

WHEN IT IS PAST TIME FOR THE CEO TO LEAVE

PLANS FOR CEO SUCCESSION OFTEN LEAVE OUT DEATH AND DISASTER

BY BRIAN BURTON

CERTAIN STATISTICS INDICATE that up to 36 per cent of private-sector companies lack advance planning for any kind of leadership change, strongly suggesting an even larger number may lack procedures for the unanticipated death, departure or removal of a corporate leader. As in-house counsel, that is not going to be you. Perhaps you've endured an unplanned expulsion of the CEO in a previous role and you've vowed not to relive the experience.

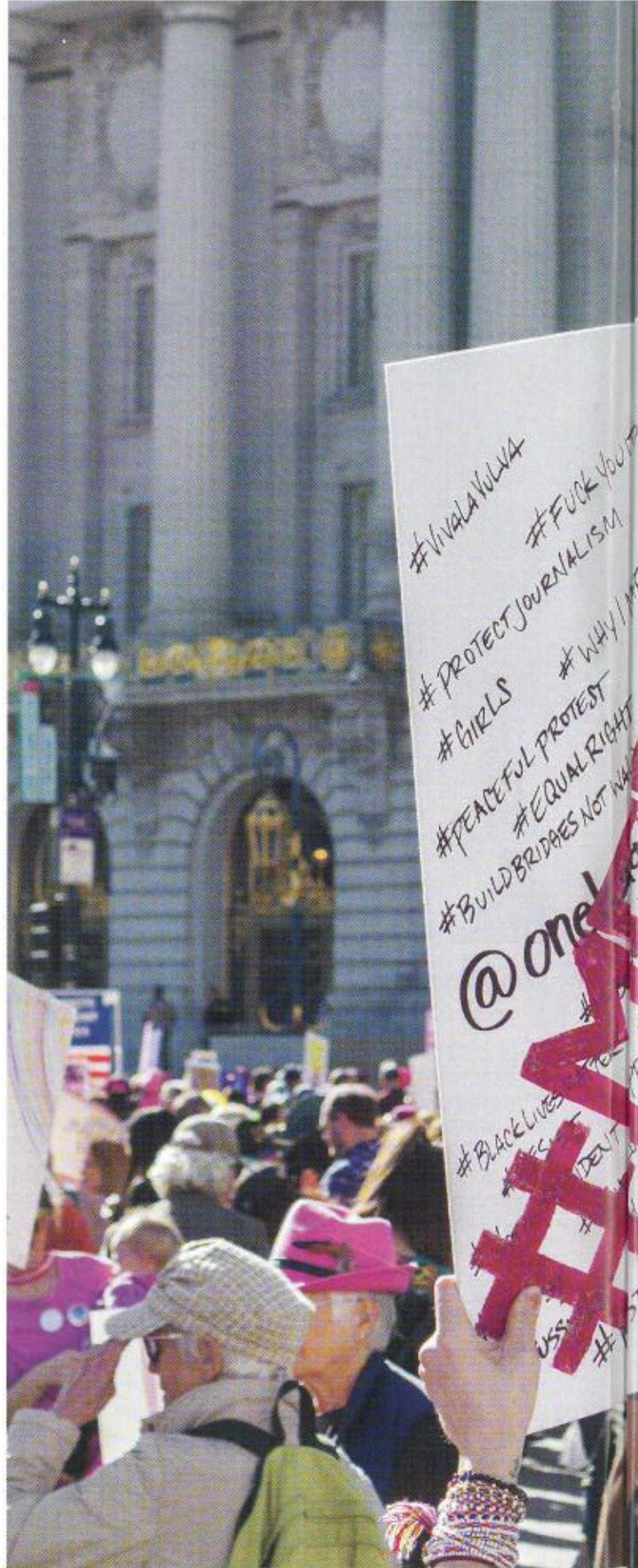
There was a succession plan, of course, the previous time. But it did not anticipate the many scenarios that can go wrong.

DEATH AND DIVORCE

As a newly-minted lawyer and in-house counsel at a telecom company, Shana French had a front-row seat during the removal of the CEO and the subsequent departure of his entire executive team, people with whom she'd built professional relationships. Some two decades later, as a corporate governance specialist with the Toronto office of Sherrard Kuzz LLP, French estimates she's advised nearly 100 client companies on the sudden loss or expulsion of a corporate leader.

"I'm like a (corporate) divorce lawyer," she says. Continuing the analogy, she says Boards of directors need to be careful about the credentials they look for when it comes to finding a successor in the top job. "You need to make sure you're hiring someone who's going to be good marriage material." That is, someone who's in it for the long haul and not just a hot CV. But it's far from the only hurdle ahead of a corporate Board with a sudden vacancy at the top of the house.

She says succession planning at many privately-held companies is typically done as a long-serving CEO approaches retirement. If





SHANA FRENCH
 > SHERRARD KUZZ LLP

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“It’s risk management, like fire or cyber security risk,” he says. “You have fire insurance, you have staff training, fire safety equipment and computer redundancy. Then, if there’s a fire, it should go a lot better than if you didn’t plan for it.” He points to the practice of tabletop exercises around cyber security, in which a corporate leadership team is given a hypothetical cyber security breach and required to devise a complete response. “They’ll fumble around for a bit, but eventually they’ll figure it out.” When everyone is satisfied with the tabletop response, it’s incorporated into the cyber security plan. “You can’t do too much of this.”

Reiter says a similar sense of exigence should drive succession planning, but that’s the exception rather than the rule. “In my experience, although many, many companies recognize the need for it, very few have done it.”

BEST LAID PLANS

French says it’s now rare that she gets called in by a client company after the CEO has been fired. But sometimes it’s not long before. “What would it look like if we fired our CEO?” is the general shape of the question she gets asked in numerous cases.

For the more forward-minded, she says, planning for the untimely loss of a corporate leader should begin by ensuring the Board of Directors has full legal understanding of its authority in the firing and transition stages. Boards can be hamstrung by such questions as how far in advance to give Board members notice of a meeting to remove the CEO, whether the meeting can be conducted by phone or whether they actually have the power within corporate bylaws to fire the CEO, she says. If it’s not

spelled out, it should be. And that should be followed by similar authorities for all the necessary and potentially necessary steps until a new leader is instated, including appointing an interim leader from amongst the executive Board members, having the Board chair fill in, retaining an interim leader on contract, hiring a search firm and appointing special committees to oversee succession and business-as-usual operations during the interregnum. The check list is long and involved.

“I literally have a binder, so that it’s all laid out,” French says. Muddling through, she promises, will not be an ennobling experience.

“Being prepared and proactive is key,” says Lisa Talbot, a governance expert with Torys LLP in Toronto. “The necessity to remove a CEO on short notice can be a crisis (and) one of the fundamental responsibilities of a Board is to manage risk and prepare for crises.” A new CEO’s employment agreement should include grounds for removal, entitlements upon termination without cause and circumstances giving just cause for termination without notice or severance. Policies should address proper procedure for the investigation of allegations of misconduct and Boards should consider an outside audit of their policies and procedures.

“Boards would be well-advised to have a plan in place (for) the removal of a CEO on short notice,” Talbot says.

INTERNAL ISSUES

As primary legal advisor to both the Board and the CEO, in-house counsel an unenviable position when it comes time to toss the boss. The GC likely works closely with the chief executive on a daily basis and this

often develops into a close professional and personal relationship. While the GC owes his or her first duty to the company, French says, the Board may still decide it’s best for all concerned if key aspects of a CEO firing are left to outside counsel.

Reiter says Boards bear primary responsibility for a succession plan that contemplates removal of the CEO. But if the Board doesn’t address the issue, “the GC should be calling it to their attention.”

If a time comes when the Board is considering CEO removal without cause, perhaps because of corporate performance issues, French says, they may wish to consult outside counsel and leave the GC out of it to avoid souring the trusted-advisor relationship in the event they ultimately decide to keep the CEO.

In the event that the CEO is about to be fired for nefarious activities, Reiter says, the GC very well may be the one bringing the case to the Board. “I’ve seen a range of GC involvement from nothing to leader of the pack,” he says.

But, no matter the circumstances, Reiter says, “the GC shouldn’t be the one to walk in and say, ‘I want you to know you’re fired.’” After all, the GC is a subordinate of the CEO. Firing should be the role of the Board chair, typically accompanied by outside counsel. It’s just more respectful and leads to fewer combative reactions from the deposed executive, he says.

“What doesn’t work,” French cautions, “is sending in the guy on the Board who has a relationship with the CEO.” She is sometimes retained specifically to fire the CEO and she says it should always be done on the basis of thorough legal advice. “It goes wrong when there’s too much cutting of your own hair.”

However it’s handled, it should never be allowed to devolve into a negotiation, Reiter says.

“The decision is taken, it’s not a discussion,” he says. The Board representatives should present terms of dismissal that have been thoroughly worked out in advance. Depending on the situation, the Board may decide to be generous or tough. “You need to have thought through, is this for cause, or not?” he says.

TRUE FACTS

Communication is vital whenever a leader

is unexpectedly lost, Reiter says. Governance specialists agree it's crucial to instill confidence in investors, bankers and other suppliers, employees and customers.

"This whole communications piece is very important," he says. "You have to decide who to inform and what to communicate" and that's much easier to do as an advance-planning exercise than when the Board is besieged by crisis — possibly triggered by scandal. French says her binder includes two drafts of initial press releases, one for the case of the mutually-agreed departure and one for a unilateral Board initiative.

Reiter says communications rule number one is that, where scandal is concerned, transparency will prevail. "In today's world, everything will come out. Somebody has a video of everything and the notion that

future endeavours, well, that's not really authentic," she observes. It invites rumour to take over from fact, creating distractions at a difficult time and giving the company a credibility problem to add to its woes.

"For purposes of setting standards, the company may want to state the cause," she says. "But if you terminate for cause, is that something you want to litigate?" Termination for cause gives the former CEO strong motivations for litigation, including loss of severance pay and hurt pride, and litigation will ensure that all the ugly details of the situation become public through court filings. Between full disclosure and fudging the facts, she says, there's likely room for external counsel to convince the departing CEO that both sides interests will be best served by a dignified parting — including a press release that makes the

an interim leader — the very situation the succession plan was intended to avoid.

When she was in-house counsel, French recalls, the Board had taken all the necessary steps to identify and approve a successor well before the CEO was deposed.

"That made the transition more successful than it otherwise might have been," she says. The successor appeared at the employee meeting where the transition was announced and became the focus of employee questions, rather than the departing leader.

Where an internal successor is neither designated nor obvious, Reiter says, naming an interim leader buys time for the Board to consider its options while posing no threat to internal candidates.

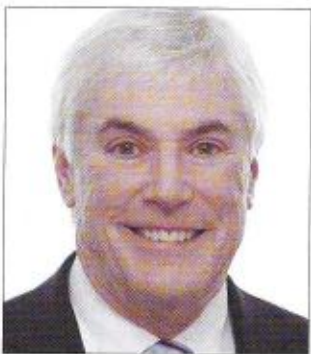
WHEN THE CEO WAS A FOUNDER

Harpreet Sidhu says Pethealth Inc. is a very different company today than it was when she became general counsel, soon after admission to the bar six years ago. Today the multinational pet insurance provider is a subsidiary of a larger company with solid governance procedures. Then it was a rapidly growing, publicly-traded concern under the direction of a mercurial founder and CEO.

Between 2012 and 2014, the founder and leader left "not once, but twice," Sidhu says.

In the first instance, a phone call informed the founder that his pre-teen daughter had suddenly died. "He just literally ran out the door," she recalls. "Half the executive didn't even know he was gone." He took a six-month leave and a company accustomed to rule by founder fiat was left rudderless, she says. No one else had relationships with major suppliers and customers and executives contested authority for key decisions. "They were going through Board minutes to figure out what he would do if he were here."

Then, in 2014, the Board voted to remove the founder and appoint a new CEO. The second time, she says, things went a bit better but it was still a rocky transition. Since then, the entire executive team has been changed out, with the exception of Sidhu, and the business is on a solid foundation. Transition has been a lengthy process but she says she expects the Board and the new CEO will soon be in a position to consider detailed succession planning. ☺



BARRY REITER
 > BENNETT JONES LLP

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"It's short-sighted and pretty well universally wrong to pretend the facts aren't what they are," he says. "If you're firing for some scandalous cause, you say, 'We've learned this, and we don't stand for this.' Otherwise, your employees look at the company and say, 'Is this who we really are?'" At which point, he says, the most valuable talent begins to bleed away. And customers are far more mobile than employees.

In the public domain, Reiter says, "it's not the problem — it's how you deal with it that matters."

Just as companies bring in outside counsel to advise on sudden transitions, French says, they should consider whether they need a crisis communications advisor.

"Announcing the CEO is leaving, effective tomorrow, and wishing him well in

company policy clear.

Clear communications from the Board will also be important in empowering managers at all levels to continue business as usual and maintain progress on major projects.

WHO'S NEXT

Reiter says, if a succession plan is conceived well in advance and includes the name of a designated successor, that fact needs to be very tightly held by a small committee of the Board until a transition is under way. "If I name Mary, over there, as successor and that gets out ... the other three people who thought they should be successor will have their resumés out on the street pretty quickly," he says. Then, if Mary leaves the company before a sudden CEO loss, the Board may well be left to choose between its fifth-in-line-of-succession or installing