange and The British Land Company

Randall J. Hogan, chairman and CEO of Pentair and a board director of Covidien

Louis J. Lavigne Jr., chairman of Accuray and board director of Allergan, BMC Software and SafeNet

Christine Morin-Postel, board director of British American Tobacco, Exor and Royal Dutch Shell

Edward A. Mueller, CEO of Qwest Communications and a board director for The Clorox Company and McKesson Corporation

Denis Ranque, chairman of Technicolor and a board director of Compagnie de Saint-Gobain

Philip Rogerson, nonexecutive chairman of Aggreko, Bunzl and Carillion

John Wiehoff, chairman and CEO of C. H. Robinson and a board director of Donaldson Company and Polaris Industries

Anthony Wyand, vice chairman of Société Générale and board director of UniCredit and corporate responsibility, as directors take a more expansive view of their responsibilities. The financial crisis and economic downturn elevated the importance of risk and remuneration in the boardroom, but directors also feel pressure to take on issues such as the environment and corporate ethics in response to their growing visibility with investors and society as a whole.

> "Accountability is far greater today, and that has real implications for the involvement of the board members."

Changing board dynamics. Finally, boards themselves have changed. As a result of increased specialization, the growth in the number of first-time directors and greater gender, ethnic and geographic diversity, directors find fewer people "just like me" seated around the board table. Led by the chairman or lead director, the board has to create an environment that harnesses these different perspectives. And, with so many responsibilities, directors are holding each other to higher standards. "Accountability is far greater today, and that has real implications for the involvement of board members. A board member who doesn't work is immediately detected, as well as an incompetent one, which was not always the case before. Board meetings are no longer a club meeting," said Christine Morin-Postel, currently a board director of British American Tobacco, Exor and Royal Dutch Shell.

WHAT DO DIRECTORS WANT? PRIORITIES FOR SERVING ON THE RIGHT BOARD

The current environment creates some real challenges for boards that need to recruit directors. Because of the scrutiny on them, boards must be very thoughtful about defining the necessary skill-sets for new board candidates and recruit directors who have those skills and a reputation for working hard, contributing to board discussions and respecting management and their colleagues on the board.

As important as it is for boards to carefully define the capabilities and qualities of the ideal board candidate, boards also must remember that director candidates weigh a variety of professional and personal priorities when considering an invitation to join a board. Understanding what's important to director candidates will be increasingly critical to recruiting new board members.

So, why do directors join a board?

Directors tell us that they find great professional satisfaction from contributing to the performance of a company and personal satisfaction from challenging themselves in a new situation.

"Certainly, part of the reward is yourself versus all the challenges we've been talking about. Can you do this? Can you be effective in a new context?" said Chris Gibson-Smith, chairman of the London Stock Exchange. "Another reward is the opportunity to learn. If we think of ourselves in medieval terms, we go on an apprenticeship and eventually become a master craftsman, but the journey never stops. That's rewarding."

For John Wiehoff, chairman and CEO of C. H. Robinson and a director on the Donaldson and Polaris boards, an important reward for serving on an outside board has been the insight he has gained to improve how he works with his own board. “Board service has taught me to simplify and prioritize with my board. I’ve learned as a director that it’s very challenging to stay on top of things in between meetings. As a CEO, I’ve had to learn that even though my directors are very smart, committed people, they can’t be expected to remember the details of my business.”

While experienced executives continue to see great value in serving on a corporate board, they want to serve on the right board. In general, directors want to join boards where they will have the opportunity to learn, where their talents and expertise will be valuable and where they can make a difference to the company. They want to be a part of a high-performing team and respect the people they are working with on the board and in management.

We hear from director candidates that the intangible rewards of board service — affiliation with highly respected companies and other directors, exposure to other governance processes and the opportunity to gain new ideas valuable to their own company — continue to be important factors in the decision to join a board. For most director candidates, choosing the right board involves a formula with multiple factors. Below are a few of the most common:

Industry and company size. For many directors, a company’s industry sector is one of the most important

How do you evaluate new board opportunities?

“The first thing I look at is the sector. Is it a sector I want to work in or have experience in? Is the company an interesting one that has interesting challenges, whether that is growth or recovery or something else? Do I know the people and am I prepared to work with those people?”
Philip Rogerson

“The criteria I use are the same as when I first became a board director:

Will I gain experience to help me as a new CEO? It has been extremely helpful to see things from the other side.

Who is already on the board and will I learn from them?

Can I get excited about the company’s strategy? Do they have similar business challenges?

Is there personal chemistry with the other directors and the CEO?”
John Wiehoff

“The key factors for me are the qualities of the chairman and the CEO — I need to respect them — the role I am asked to play and in which committee they want me to sit; the curiosity and interest I have for the industry with a paradox to solve. I may have more interest for new industries where I am less experienced.”
Jean-Martin Folz

“I look for the opportunity to leverage my personal experience in other industries and get some ‘fresh air’ outside my own industry. This allows me to learn about the dynamics of other industries with no preconceptions and confront ideas with other executives at a high level. When recruiting board directors, I see candidates today being more concerned with having a real contribution to strategy and less with the prestige of being a director.”
Daniel Camus

considerations. Is the industry interesting to them? What they can learn from it? Do they have experience in the industry? Director candidates also may look at the regulatory framework governing the industry or the issues the industry faces. For many director candidates, especially those who are active executives, the ideal match is with a company in a complementary industry, such as an industry experiencing similar growth patterns or addressing similar challenges.

Company size also can be a consideration. Depending on a director's interests, he or she may prefer a board assignment with a large company for the exposure to world-class executives and directors and the opportunity to tackle complex global issues, or a small company assignment for the cutting-edge technology or ability to have a larger-sized impact. Some director candidates view their board work in terms of building a portfolio of assignments with different sized companies and in different industries.

> Assume that there will be good competitors for a candidate's time, whether it is another board opportunity or another interest.

The fit with the CEO and chairman. Comfort and compatibility with the CEO and the chairman also are very important considerations for most director candidates. Experienced directors advise director candidates against joining a board where they have questions about the performance or the ability of the CEO, or if they get the sense that he or she doesn't value the board and its role in the company. Said one director: "Unless it's a role that requires the removal of management, I wouldn't work in a company where I don't think I'll get on with the chief executive."

The quality of the governance. Directors want to join a well-functioning board that plays the appropriate role in the major strategic decisions of the company and to be comfortable with the company's business and governance practices. Directors look at the quality of the governance processes, the independence of the board and the management's attitude toward the board.

The challenge. Does the company have stimulating challenges related to growth, recovery or something else? Some directors tell us they are excited by opportunities to participate in a turnaround or the rebuilding of a company that is struggling or to be a part of a board that has to select the next CEO. As one director explained, "It is more exciting when the company faces problems, because it is then that the board is the most useful."

The strength of the company. While some directors relish the idea of helping to turn a company around, others are drawn to top-tier organizations that have healthy financials and an excellent reputation — those that seem unlikely to fall victim to a major scandal or business disruption. These directors look closely at the financial strength of the company and its competitive position in the marketplace, and want to be comfortable being affiliated with its reputation and values. Some director candidates report that they conduct more rigorous due diligence than in the past about the company's financials, reputation and governance through extensive interviews with current directors and senior executives and careful reviews of publicly available financial information. They also mine information from contacts in the industry and other trusted business sources, check the company's corporate governance ratings, examine its public policy positions and speak with industry and financial analysts about the company.

The other board members and the chemistry between them. Director candidates always want to know who already serves on the board they are being asked to join. For some, the opportunity to work closely with and learn from business leaders they respect is as much a motivation for joining a board as what they can learn from the company. In addition, directors want to avoid boards that are rife with conflicts or lack the independence from the CEO to do their work. While it is impossible to know precisely how a board will behave until one starts, it helps to meet as many directors as possible and learn about them and their work styles through mutual friends and colleagues.

The time commitment and potential scheduling conflicts. Serving on a board today takes much more time than in the past, directors say. The time demand is even greater for companies that are restructuring or undergoing a CEO transition. Director candidates want to be comfortable that their schedule can accommodate a new board assignment, and many directors now limit the number of public company board roles they will accept.

"These are the criteria I used when considering an outside board:

Do I have time? Boards take more time now, and appropriately so.

Will it be stimulating? Is it something I want to put time into?

Will it help me grow in my job as a CEO and chairman?

Can I make a positive contribution to the company?

Does it have a fair degree of complexity? For instance, I wanted something larger than my own business: one that was meaningfully global.

Is there a fit with the CEO? I think the benefit to a board of having a sitting CEO as a board member is greater today due to the enormous number of changes in the business and regulatory environment. Retired CEOs can play a role too, but they're not in the same battle day to day."

Randall Hogan

"The best way to put it is, what can I learn and what can they learn. What can they contribute to my personal growth and what could I contribute to theirs."

Edward Mueller

How do you define board chemistry?

"Good chemistry is essential. A board must have mutual trust, self-confidence and transparency. No issues should be hidden or 'coded.'"

Tony Wyand

"Good chemistry is a positive atmosphere, which includes the ability to express strong views in a positive way and the willingness to work together. What contributes to a board's chemistry? Diversity and complementary profiles, hard-working board members who actively participate."

Christine Morin-Postel

IMPLICATIONS FOR DIRECTOR RECRUITING

Recruiting new independent directors today can be difficult and time consuming. The desire for specialized expertise and increased diversity in the boardroom — and in some cases the requirement that boards become more diverse — has increased competition for some candidates. At the same time, many directors are accepting fewer board assignments than they did in the past and more companies, particularly in the U.S., have restrictions on how many additional outside board roles a director may accept. As a result, many directors are more discriminating than in the past about which boards to join.

> Tap into the expertise and brain power of directors by structuring board meetings in a way that gives directors the opportunity to engage with one another, rather than having a series of presentations.

Boards can improve the chances of attracting directors with the most relevant experience by understanding the motivations and concerns of director candidates and the company's perceived strengths and weaknesses. Here are a few lessons from the front line of director recruiting:

- Assume that there will be good competitors for a candidate's time, whether it is another board opportunity or another interest.
- Understand your board's "value proposition," based on where the company is strategically, the kinds of issues that come to the board, the composition of the board, the strength of the management team and even the quality of the board's new-director orientation.
- Carefully define the expertise that is important for the board, for example, industry or functional knowledge, language ability or international business experience.
- Continuously review the board's skill-sets relative to the company's strategy and direction to ensure that the board as a whole has the knowledge, experience and skills to guide the management team as it addresses new challenges and market opportunities. The annual board self-evaluation is a natural platform for the full board to review its composition and discuss the expertise that it will need in the future.
- Define the board's notion of chemistry and promote an environment that encourages active participation by every director and is respectful of differing views. The chairman or lead director plays an important role in creating this environment and getting contributions from everyone around the board table.
- Make board service a rewarding experience for directors. Tap into the expertise and brain power of directors by structuring board meetings in a way that gives directors the opportunity to engage with one another, rather than having a series of presentations. CEOs gain additional benefit when they develop one-on-one relationships with individual directors.

"If you get the right chemistry, you'll have a good board. It's about people looking forward to the next board meeting and feeling that they have an opportunity both to learn and to contribute, either at the board meeting or subsequently. For me, a board that works well is one in which individual executive directors feel able to pick up the telephone to nonexecutive directors who may be able to help them with a specific issue and just ask advice without feeling the need to go through the chairman or the chief executive. Once you have achieved that, you've got a board that's working, and that doesn't necessarily come terribly easily."
Philip Rogerson

"It is important to have chemistry in which directors vigorously interact. However, it is important that everyone comes together to adopt a point of view about the direction that the company is going to take, and that everyone gets on board with the decision and supports the decision, that it not be a divided decision. It doesn't mean consensus. It means that everybody is heard, the issue is vigorously debated, but in the end, everybody needs to come to a conclusion on the direction to be taken."
Louis Lavigne

"Chemistry is a matter of mutual respect, before all things. If the board members have mutual respect, then it doesn't matter how diverse they are. They've got to be able to recognize capability in the people who are not like themselves."
Chris Gibson-Smith

"It is a board where there is a culture of consensus and where nobody wants to impose his views and will do the best for the company interest. It includes mutual respect and the willingness to work together. Good chemistry is not a given. You have to build it."
Denis Ranque

A Advice for the CEO

"Have the courage when they're in your knickers trying to run your business to say, 'That's not your job,' and have patience when they don't understand or you haven't presented your strategy in a way that they like, including CEO succession."
Edward Mueller

"Consider your board as a support and not as an enemy; and be open with your board and expose your team to the board."
Denis Ranque

"I think it's important for CEOs to sit on other boards, so they can empathize with their own board. Before I sat on another board I wasn't sensitive to how selectively informed an outside director can feel. After understanding that, we raised the standard that we use for informing our own board. When you sit on someone else's board as a CEO, it is much easier to understand the difference between managing and oversight."
Randall Hogan

"The number-one thing is trust. You must have open communication, transparency and vulnerability."
John Wiehoff

"Really use the board as a sounding board."
Daniel Camus

"Don't be afraid to discuss your innermost worries with the board. The biggest thing you have to worry about is what you don't tell the board, not what you tell them. My other piece of advice is to figure out how to best leverage the capabilities of the board to add value to what you're doing."
Louis Lavigne

Experienced directors want to serve on well-managed boards that make a difference in the performance of the company. They want to work with smart, engaged directors and be comfortable with the CEO's leadership capabilities and character. Finally, they want to serve on boards that allow them to learn and build new skills. When they find board opportunities that offer these professional and personal rewards, they are willing to accept a new director role — despite the pressures and demands.

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Patrick B. Walsh contributed to this article.

UNDERSTANDING EXECUTIVE POTENTIAL

The underappreciated leadership traits of the most successful executives — and why they're important

CATHY ANTERASIAN, *Silicon Valley*
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How can an executive who is brilliant in her area of expertise — "the smartest person on the team" — end up failing at the next level of management or in a key international role? Why does a senior leader who has mastered the execution of strategy in a very complex, global business struggle in the next role that requires him to set and evolve the strategy?

Leaders are invariably surprised when a high-performing executive on their team fails to deliver in a different or more complex situation, but they shouldn't be. Most organizations have a limited view of the potential of their high performers, for several reasons:

- The traditional definition of "smart" tends to be narrow, often focusing on an individual's depth of knowledge in a particular subject area or his or her verbal acuity.
- Executives are typically evaluated on their track record in their current or most recent positions, or on attractive personality traits, such as energy or charisma. Significant domain expertise, strong relationships and relevant skillsets allow individuals to excel in narrower roles, even when they lack the fundamental skills necessary to succeed in the next job.
- Most companies lack ways to gain a more nuanced understanding of an individual's capabilities, especially their potential for complex roles beyond their current expertise. Few organizations have a method for measuring the underlying drivers of leadership effectiveness, which limits their ability to make informed judgments about how someone is likely to perform in future positions.

One way Spencer Stuart works with clients is to help improve their understanding of the fundamentals that drive executive performance and evaluate how the individuals on their management team stack up in those key areas. Formal assessments provide detailed insights into the strengths, weaknesses and potential of executives, and reveal the specific developmental needs of each individual so the organization can provide them opportunities to build skills and experience through targeted coaching or new assignments. Our assessments evaluate individuals in three areas: their business and functional competencies; their Executive Intelligence, or cognitive abilities relevant to business, including their problem-solving ability, understanding of people and self-evaluation skills; and the observations of others, who can validate the individual's performance in current and past roles.

The building blocks of great leadership

Drawing on extensive research and thousands of executive assessments, we have identified several leadership traits and skills that we see as fundamental to senior-level executive success, but that are often overlooked or underappreciated when companies evaluate individuals for their next position. We also include questions leaders can use to better understand whether high performers in one setting are likely to be able to make the leap to more challenging senior roles, particularly where existing knowledge will be a less important factor for success. These questions will not produce the insights of an in-depth executive assessment, but are meant to help executives maximize the quality of their judgments around these fundamental skills.

The knowledge and skills that propel an executive early in his or her career — such as domain expertise, knowledge of the business and strong relationships — are not necessarily good predictors of an individual's ability to excel in the senior-most roles. As a result, when organizations focus on these strengths rather than the leadership traits that are essential to success in new and highly complex roles, they can make the mistake of placing a strong performer in a position beyond their capabilities.

Exceptional business judgment

Executives' knowledge of the business, technical expertise and understanding of how to get things done in an organization are critical to their career advancement and effectiveness in a role. Individuals with extensive experience draw on their knowledge when making decisions about the business; they understand the competitive and market issues, the capabilities of the organization and the potential consequences of different courses of action.

However, domain expertise itself is not sufficient to excel as a CEO or in the other most senior roles in a company. Executives at the top have to be able to operate in an environment with a great deal of ambiguity and many unknowns. The issues they face are more complex, and their decisions have broader impact and have to be made with less information and, often, with less time to deliberate. Executives in these roles must be able to go beyond executing strategy to setting and evolving strategy.

To be effective at this level, leaders must be able to frame problems accurately, see issues from multiple perspectives, make reasoned judgments about how to proceed or not proceed, evaluate the quality of information that may be outside of their area of expertise, tease out areas of priority or emphasis and foresee the potential consequences of different courses of action. This set of skills, which are critical to business judgment and decision making, are core to what we call Executive Intelligence.

Questions to consider

Do I trust this person's judgment in complex, ambiguous situations?

Has their decision making been tested when leading a team outside of their area of expertise and in situations of great complexity and ambiguity?

Ability to recognize interpersonal dynamics and apply them in decision making

Over time, successful executives typically have built strong relationships with other people across the organization, which they can draw on to get things accomplished. An experienced executive typically knows who in the organization has the necessary skills or knowledge for specific projects and has insight into other people's motivations and agendas. These relationships also help the executive navigate organizational complexities and provide behind-the-scenes sources of information and intelligence. When executives have good relationships, other people will tell them what is going on, warn them about potential challenges or landmines and tolerate their mistakes.

But leaders at the very top may not have the luxury of these established relationships when they have to make decisions and influence behavior. At the most senior levels, executives have to be skilled at operating in politicized situations and reading the power dynamics — both internally and externally. They need to be aware of how others might perceive their words and actions as well as the internal dynamics related to competition for resources and individuals' efforts to position themselves with the board or CEO.

Leaders who do this well are able to accurately identify the issues and perspectives that are central to a conflict and balance the different needs of relevant stakeholders. They recognize the agendas and motivations of individuals and groups who are involved in a particular situation and anticipate the emotional reactions that people may have to actions or communications. This set of skills, related to an individual's social intelligence, is another critical component of Executive Intelligence.

Weakness in this area can be very costly to executives. People who score lower in social intelligence often misread the complexity of a situation, tending to ignore or overlook the behind-the-scenes dynamics or less obvious players who may have an impact on the outcome. They may struggle to find the right balance between safeguarding relationships and pushing the agenda forward, either forcing an outcome at excessive cost or failing to advance a business objective in the interest of avoiding conflict. Even individuals who are brilliant analytically can sabotage themselves or their programs by saying the wrong thing to the wrong person at the wrong time.

Questions to consider

How effectively does the executive read and respond to interpersonal dynamics in sensitive, high-stakes and complex situations?

Does the individual understand the power of his or her words and actions on others and quickly create alignment among stakeholders with divergent interests?

Can he or she successfully navigate politicized situations where personal relationships and a cooperative style are not sufficient?

Highly effective people management and team building

Many of the very best executives command extraordinary loyalty from their people and, at the same time, maintain the pressure to perform at a very high level. These leaders are simultaneously tough and demanding and well-respected and loved by their teams. They do this by being clear about expectations, relentless about holding people accountable for results, and by creating an environment where members of the team feel trusted and empowered to make a difference.

Strong leaders in this area are willing to delegate to their team and listen to their ideas. They give people the creative freedom to accomplish their tasks as they see fit, while holding them accountable for results and taking corrective action when commitments are not met. By creating such an environment, these executives put themselves in a position where they are able to cherry pick and evolve the best ideas from their team.

Questions to consider

Does this person have a track record of building high-performing teams?

Is he or she willing to hold people accountable when they fail to meet objectives?

Does this person create an environment where people feel motivated to contribute, while also holding others to high standards?

Humility and substance

The traditional view of a business leader is an individual with a commanding presence, who conveys confidence and certainty. Today, we take a more balanced view of the ideal leadership style. While executives still should be confident and decisive when appropriate, they increasingly are expected to be humble, self-aware and transparent.

This change in expectations is being driven by both internal and external forces. In the wake of corporate scandals, the financial meltdown and very public business crises, trust in corporate leaders has eroded. Governments and the general public look critically at leaders who don't seem to "get it" or whose egos keep them from listening to the concerns of others. Meanwhile, changing expectations in the workplace also demand a more open and transparent style of leadership. Younger workers are less comfortable in a command-and-control environment and want to work for companies where they feel they can make an impact and where their values are aligned.

This set of skills represents the third component of Executive Intelligence. Executives who excel in this area continuously signal that "it's not about me, it's about us." They cultivate self-awareness and are conscious of the different work styles and communication styles of others. They are willing to listen to the ideas and concerns of others without becoming threatened or shutting down discussion. When their point of view is challenged, the best leaders are able to park their ego and recognize the opportunity to hear the substance of somebody else's argument, work hard to understand it and apply it, rather than go into defense-and-attack mode. Reacting negatively at these critical moments can close the door to future dialogue and input from others.

Questions to consider

Does the individual show the mental flexibility to quickly evolve their thinking based on others' inputs?

How does he or she react to feedback or criticism of their ideas?

Does he or she really listen to substantive input from people who know? Does he or she seek it out?

Great developers of people

The best leaders collect other great leaders over time. They attract strong people to their teams. They invest the necessary time to personally coach members of their team through informal conversations and ongoing feedback about what they are doing well and areas to improve.

Most executives today understand that developing a strong team is a very important requirement of effective leadership, and a growing number of organizations expect senior leaders to groom successors. Executives who truly excel in this area are committed to developing their teams and are able to talk about the stars who have worked for them in the past. They keep track of these individuals' careers and can describe their developmental milestones.

Developing talent requires much more than once- or twice-a-year performance evaluations. It involves a proactive and sustained commitment to coaching team members through formal and informal approaches. When executives are skilled in this area, there will be a pattern of results — individuals inside and outside the organization whose careers have been shaped significantly because of their relationship with that executive.

Questions to consider

Is talent development a priority for this executive? How has he or she demonstrated that it is a priority?

Are there a number of individuals in the organization whose careers have been shaped through their relationship with this executive?

The ability to drive change

People often view driving change as an organizational task, requiring, for example, a realignment of processes or the development of a new structure that makes sense on paper. But truly driving change is an activity that touches every element of an organization — people, processes, structure, culture and strategy. The ability to initiate and drive change, then, is a hugely complex task that requires a very broad skill-set, including business judgment and strategic insight, social intelligence, self awareness and excellent people management skills. In addition, driving change requires influencing skills and, as one moves to the highest levels of an organization, the ability to inspire from a distance.

A CEO or other top leader does not have direct relationships with all of the people in the organization who must buy into and help execute a new vision. So, to lead change at these more senior levels, an executive has to be able to connect, engage and influence from that distance in order to infuse an organization with a sense of purpose and the motivation to do the hard work of change, especially in the absence of a crisis.

In reality, an individual is unlikely to excel equally well in all of these areas. Some people have the visionary and strategic skills that enable them recognize opportunities to change, but lack the ability to influence people throughout the organization to get on board. Others are brilliant at implementing change that someone else initiated, but are not good at envisioning alternative directions.

Questions to consider

What are this person's strengths? Does he or she come up with the big ideas? Are they most skilled at executing an idea from elsewhere?

In past situations of change, what was the individual's role in developing the vision, influencing and motivating others to embrace the idea, and driving to a result?

Conclusion

While many people have built successful careers on the strength of their domain expertise, strong relationships and knowledge of the workings of the business, executives who ascend to the highest levels of an organization require skills that transcend experience and situational knowledge. These fundamental leadership qualities, which enable executives to deftly stretch into new and more demanding roles, include:

- Exceptional business judgment
- The ability to recognize interpersonal dynamics and apply them in decision making
- Highly effective people management and team building
- Humility and substance
- Effective people development skills
- The ability to drive change

Few individuals possess all of these capabilities in equal measure, but executives with more of the fundamental skills can be stretched much further, much faster than others. In fact, data from our executive assessments reinforce the importance of these skills as a driver of executive performance: CEOs and CEO candidates as a group score markedly higher on average than other executives in the three areas of Executive Intelligence — business judgment and problem-solving ability, social intelligence and self-evaluation skills.

By understanding the capabilities that are fundamental to executive performance and learning how to recognize them in individuals on their team, CEOs and other leaders can make better deployment and development decisions when considering individuals' potential to excel in their next position, and beyond.

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THE CEO AGENDA

How CEOs are prioritizing for the year ahead

THOMAS J. NEFF, *New York*

CEOs today have no shortage of priorities and issues vying for their attention and company resources. Several forces are converging to increase the pressures and complexity of the CEO role and influence CEOs' top priorities. These include: the financial crisis, the subsequent recession and its prolonged effect on the economy and business outlook, new opportunities and challenges in emerging markets, competitive threats from evolving business models, uncertainty over government actions and decisions, changes in customer expectations, not to mention a variety of developments on the corporate governance front.

As a result, many CEOs are asking themselves and their organizations how best to respond:

What new and different growth strategies should we explore or embrace?

How can we best manage change in the face of new regulatory developments, or other governmental priorities?

What critical markets — China, the entire BRIC group or other geographies — should be at the top of our agenda?

Do changes in customer behavior, disintermediation threats or other new opportunities demand a response in the form of new business models?

Should we be rethinking our risk management philosophy or processes?

How can we re-engineer our supply chain to improve quality and become more efficient?

In light of the above, what changes should we make to our talent and leadership development priorities and processes?

Of course, changes to strategy or operational processes may require CEOs to enhance skills or call on different strengths. During the past two years, we have seen a greater demand for turnaround, crisis management and restructuring skills. More recently, we have begun to see a shift back to growth-focused CEO specifications. In light of the current challenges, other important capabilities include: investor interaction and public relations savvy; an understanding of the regulatory environment and an ability to interact effectively with various governments; on-the-ground international experience and global perspective; and disaster planning.

With these changes in mind, I invited a handful of experienced CEOs of global companies across industries to weigh in on the key themes in business today by highlighting a priority they will be focusing on in the year ahead. Of course, each of these leaders has a far more extensive agenda than presented here, but, by highlighting one or two primary objectives from each, my goal is to convey the breadth and diversity of the challenges facing CEOs. While companies' specific priorities may differ by industry and region, the themes these CEOs discussed during our conversations represent some common concerns.

Navigating a new regulatory landscape

We've had the biggest regulatory changes in 75 years across the financial industry domestically and, now with Basel III, internationally. This will be a net positive for the markets because it will introduce stability, better capital buffers, better liquidity, reduced risk profiles and more disciplined oversight. Business leaders will have to adjust their models by taking a clear-eyed view of where they get a return on capital in each of their businesses and regions, and feeding and starving businesses and regions accordingly. For Morgan Stanley, this involves shifting our focus from proprietary investing and trading to using a balance sheet in our client-related activities — moving from a more inward-looking focus to a more aggressive external focus. Secondly, it's applying more discipline in each of our businesses based on the capital they use and return they get, and adjusting the model accordingly. Thirdly, it is incumbent on us to grow in the core BRIC countries and other international markets, but our focus will be to put more resources in fewer markets; narrower and deeper is how I would characterize it.

These changes will call for a skill-set among the management team that is more focused on execution. To generate the same return, you have to be much more disciplined, both on the expense side and the return side. So, you need real business operators, business getters and people magnets. In our industry, we've been very long on business getters and people magnets, and less so on exceptional operators.

It's very hard during a period of great turmoil and change to have patience and stick to your long-term vision, but we're determined to do that. We have a business model that we like. We're transitioning ourselves in terms of our financial structure, skill-set and the infrastructure supporting our various businesses. I'm determined to keep a clear eye on the long-term objective and not be blown around by short-term trials and tribulations.

James Gorman
CEO, Morgan Stanley

Balancing cost control and innovation

Last year was a very difficult year in the aluminum business, given a 60 percent decrease in prices. Therefore, we placed enormous focus on cash management. We made an extra effort to shed costs and accelerated the divestments of elements of our portfolio. Even in that challenging period, however, we never lost sight of what I would call "true north" — profitable growth — nor did we stop investing in opportunities in the upstream, midstream and downstream businesses.

For example, with a Saudi partner, we are building in Saudi Arabia one of the largest and lowest cost integrated aluminum systems that has ever been built on this planet. We just brought on line and are ramping up our new bauxite mine in Brazil on the Amazon, which is connected to a refinery in the northern part of Brazil. Also, we have a new smelter in Iceland that runs totally on hydropower. Even during the crisis, that was one of the few smelters that ran at maximum capacity, given its attractive position on the cost curve.

The downstream business is also about innovation. During the crisis, we accelerated the speed at which we introduced innovations. One of these innovations is a new aluminum wheel that is self-cleaning and much lighter than steel and even our competitors' aluminum wheels. We also have expanded into new areas, the most notable of which is consumer electronics. Growing out of its emphasis on sustainability, Apple has switched its whole product line to aluminum. This material is infinitively recyclable; 75 percent of all aluminum produced on this planet is still in use. Its surfaces look great and, because aluminum is heat conductive, it eliminates the need for a ventilator, allowing for a very thin form factor.

With the world more competitive, one of our key priorities is to bring down costs on one hand and, where innovation matters, increase the speed of innovation.

Klaus Kleinfeld
CEO, Alcoa

Re-engineering the supply chain

Given our experience with the 787, the hard lesson that we learned is that we need to have better control over the supply chain. Most companies today are pursuing a business model where the suppliers are assuming more responsibility for design and production. The financial model is very seductive because you are not investing in the assets, your suppliers are. But in moving to a more horizontal model, some businesses have lost sight of the fundamentals of delivery and quality. I think we will see more industries, including ours, get back to a more vertical orientation in order to get a firmer grasp on both quality and schedule.

There is a balance that needs to be achieved, and that balance will be different for each industry. Owning every element, all the capital, all the costs and all the people vertically is a difficult financial proposition in a globally competitive world where you're competing against the best of each element in the supply chain. Having said that, you can't go to the other extreme, allowing your product to be held hostage by the weakest link in a supply chain you don't control.

You have to take responsibility for those elements that do bear on quality and schedule. For example, if first-time engineering quality is critical, as it is in everything we do, and if having a global visibility on your supply chain is critical, then you can't let those things go. You have to know what the long poles in the tent are. No matter what the investment is or the management task or the costs necessary to manage it, you have to realize that your customers will stop buying from you unless you manage those things. If you are keeping the right things in-house with a mind toward quality and schedule, you have a much better chance of managing the supply chain most effectively.

W. James McNerney Jr.
CEO, The Boeing Company

Focusing on the basics

I wish I could highlight just one priority, but our agenda is complex. If I had to choose one primary theme for the year ahead, however, it would be to continue working hard on the basics. It's not glamorous, but it is important to our strategy to get these things right. It boils down to even stronger execution and seizing *the opportunities we have identified. Primary among these opportunities is to continue to build commercial and business development capability to enhance margin capture, generate organic growth and identify potential acquisitions. We need to sharpen our execution in a brand-led strategy for the fuels business. We're working on unlocking shareholder value through the separation of the coke business from the fuel business. We must continue to relentlessly pursue opportunities to reduce overhead costs and achieve procurement savings. We also are building on our operational excellence focus in manufacturing, which includes process safety and reliability at a competitive cost structure. Of course, we have to have the talent to excel in all these areas, so talent development across the organization is also a top priority.*

Lynn L. Elsenhans
CEO, Sunoco

Becoming a flexible organization and a visible voice with government

One of the themes that I emphasize with our investors and our people is that, despite changing times and changing environments, we need to have a consistency and constancy of purpose and direction. Eighty percent of what a business does should be the same, regardless of the current circumstances. This includes all the basics that we sometimes take for granted, but have very real consequences for business performance: focusing on the customer; improving growth and productivity every year; developing new products and services that customers want; maintaining good employee morale.

With that as a backdrop, a couple specific things are concerning me as I look ahead. The first is maintaining flexibility in light of the unpredictability of demand. It's much easier to run a business when everyone expects GDP to grow 2 or 3 percent a year; it's much more difficult when no one knows whether GDP will grow 1 percent or 4 percent or even fall. So, we're focused on flexibility, both with our suppliers and internally, to make sure we can respond to growth in demand if we need to, but also maintain costs at a level that makes sense if growth doesn't materialize.

The other concern on my agenda is staying engaged in the regulatory process. I'm always surprised by the general suspicion of business by government — and this is generally a worldwide phenomenon. Over the next two or three years, governments are going to be increasingly important players in business as they try to figure out how to get the global economy and their national economies moving again and, at the same time, put in place preventative mechanisms to ensure the "great recession" never happens again. As business leaders, we all need to be involved and stay engaged with government, not just saying, "Don't do that," but saying, "Hey, here's what you ought to do." We need to make sure that our point of view is heard, even if it's not always agreed with.

David M. Cote
CEO, Honeywell

Investing in technology to improve healthcare

Aetna is in the business of helping people live healthy lives, and good health is a universal need.

In January 2010, the World Economic Forum identified chronic disease as a global risk with systemic impacts equivalent to those of fiscal crises, high unemployment and underinvestment in infrastructure.

Obesity, unhealthy lifestyles and urbanization, compounded by aging populations, are major contributors to the increased prevalence of chronic disease. These factors drive higher utilization of health care services, in turn increasing costs. While different countries spend different amounts on healthcare, underlying healthcare costs are increasing for countries around the globe, regardless of the healthcare system they support. As chronic disease and the demand for healthcare services increase, there will be greater pressure on finite resources, leading to economically unsustainable healthcare systems globally.

As we look ahead to 2011 and beyond, making quality healthcare more affordable and accessible is at the top of our agenda. Aetna is investing heavily in technologies that identify health risks and help people manage their conditions. Optimizing technology across global health care systems to improve the flow of information can lead to important breakthroughs in managing the health of populations; increase transparency; and broaden the use of evidence-based medicine to support clinical decisions, improve outcomes and reduce costs.

Our hope is that, using our experience and intellectual resources, we can build stronger healthcare systems to create a healthier, more productive global community.

Ronald A. Williams
CEO, Aetna

ABOUT THE AUTHOR

Thomas J. Neff is chairman of Spencer Stuart U.S. He founded the Board Services Practice in the U.S.

Wanted: CEO 2015

ANJALI BANSAL, *Mumbai*
JAMES M. CITRIN, *Stamford*
JONATHAN SMITH, *London*

With the increasing complexity of global business and pressure mounting every day, the CEO's role continues to evolve. We wanted to explore how the role of the CEO might be different five years from now. To this end, we have created a brief case study that reflects some of the important trends that may influence the priorities of future CEOs, as well as the skills and characteristics they are likely to need in order to be effective. These trends include the globalization of corporate ownership, expansion into new markets, the need for new business models and the relationship between government and business.

In this article, three Spencer Stuart consultants respond to the case study, which describes the background and leadership needs of a business set up in 2015 to exploit new opportunities in developing markets. The company is hypothetical, but the conversation is real.

Case study: Devotel*

With exponential growth in the microfinance movement and a banking system incapable of expanding its branch-based operations profitably to handle high-volume/low-value transactions, governments in developing economies have started to recognize the economic value of putting banking within reach of the mass market. Mobile telecoms companies are set to play a critical role. Licenses are being offered on favorable terms, regulations are loosening up and corporate tax rates are coming down for pioneering companies willing to solve the logistical complexities of bringing mobile banking to low-income populations.

Neshtel, a fast-growing, family-controlled, Indian telecoms company part-listed on the Bombay Stock Exchange, and Showtel, a European mobile virtual network operator, have created a joint venture in order to expand their operations into developing markets in Asia Pacific, Africa and Eastern Europe — with the goal of becoming a global leader in mobile banking. For some time, both companies had been eyeing the potential to provide much needed banking services to low-income populations in countries whose rural poor (in particular) are ill-served by the existing retail banking infrastructure. The newly formed company, Devotel, also has ambitions to exploit its expanding mobile distribution network by extending its services into new areas such as insurance, shopping, entertainment, education and tele-medicine.

Thirty percent of Devotel's share capital has been raised from international investors, including two sovereign wealth funds. Devotel's chairman, Raj Charma, has real stature and wisdom, but he is neither a banker nor a telecoms expert. He has a large international board with all the major shareholders represented; the four independent directors are in a minority. The board is looking to appoint a CEO who will be responsible for developing a strategic plan and delivering outstanding results based on the outlined goals.

The CEO will be expected to bring a diverse set of skills and experience to this challenging role, and be capable of forging strategic alliances and joint ventures with financial services, retail and content-oriented businesses through Devotel's network of national subsidiaries. The CEO will have access to Neshtel's head office functions, but will be expected to assemble and retain a world-class team, based in Dubai, with the necessary expertise and entrepreneurial flair to deliver results on the ground.

*Company and individual names are fictional.

Observations on the company

CITRIN: Devotel sounds like a complex, fascinating and important business with tremendous potential; whoever ends up at the helm would face a demanding test. First, let's establish what kind of a business this is before we consider the skills and experiences that might be needed in the CEO. On the face of it, as other new businesses before it, this is a converged business, combining telecoms and banking. Mobile phone technology is breathing new life into virtual banking and changing the way remote communities function. For people who live nowhere near a bank branch and have never seen an ATM, this is a mini-revolution.

BANSAL: From a business perspective, it is a huge untapped market. In some parts of India, for example, a mobile banking business serving the rural poor could grow 100 percent each year. Yet it's not a straight-forward capitalist enterprise. Devotel will be fulfilling an important social mission wherever it operates, so the political economy dimension will have a crucial bearing on investment and hiring decisions. In certain markets, conflict between social and financial return could be the source of considerable tension.

One of the key decisions for the CEO will be to work out the priority markets to invest in — there are potentially 50 or more countries where this business could take off...

SMITH: The notion of Devotel adding other financial services into the mix and ultimately becoming a distribution vehicle for a wide range of consumer goods and services is interesting. It is a logical ambition, but how realistic it is in the short term is debatable. You can imagine some of the key investors having conflicting expectations, which might lead to fundamental disagreement on the board over priorities. This business has a complicated ownership structure and there's a real danger that Devotel's principal shareholders are going to find it hard to agree on what kind of business they're in and where the capital should be invested. One of the key decisions for the CEO will be to work out the priority markets to invest in — there are potentially 50 or more countries where this business could take off, I imagine.

BANSAL: This is a company that could go in a number of directions. Solving a CEO assignment without knowing what the company expects to look like in the medium term is extremely difficult, which begs the question: Does it make sense at this stage to consider all of the company's possible futures, or should we be focusing on what is really essential during the first three years or so?

CITRIN: With all the major shareholders represented on the board, it will take all the chairman's experience to establish a consensus on where the business should focus, what the model should be, and the board's appetite for risk. On the question of geographic expansion, you could easily imagine one faction set on Asia, with another wanting to prioritize the African continent.

SMITH: The chairman's role is pivotal in establishing a direction for the business and keeping the board on message. I think that the CEO coming into this situation will want and need to establish a very clear remit, agree on the strategic priorities early on and be very confident in the chairman's ability to keep the board on a tight rein. The business is going to be complex enough operationally, without having to worry about shifting priorities, or lack of consensus over investment decisions, or conflicting expectations of financial return.

BANSAL: The chairman will also need to exercise all his or her diplomatic powers outside the board; by adopting an active role as ambassador for the business with politicians and government bodies he would be doing his CEO a big favor. This task could easily distract the CEO from running the business. There is no mobile banking system that is globally acceptable to regulators, which means that the chairman and the CEO will have to work closely to overcome all kinds of regulatory hurdles. Furthermore, as the chairman of a highly visible and politically sensitive company that makes a profit by serving the poor, he will need to retain a high profile — promoting the social benefits of Devotel's business and, whenever necessary, drawing fire from the CEO.

CITRIN: The relationship dynamics between the chairman and CEO are crucial to the success of an enterprise like this. The CEO must be able to work hand-in-glove with the chairman — one in a leadership and operational role, the other as an ambassador.

SMITH: However important the chairman/CEO relationship is, the board should not lose sight of the fact that the person who kick-starts this business may not be the right person to take it into phase two — whatever that looks like. In similar situations in the past, we've expressly said to clients that the person you want to hire today is not the person you'll want in that role in three years' time. The worst thing you could do in situations like this is try to appoint somebody who will be all things to all people, because they often end up not satisfying any of the needs.

BANSAL: It might be better to view the long term as a series of successful short-term scenarios — this is especially true in high-growth and rapidly changing emerging markets where long-range forecasts are challenging, if not impossible, with the simultaneously changing variables of technology, regulation and macro-economic dynamics. Boards need to be patient and supportive to ensure leadership continuity through periods of change.

The relationship dynamics between the chairman and CEO are crucial to the success of an enterprise like this. The CEO must be able to work hand-in-glove with the chairman, one in a leadership and operational role, the other as an ambassador.

CITRIN: Our analysis of CEO transitions has shown us that the stronger the performance of the CEO, the longer the tenure. It's quite possible that the right CEO will be capable of evolving with the business and maintaining the top leadership position over the long term. The reality here, though, is that Devotel needs someone to do a specific job and the new CEO should think of it as being hired to do that job. It's not a permanent designation, like faculty tenure or a coronation.

The CEO role — competencies & experiences

BANSAL: Let's consider what kind of person will thrive in this environment. You could make a case for a diplomat, a deal-maker, an operations expert or an entrepreneur.

CITRIN: We should assume that the principal shareholders will have different views on the characteristics and competencies needed. Developing the spec gives us an opportunity to help build alignment on the board and focus directors' minds on what is essential, as opposed to "nice to have."

Cultural fluency is a key attribute in this situation. You can't lead a cross-cultural organization on this scale without empathy and sophisticated cultural antennae.

SMITH: Despite the board's intention that Devotel should eventually diversify into other products and services, at the outset this is essentially a financial services business employing mobile phone technology to open up new markets and win new customers, many of them with little or no experience of banking.

BANSAL: So regardless of whether the CEO's background is in banking or telecoms, he or she will need to be able to win over the regulators, bid successfully for licences and work with government on infrastructure development and financing. And behind all that must be plenty of conviction, a clear vision and a desire to influence social policy.

CITRIN: Rolling out a mobile banking system across multiple jurisdictions also involves enormous operational complexity, so identifying someone who knows how to scale up a business is important; perhaps an entrepreneurial CEO who has successfully built market share. Just as important, though, given what this company is all about, this person should be driven by a mission.

SMITH: The CEO's job seems to me to be all about creating an effective market entry strategy — knowing how to tailor the proposition to different markets, how to employ capital efficiently, how to get the most out of third parties to deliver "in market." There's the big operational issue of how to make it all happen, but for me that comes down to the CEO recruiting a really first-rate team in the regions.

CITRIN: Cultural fluency is a key attribute in this situation. You can't lead a cross-cultural organization on this scale without empathy and sophisticated cultural antennae. You'd expect CEO contenders to have a serious international assignment under their belt, preferably one involving a developing market. If you look at any large mobile business today, it operates in multiple markets. To lead a business like this you don't have to understand every single market or culture, but adaptability and cultural fluency do matter.

BANSAL: You certainly need a great deal of sensitivity in a country like India, where there are vast social and linguistic differences at play between states, let alone across national boundaries. We should bear in mind that most candidates we talk to will belong to a particular socio-economic strata — fully understanding Devotel's consumer base will require empathy, a capacity for integrating with local communities and a sense of social responsibility.

SMITH: I would tend to put cultural sensitivity somewhat down the list. Let me explain why: the priority for the CEO is to understand the economic and regulatory model operating in each country, then be able to unpick it, figure out how to get the service offering to stick, and make money. You can be as culturally sensitive as you like, but if you can't crack the business model and devise a compelling entry strategy, it's wasted.

CITRIN: Devotel will have aggressive growth projections, and if most of that growth is to be organic rather than through M&A, then the winning candidate will need to show evidence of having built a business in that way. He or she will have demonstrated successful leadership in a market facing constant change, competitive pressures and integration challenges. I would also look for evidence that they were used to evaluating strategic opportunities and capable of making smart choices.

BANSAL: The CEO will need to understand risk, and not just on the downside, seeing clearly where the leverage is in additional markets and new products and services. The ability to recruit a formidable senior management team and manage that talent is going to be a critical test of the CEO's leadership. I would also expect to be looking for someone with an open mind and strong critical thinking skills who can work collaboratively with the leadership team and the board.

CITRIN: In my view, there is no business so large that one person cannot be responsible for it. However, it is certainly the case that no one individual can have all the domain expertise. The CEO needs to have some threshold level of credibility in one of the key areas (say developing markets or mobile or payments), coupled with a deep curiosity and an ability to problem solve, to learn, to know what he or she doesn't know, and to surround himself with those who do. The CEO will need to establish robust management processes that are appropriate for the evolving state of the organization and hold everyone to a high standard of operational excellence throughout what will inevitably be a period of rapid growth.

SMITH: In my experience, the further from the mother ship you try to operate the business, the more difficult and risky it can be, since you have less direct control over your people. The CEO is going to end up with a small number of regional directors who run the country operations and he or she absolutely has to get those hires right. You would expect the CEO to take a strong, personal interest in the recruiting process and then work hard at inculcating key hires with the values of the organization. Outstanding operational excellence will be a prerequisite.

Where will the winning candidate come from?

CITRIN: Even though Devotel is effectively a startup, we would want to look closely at the senior leadership teams within each of the joint venture companies in case there is a credible insider who is ready to assume control of the new business, although we would have to be careful that any internal candidates have the necessary breadth of experience, including genuine P&L responsibility. A credible candidate from within the telecoms industry would need to have had exposure to the complex and constantly evolving regulatory environment, and would preferably have been associated with the phenomenal recent growth in mobile phone adoption in the developing world.

The CEO will need to understand risk, and not just on the downside, seeing clearly where the leverage is in additional markets and new products and services.

BANSAL: It is the banking regulators that will be the most rigorous, though, and you could argue that a CEO with a banking background would be at an advantage — someone who understands credit, risk management and asset product distribution. However, bankers can have preconceived ideas of how lending is done and this might prove to be a weakness; Devotel's business is quite different from traditional banking, so it will be important to diversify our search and look at consumer and telecoms as well.

SMITH: There may be other talent pools beyond telecoms and banking/financial services worth considering: for example, senior executives from fast-moving consumer goods and services. A strong consumer orientation and the ability to develop a common brand across different cultures would be important; likewise, an appreciation of distribution and logistics. There are some senior executives who have taken retail brands extensively international, but the advantage of hiring a CEO from the consumer products side (e.g., Coke, Pepsi Kraft, Nestlé, P&G, Unilever) is that those businesses are used to taking products into very different markets. Getting bottles of Coke to 14,000 feet in Peru is wholly different from distributing it around Manhattan. The "market-entry" strategy and subsequent operational dynamics are diverse. My sense is that consumer products companies have done a great deal of what we're asking Devotel's CEO to do.

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The growing role of the board in risk oversight

KEVIN M. CONNELLY, *Chicago*
CAROLYN C. EADIE, *London*
VALERIE R. HARPER, *Stamford*

The oversight of financial risk is a well-established responsibility of the board. But as recent crises faced by companies such as Toyota and BP show, boards today are being held accountable for an ever-more diverse range of risks that can include safety, environmental, technological, regulatory and reputational risks, among others.

To gain an insider's perspective on the evolving role of the board in risk oversight, Spencer Stuart recently conducted several confidential interviews with the audit and risk committee chairs of leading multinational corporations in the industrial, life sciences, banking and financial services sectors headquartered in Europe and the United States. These executives shared their insights on the board's role in risk oversight, the skills the board requires to fulfill that role effectively, the pros and cons of creating a separate risk committee, and the steps the board should take to enhance risk management throughout the organization. We also heard their views on the role of the chief risk officer and its relationship with the board of directors.

With this article, we are not attempting to provide definitive answers to all of the questions boards have about risk oversight, but to offer a firsthand view from the boardroom on how leading companies and their board directors are reassessing risk.

> "Effective risk oversight is about courage — the courage of swimming against the tide when there's momentum for something, whether it's a new product or innovation or an M&A opportunity. And part of the courage is to accept that you'll have false positives and will be engaged in a degree of apology, but you won't be deterred."

Greater accountability

The directors agreed that the expectation that boards have a broader responsibility for risk oversight is not entirely new. It is instead a continuing trend that has merely attained greater prominence of late in the wake of the financial crisis and recent high-profile corporate missteps. In today's digital society, these missteps are much more visible, are transmitted more quickly and are more likely to affect the personal reputations of board directors in a negative way.

"Twenty years ago, it was unthinkable that individual directors would be profiled the way they are today, with their curricula vitae scrutinized in the press if something went badly with an organization," said one risk committee chair. "But today directors take a huge personal risk. Directors have to learn that they will be blamed for things that they didn't have an earthly chance of preventing or diagnosing."

Board directors are also confronted with a world in which the number and scale of risks they must examine have multiplied. In an increasingly global environment, this growing complexity of risk results from factors such as lengthening supply chains; expansion into emerging markets and the segmentation of existing ones; new regulations; more frequent joint ventures, mergers and acquisitions; and product lines of growing complexity and diversity.

The board's role: management or oversight?

In this complex environment, the directors we spoke with agree that risk can't be managed from the board level, but only overseen. A key responsibility for the board, then, is to set the company's risk appetite and culture. Taking risks — the right level and kind of risks — is critical to running a successful business. "I'm on the board of a reinsurance company," said one director. "There, a very valuable distinction is drawn between the risks the company is in the business to manage and the risks it has to manage if it wants to stay in business."

Once the board has decided upon the appropriate level of risk for its company, it should also communicate this risk appetite throughout the organization and oversee the creation of controls that keep the company operating within these established boundaries. "The board must set up a precise risk profile and risk tolerance, communicate it loudly and clearly to the business units, make sure that the business units remain within it, and see to it that the monitoring process captures any meaningful deviation from the profile and tolerance accurately and in a timely fashion," said one audit and risk chair.

According to directors, this is best accomplished by ensuring that there is an ongoing review of risk performance across the different categories of risk (credit, market, operational and compliance) and across the business units. Regular assessment of the strength of existing risk management systems and contingency plans is also important, from the company's accounting platforms to its technology, reporting and business continuity procedures.

The board cannot conduct these reviews itself, but is responsible for seeing that these review processes are in place. For example, one leading industrial company has a risk database that catalogs each of the 200 to 300 risks that have been identified for the organization. Each risk is assigned to a front-line person who is responsible for mitigating, managing and watching that risk. The internal auditor who reports to the audit committee, in turn, accesses that system to prepare his or her risk-related reports and analysis to the board.

In addition to seeing that the risk appetite is identified, supervised and monitored, the board can also play a role in ensuring that employee incentives are designed to reinforce the established risk culture, as opposed to rewarding risks by individuals that fall outside the desired risk profile.

Board skills for effective risk oversight

According to the directors we interviewed, the boards — and risk or audit committees — that are most effective at risk oversight possess a mix of skills. It is particularly helpful to have directors on the board who have a background in the company's industry. "It's very difficult to fully appreciate the risk management challenges a company faces without that understanding of the business," said one risk committee chair. "Risk is very different than leadership on the audit side, where it's primarily about financial reporting and financial controls — things that are to some extent generic across industries."

That being said, directors note that financial expertise is itself an important requirement in a board hoping to achieve effective risk oversight. For example, the audit chair of one multibillion-dollar industrial company explained that the value of his company's pension plan is equal to the company's market value, making financial risk an enormous component of the organization's risk portfolio.

Some directors argue that the addition of an outsider's perspective also can be important to help boards think about risk in a new way. "The board should include people who are capable of understanding the different dimensions of the business, but who come from another world, be it through adding someone from a public sector background or someone who has worked in other countries," said one risk and audit committee member. "There has to be a possibility of having a different sort of discussion on the board about risk from what you have on the management team."

Sometimes, it can be helpful if this diversity of perspective even extends to having board directors who may be viewed as counter to the company's prevailing culture. As one risk chair said, "Effective risk oversight is about courage — the courage of swimming against the tide when there's momentum for something, whether it's a new product or innovation or an M&A opportunity. And part of the courage is to accept that you'll have false positives and will be engaged in a degree of apology, but you won't be deterred."

The political difficulty of sustaining such a position is one reason many risk and audit

Risk oversight: A checklist for the board

- Define the company's risk appetite and culture.
- Make sure that risk expectations are communicated to the organization.
- Determine the appropriate risk oversight structure, including the role of the full board and audit committee and whether a dedicated risk committee is needed.
- Ensure that there is an ongoing review of risk performance across the risk categories (credit, market, operational and compliance) and across the business units.
- Make sure that the strength of risk management systems and contingency plans are assessed regularly.
- See that each risk is assigned to a front-line person who is responsible for mitigating, managing and monitoring that risk.
- Ensure that employee incentives are structured to support rather than undermine the risk profile.
- Consider the appropriate mix of board expertise: knowledge of the business, financial expertise, technical knowledge or outsider perspective.

chairs in the U.S. believe it is best to keep the board largely independent, with only one insider — the CEO — on the board. Those feeling this way believe that other insiders are compromised by their overall reluctance to have a difference of opinion with their CEO at the board level.

In some particularly complex businesses, however, the knowledge another internal executive can bring may be worth tolerating this dilemma. For example, in the pharmaceutical industry, the proliferation of biotech medicines has resulted in products that are becoming increasingly complicated to produce, with some pills containing more than 50 elements. To deal with the inherent complexity of the industry today, the board of one pharmaceutical company includes two directors with a science background in addition to three internal directors: the CEO, CFO and head of R&D.

Overall, effective risk oversight requires the board to have increased technical ability — in understanding the business and numbers as well as the stress tests and other measurement tools that can provide a fair picture of the company's major risks. "The trouble with risk oversight is that you have to up the intellectual stakes on the board to be able to do it," said one risk chair. "It can't be accomplished by a board in which the directors sit around and joke about all the confusing numbers that are brought to them."

Risk versus audit

While risk oversight is a responsibility of all board directors and is handled in some companies at the full board level, it is typically owned by either the audit committee or a dedicated risk committee. And while the audit and risk committee approaches can both be effective, the nature of the organization and the kinds of risks the business faces can significantly influence which approach makes the most sense for a specific company.

"The more a business is dependent upon the proactive taking of risk in a dynamic way, the more likely it is to be better served by a risk committee separate from audit," said one director. "If the risk profile changes very infrequently and is essentially around strategic and operational considerations, I think it's plausible that an audit committee can handle that in addition to its regular duties."

Those who argue against separating risk oversight responsibility from the audit committee note that the internal control system that the audit committee provides must still deal with risk assessment even if a risk committee is formed. This can create a weak boundary between the two committees, a strong risk of overlap and the possibility that issues could fall between the cracks of the two committees. Those who favor a structure centered on a powerful, global audit committee also argue against the formation of a separate risk committee because it can dilute this power.

Even those directors who favor the oversight of risk by the audit committee acknowledge that it is a time-consuming task, however. One audit and risk chair from the banking industry argues that at least half of the audit committee's time should be devoted to risk monitoring. Another risk chair who favors keeping risk oversight under the audit committee believes that separating the two committees can create a structural problem, but also admits that tackling every risk issue from the audit committee can mean day-long meetings for that committee.

As a result, one potential problem associated with keeping risk under the audit committee is the danger that risk will become a lower priority. "The problem is that so much of the audit committee's traditional agenda is time-sensitive," said one U.S. risk committee chair. "If you're going to oversee risk within audit, it requires discipline to ensure that the risk elements of the agenda do not become displaced due to the time constraints associated with quarterly earnings releases, 'Q' filings, Sarbanes-Oxley reviews and executive sessions."

For some companies, the extensive commitment already required by committee members just to fulfill traditional audit committee tasks may be the best argument for creating a separate risk committee. This is particularly the case for financial services companies, which are required by law in some countries to have a separate risk committee, and in some nations even to get regulator approval of the risk committee's composition. "For companies that are in the business of intermediating financial risk, I think it's very hard to argue that they wouldn't be well-served by having a sepa-

"The trouble with risk oversight is that you have to up the intellectual stakes on the board to be able to do it. It can't be accomplished by a board in which the directors sit around and joke about all the confusing numbers that are brought to them."

rate risk committee, because the workload of the audit committee is already so overwhelming," said one risk chair for a financial services company.

The role of the chief risk officer

As more boards create a separate risk committee to oversee enterprise risks, more organizations are also instituting a chief risk officer (CRO) role on the management team. While directors may disagree on whether the role is necessary, nearly all of the directors we spoke with believe that the appointment of a CRO should not influence the responsibilities of either the board or the CEO in regard to risk, though the CRO may help them in those tasks.

"It's easy for directors to sit there and look at dense pages of technical information, but that's not what boards are supposed to do," said one audit and risk committee member. "They're supposed to get their minds on the big questions and extract big messages, and that's where a good CRO can help. If you don't have analytical underpinning for these discussions, they are hot air. You've got to have both the intuitive and the analytical, and risk professionals help you hugely on the analytical side. The business judgment, imagination and life experience of the board members come into play on the intuitive side."

What the CRO should not do in many organizations is take on responsibility for risk management. "It's inconceivable to me that a CRO could handle the product and engineering complexity that we have," said the audit chair of one industrial manufacturer. "Responsibilities for those risks need to be embedded in the businesses, and if you're not going to listen to the employees in the trenches and hold them responsible for the risks they take, you will not have good risk management."

According to the same director, the CRO role is most effective when he or she instead is responsible for making sure that there is a risk management system in place in each business that includes effective risk-control mechanisms as well as information systems that flow up to senior management. According to another director, the CRO can also help shape the risk principles and policies of the company, determine analytics and methodologies to evaluate how much risk is being taken, track the capital risk capacity of the company, define who is responsible for managing the specific risks within the organization, and provide a framework for judging the effectiveness of risk-taking.

But while the CRO should have high visibility to the board and to the risk committee if there is one, the CRO does not function as the internal auditor does for the audit committee. Instead, as most directors we spoke

"You've got to have both the intuitive and the analytical, and risk professionals help you hugely on the analytical side. The business judgment, imagination and life experience of the board members come into play on the intuitive side."

with agree, the CRO is part of the management team, ultimately acting independently of the board and of the individual business units as the CEO's highest-level representative on risk.

A primary responsibility

The risk and audit committee chairs we spoke with agreed that risk oversight is one of the board's most integral responsibilities. It is also one of the trickiest, since risk by its very nature can never be reduced to a science. Things that no one could have predicted do happen, and in those cases, the board's role is to respond to the crisis in a sensitive, effective and comprehensive way.

But other risks are more predictable, and boards need the knowledge to determine the likelihood of risks, the impact if they occur and the company's appetite for taking those risks relative to its ability to absorb those impacts. By defining the company's risk appetite; ensuring that risk-taking is visible, appropriately monitored and evaluated throughout the organization; and creating employee incentives that support rather than undermine the selected risk profile, boards can largely fulfill their role in risk oversight. At the same time, following these steps can also help board directors mitigate their personal reputational risks associated with board service — and embrace the benefits of serving on the board of a world-class, well-governed organization.

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Additional interviews were conducted by James Colhoun, Carlo Corsi, Will Dawkins, Enzo De Angelis, Ollo den Tex, Duncan Reed, Bertrand Richard and Han van Halder.

LESSONS FROM THE BOARDROOM

SEVEN SUCCESSION PLANNING MISSTEPS BOARDS SHOULD AVOID

YVONNE BEIERTZ, *Frankfurt*
DAYTON OGDEN, *Stamford*
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Succession planning for the CEO role is a key responsibility of single-tier boards, just as responsibility for the succession of the entire executive committee is the supervisory board's obligation in a two-tier system. The days of boards waiting until several months before a transition and then accepting or rejecting the recommendation of the outgoing executive regarding internal candidates are largely gone. In well-governed companies today, boards fully understand that effective succession planning is an ongoing process that requires consistent, dedicated work on their part.

As they approach this complex and highly political task of succession more seriously, however, even the most well-intentioned boards can encounter pitfalls that can derail the process, offend internal candidates or negatively affect employee morale or the company's reputation.

This article highlights the missteps boards make most often in succession planning. By avoiding these mistakes, boards can handle succession planning more sensitively and sure-handedly to create a process that allows all parties involved — from the board directors to the incumbent executive, internal candidates and the company as a whole — to benefit from the experience.

1 Failing to align on strategy

Before deciding on a future leader, board members need to agree on the strategic direction of the company. Most board members assume their company has a fairly well-articulated strategy, but we have witnessed situations in which there was, in reality, fundamental disagreement between individual board members as to where the company should go. For example, one director may favor emphasizing the high-volume part of the business that earns the lowest multiple, while another sees more potential in focusing on the riskiest part of the business that earns the highest multiple but could sink the ship.

Wise boards reach universal agreement on these strategic issues up front, since these decisions will influence the kind of future leader or leaders the company will need. This is a critical step that helps make the process go smoothly, and helps boards avoid the common trap of choosing an executive who mimics the incumbent's strengths, instead of selecting the candidate with the qualifications best suited to the company's strategy for the future.

2 Over-involving the entire board

Succession planning is arguably one of the more interesting responsibilities of the board — and a task that many board members are eager to be a part of. It is also one of the most time-consuming board responsibilities, requiring significant work between meetings. While the entire board should be involved at critical touch points throughout the succession planning process, a smaller succession planning, nominating or personnel committee — that includes only directors who are the most qualified and who have the necessary time — can steer the process for the board and handle the granular work associated with assessment and benchmarking.

In our experience, the ideal size of this group is three or four directors for a single-tier board. The lead director or nonexecutive chair is often included in this group, and it can be helpful to include two board members who have the expertise of being former CEOs, but who are not active CEOs, given the time commitment. It is even better when at least one of these former CEOs also chairs another committee such as the nominating, governance or compensation committee. However, boards may want to avoid assigning the audit committee chair to this task because of the time commitment for that role. In some governance models and markets, the succession planning group may also include the company's current CEO acting in an "of counsel" capacity.

As this committee takes ownership of many of the details of succession planning, it should keep the rest of the board up to date and ensure its continued buy-in throughout the process. This should happen at the beginning to ensure that the board understands the process; upon the development of the key selection criteria for the position; at the review of the assessment summary of internal candidates; and upon the review of the benchmarking information on external executives.

3

Conducting internal assessments too late

Once the list of key qualifications for the role has been approved by the board, it is generally best if the assessment of internal candidates takes place as quickly as possible. The more time internal candidates have to focus on their developmental areas, the better the chance that one or two of them can become a serious candidate. If an executive is told three months before the transition that he or she really needs an international assignment to get ready for the role, obtaining that experience is not a realistic option. But if that information is shared a few years in advance, the executive can gain the experience needed to contend for the role.

By conducting internal assessments early, boards also have a chance to create the proper developmental plans for those internal candidates who, upon assessment, are clearly not ready to assume the role during the next transition. Medium- and long-term planning keeps executives engaged and builds the company's bench strength for future succession opportunities.

4

Creating a "horse race" too early

Whenever possible, companies should conduct a formal assessment of internal candidates two or three years in advance of an expected transition. However, avoid organizing a process that fosters excessive early competition between candidates or that intimates in any way that the process is an interview for the job.

Instead, it is usually more helpful to position the assessment exercise as principally supporting the career development of the people involved. The executives assessed will no doubt realize that the process could have bearing on succession. Because of this, we recommend clearly communicating that the company has decided to make a significant investment in their career by putting them through a rigorous process and giving them feedback. Internal candidates should be aware that the board will monitor their progress against their development objectives periodically over the next two or three years as it goes about its fiduciary responsibility of planning for long-term succession.

This approach can make the process a valuable — and valued — developmental exercise for each of the executives involved, rather than spurring a horse race between candidates that creates winners and losers and can negatively affect the company's retention of top executives who are important to the organization.

Another consideration in handling this politically sensitive process is to carefully choose the group that will undergo assessment — whether it is the executive committee, the operating group or the CFO plus any business heads. If this process is done properly and started early enough, there is no reason it cannot be a very constructive process for all concerned, including the people who do not get the job.

5 Neglecting external benchmarking

The benchmarking of internal candidates versus external ones is a sensitive issue, but it is also an important component of effective succession planning. Just as companies benchmark their products, manufacturing operations and financial management processes against the best in class, they can also benefit from seeing how their executive leadership stacks up against that of other companies in their industry.

Ideally, benchmarking should happen in tandem with internal assessment, so that the results of the internal assessments and external benchmarking can be compared simultaneously. This process is critical to giving the board a good sense of the relative strength of the internal candidates, as measured against the outside talent pool that would likely be considered for the role, based on the priorities for the position.

It is generally best to be transparent with internal candidates about the purpose of and approach to the benchmarking process. In our work with clients, we benchmark internal candidates in two ways. The first is through an assessment instrument that will compare them against the thousands of other executives who have gone through this process, and the second is through a less scientific comparison of their strengths and weaknesses to those of select executives outside the company. Communication with internal candidates should stress that both steps are being taken to assist the development of the internal executives and help them become best-in-class leaders. It should also be reinforced that external benchmarking is not a search, but merely a confidential desk-based research exercise that evaluates the strength of potentially ready candidates on the outside.

6 Overvaluing external candidates

When boards look at internal candidates, particularly those who have undergone rigorous assessment, they understand the strengths they could bring to the role — and are just as aware of their weaknesses. But because outsiders do not typically undergo the deep assessment that internals do, it can be easy to forget that they have downsides and development needs too.

For this reason, when there is genuine uncertainty about whether one of the internal candidates can be a favorite for the position, we often recommend that a gap analysis be performed. In this exercise, we take the best internal candidate or two and stack them up against the best external benchmarks using the selection criteria.

If the analysis results indicate that the external benchmark is at least 25 to 30 percent better than the internal candidate, we encourage the board to have a conversation with that person. If the gap is smaller, the risks of reaching outside the company may outweigh the benefits, especially for a healthy, well-run company. Every company has a unique strategy, history and culture. Even a highly skilled outsider might not turn out to be the best fit for the organization's values, way of operating or position in the market — and this is not always obvious in advance.

As a result, we always encourage boards to give their internal candidates every chance to get the appointment unless an outside candidate brings considerably more to the table. If the outsider does, the board must make the important decision of whether to conduct discreet conversations with select externals or whether the internal options are so weak that they want to conduct a broad, engaged search, a process that ideally should begin nine months to a year before the transition.

7 Failing to update the plan

While many of the points in this article discuss suggested steps leading up to a planned transition, succession planning is an equally important fiduciary responsibility of board members when no obvious transition is on the horizon. Moreover, being prepared for unexpected transitions is a major factor separating well-governed companies from poorly governed ones.

Now more than ever, companies and the markets they serve are dynamic. Succession plans and the key specifications for the role that underpin them should be adapted regularly to reflect these changing realities. At a minimum of once a year, and preferably more often, the succession planning committee should evaluate and, if necessary, revise the specifications for the role (or roles for a two-tier board) to ensure they are current. They should also review the progress of internal candidates against their development objectives and revise the objectives, if needed, to reflect the changing qualifications that will be needed for the evolving role.

Well-governed companies also take a longer-term view toward succession. The board's responsibility may not extend to a granular role in the identification and development of roles beyond the CEO role for a single-tier board and beyond the executive committee for a two-tier board. But it should make sure that there is a process in place to develop talent for all the top positions in the company, and that the pay of the CEO and other top executives is linked to their success in developing and retaining talent.

By taking these actions — while avoiding the pitfalls we have described — boards can more effectively prepare their companies for succession over the short term, and help build the bench strength that the company needs for stability and success well into the future.

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5 things board directors should be thinking about

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GUILHERME DALE, *Sao Paulo*
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5 things

The role of the outside or nonexecutive director has been attracting increasing scrutiny in recent years, and there has been no shortage of advice from shareholders, politicians and the media on what board directors of listed companies should be doing with their time. Unfortunately, much of this advice is unhelpful, often betraying a lack of understanding about what is reasonable to expect of directors or how they can put their experience and expertise to greatest effect.

Our view is that most board directors have adapted well to this new era of accountability and are doing a competent job in a difficult environment. They successfully balance their ever-expanding fiduciary duties with their role as advisers, supporting and challenging their senior executive teams. What does it mean for a board to perform well? It depends on what standards the board sets for itself. These days, the majority of boards comply with the law, observe listings requirements and uphold nationally accepted governance principles. They comprise successful, experienced directors who undertake their responsibilities diligently and are proud of the companies they serve. Yet despite this, we suspect that most boards are not fulfilling their potential.

Having worked with boards around the world at close quarters, we have identified a number of characteristics that distinguish exceptional boards from the rest. In this article, we focus on five areas of board activity. Some of these are traditional responsibilities where boards should always be striving to improve their performance; others are emerging as more important concerns than they have been in the past.

1. Effective board leadership

The effective functioning of a board depends on a number of factors, including the mix of knowledge and experience among the directors, the quality of information they receive and their ability to operate as a team. The chairman's role (or that of the lead director on many U.S. boards) is pivotal in managing the group dynamic, playing to the board's strengths and maintaining regular contact with directors between meetings. High-functioning boards rotate meetings around company locations, simultaneously educating directors about different aspects of the business and giving them access to key executives. Directors are invited to attend all committee meetings and are free to ask questions, however difficult. Boards not only evaluate the performance of the CEO, but take the formal assessment of their own work seriously and use the findings to develop — and hold themselves to — objectives for improvement. Transparency and trust prevail.

As businesses reinvent themselves, so should boards. Effective boards ensure that they have the right people at the right time. This is largely the responsibility of the chairman and the nomination or governance committee. Together they play a vital role in defining the board's needs, seeking the appropriate diversity of perspectives, and overseeing a rigorous recruitment process. As an individual director, however, you have a responsibility to ask yourself periodically whether you are still the right person for the board. It takes considerable self-awareness to assess the value of your contribution, to consider your "period of validity" and to be prepared to step down if necessary when the business has moved on.

Boards can get more out of their directors by adopting processes that promote efficiency and good communication, both among directors and with external parties. Ensuring that board papers are timely and thorough and that information is easily accessible to directors between meetings is essential. One criticism leveled at board papers is that they are top-heavy with facts and figures, too backward-looking, and not sufficiently focused on strategic issues. Another way of helping directors give their best to the board is through well-planned induction programs and by offering continual opportunities for directors to increase their understanding of the business and keep abreast of changes to legislation or governance codes. Finally, effective boards place a premium on good communication, whether it be with fellow board directors, key executives or shareholders. This needs to be orchestrated by the CEO and/or chairman, but directors need to insist on the highest possible standards of communication — whether it be presenting compensation decisions to shareholders or feedback from the latest board assessment.

2. Strategy

Progressive boards put their companies at a distinct advantage; nowhere is this more evident than in the way they address strategy, from formation through to execution. The conventional delineation of responsibility is that the executive team develops strategy, the board fine tunes it and then oversees its execution by management, measuring the CEO's performance against a set of agreed-upon objectives. The most common catalyst for this process is an annual strategy day where the CEO, supported by his or her management team, reviews a set of strategic options, assesses competitors' strategy, and makes recommendations. Given that the company's success and shareholder satisfaction are dependent on the board making wise strategic decisions, it is vital that every director be fully engaged. However, for this to be the case they must be absolutely clear about what is expected of them in the strategy discussion and how much leeway exists to question, challenge or throw out proposals.

Great boards consist of independent directors who are "rowing together in the boat." They see the development of strategy as a collective effort between themselves and management, rather than a question of "us versus them." Management generates and shares ideas that stimulate debate among directors who are there to make positive, valuable contributions to strategy development, not just to provide a critique of the ideas they are presented with.

3. Risk vs. initiative

Since the start of the most recent economic crisis, boards have been urgently rethinking their approach to risk oversight. Outside financial services, where risk committees are well established, responsibility for risk still tends to lie with the audit committee, where the majority of time is spent on financial risk. These days, risk needs to be defined in the broadest terms, encompassing not just financial matters, but also areas such as health and safety, the environment, IT security, industrial relations and corporate reputation. Boards should determine whether they have the optimal structure for overseeing risk, including whether there is a clear delineation of risk management responsibilities between the board and the executive. Great boards in-

Key questions directors should be asking

Board Effectiveness

- Does my board have the right governance model?
- How is my board adding value to the company?
- Is the board striking the right balance in its attention to governance and regulatory issues and performance?
- Is the prevailing board atmosphere collegial or tense?
- Is the board getting the most out of its annual assessment?
- What should the board look like in the future to address the changing external environment and evolving strategic priorities?
- Are my skills and experience still the right ones for the board?
- What is the right balance between broad-based business experience and specialist expertise?
- Do we have sufficient information to make wise, informed decisions?
- How do I ensure that I am staying current? Does the board provide the continual education I need?
- Am I happy with the quality of board-level communication, both internally and externally?

Strategy

- What is the board's role in developing and critiquing strategy?
- How much leeway exists to question, challenge or throw out proposals?
- What is the best way to delineate responsibility for developing, discussing, fine tuning and executing strategy?
- What is the right balance between advice and control?
- What is most valuable: knowledge or perspective?

Risk Oversight

- How should the board structure its assessment and supervision of risk?
- What are the roles of the board and management in managing risk?
- Is the board clear about its appetite for risk?
- To what extent do personal considerations affect my attitude to risk?
- Do I know what the organization's risks are? Do we spend time on "what if?" thinking?
- Is the heightened awareness of risk stifling innovation and creativity within the executive team?
- How does the board view reputational risk?

Succession Planning

- Am I confident that the most rigorous succession planning methodology is in place:
  - for the CEO and executive committee?
  - for the chairman?
  - for the rest of the board?
- Do we have contingencies for both planned and emergency succession?
- Do we have a clear line of sight into the executive ranks below the executive committee?
- Am I confident in the tools available to assess potential successors?

Sustainablity

- Are decisions being made in the long-term interests of the enterprise?
- Is the board committed to, and debating, corporate responsibility issues?
- Are corporate social responsibility, sustainability and climate change issues factored into company strategy?
- Are they seen as generating costs rather than benefits?
- Should sustainability be the responsibility of a dedicated board committee?

stitutionalize risk, they don't necessarily police it. They tailor their participation and committee structure to the sensitivity of their business to risk.

For a more in-depth look at the way boards are structuring themselves to better manage risk, see the article *The growing role of the board in risk oversight* on page 33.

The board should review its risk appetite on a regular basis. It is worth directors stepping back to assess the extent to which personal considerations may affect their attitude to risk, since this will have an impact on the degree of latitude available to management to pursue their business objectives. Boards need to be aware that heightened sensitivity to risk may stifle innovation and creativity. These days, risk downside tends to get far more attention than risk upside; many take the view that entrepreneurialism inside large corporations is under threat due to increased risk aversion. A strong and fearless board will acknowledge that risks are inherent in any business that is going to deliver long-term value to its shareholders and, with the right executive team in place, its members will have the confidence and trust to back the CEO when new opportunities arise.

4. Succession

When asked about succession planning, most directors acknowledge its importance but admit that more could be done by their board to establish a rigorous process to identify the next CEO. This is borne out by periodic high-profile emergency succession events that reveal a remarkable lack of preparedness by boards, usually spooking the market and diminishing the share price. On those occasions when companies manage a seamless CEO transition, whether it is planned or an emergency, the reaction is invariably one of surprise that preparations should have been handled so discreetly and effectively.

A great board will make succession planning a regular agenda item. It will start the process as early as possible — even if this makes the incumbent uncomfortable — and will also consider succession for the chairman (where the roles are separated) and the rest of the board. When the lead CEO candidates are internal, boards will also conduct external benchmarking. In Germany, the supervisory board must by law involve itself in succession planning for the entire senior management team. Elsewhere, the best boards take the initiative on succession, usually led by a committee, and ensure they have regular contact with senior executives in all divisions and geographies, requiring the CEO to plan for the succession of his or her senior leadership team. A conscientious director will want to be satisfied that the board has a rigorous succession planning methodology in place providing for both planned and emergency scenarios, and that the board is confident in the tools available to assess potential successors.

For more on succession planning, see the article *Lessons from the boardroom: Seven succession planning missteps boards should avoid* on page 40.

5. Sustainability

Boards of listed companies have an obligation to build and protect long-term shareholder value and to ensure that short-term decisions do not jeopardize the sustainability of the enterprise. In South Africa, the notion of sustainability is woven into the constitution and affects every listed company; it is considered inseparable from strategy and good governance. All forms of capital — financial, human, natural and social — are seen as essential for value creation. Other societies and governance codes are far less explicit about the link between sustainable practices and shareholder value, but evidence is mounting that boards overlook corporate social responsibility at their peril. While this issue will manifest itself in different ways depending on the industry sector, it is worth directors reviewing their board's attitude to corporate social responsibility and wider stakeholder issues and consider whether they require more attention — ignoring both can carry a strong element of risk. The habit that great boards have adopted is to view sustainability in its various forms as coterminous with long-term shareholder value.

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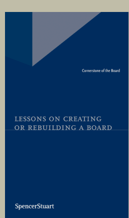

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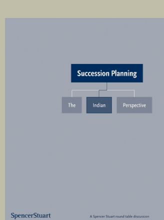
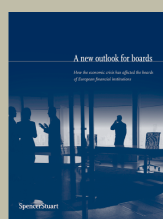
The Benefits of Board Service



Succession Planning: The Indian Perspective



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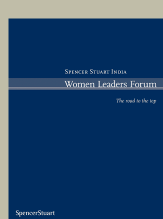

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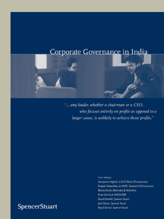

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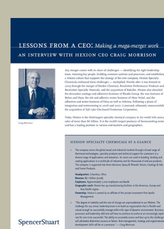

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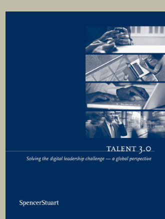

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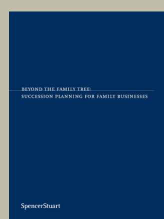

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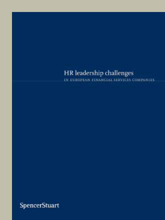

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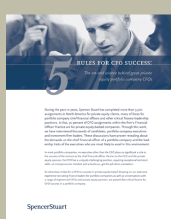

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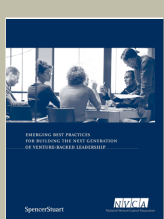

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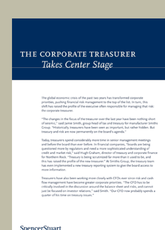
Life Sciences Leadership in Asia Pacific



The Corporate Treasurer Takes Center Stage

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