

Choosing a new CEO: This board got it right

There were three strong internal candidates, each with champions on the board. Only a rigorous step-by-step evaluation process resolved the selection dilemma to confirm the best person for the job. **BY ROBERT C. MUSCHEWSKE**

BOARD MEMBERS know that CEO selection can seem like a crap shoot. It can be difficult to predict with confidence who will be successful in the position, given the vagaries of human nature, the daunting and unknown challenges that CEOs face, and the awareness that the position is unlike any other job in the organization. However, there is a way to increase the odds of success. The entire board can engage in a thoughtful and fact-driven process, described in this article, that will lead them to a selection decision.

Recently, a \$20 billion global manufacturer faced the following situation:

- The company was nearing completion of a successful turnaround in financial performance.
- Their CEO announced to the board that he was planning to step down in a year.
- The board wanted to select an internal candidate rather than go to the outside.
- The company had three talented internal candidates, but none had experience in managing a P&L.

- The board respected all three internal candidates, but they were divided roughly into thirds, each group favoring a different candidate.

How did the board resolve this dilemma and reach consensus on the candi-

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date best equipped to lead the company?

Development of a CEO competency profile

The board's first step was to bring in an outside consultant who was an industrial and organizational (I/O) psychologist specializing in CEO succession planning. Together, they began "drilling down" to identify the challenges facing the next CEO of the company, and the skill set that would be essential in tackling those challenges.

This exercise yielded a list of eight critical leadership competencies needed in the next CEO (see Exhibit 1). Based on the presumption that the vision and key strategies required to achieve that vision had been set and that the principal challenge would be to implement those strategies, the lead competency was defined as follows:

- **Passion for Operational Excellence.** Driven by a sense of urgency and desire to achieve world-class performance on all relevant customer service, operational, and financial metrics. Provide focus, make the tough decisions, and align the organization to achieve this objective.

Acknowledging that the environment could likely change, the board knew that it needed a leader who possessed not only operational skills, but the capacity to think ahead and change the course of the company as needed. The second-highest competency on the list was:

- **Strategic Perspective.** Stay abreast of broad technological, social, governmental, economic, and industry trends. Develop and implement proactive, innovative, and pragmatic strategies to ensure that the company achieves performance objectives.



Behavioral assessment of candidates

The next step in the process was for the board to learn more about the skill sets of each candidate. In the past decade, more and more boards of directors have realized that they alone are accountable for making the selection decision. Although they look to the current CEO for input on capabilities of the candidates, at the end of the day they need to know enough about the candidates to make an informed decision. They come to grips with the fact that they often do not know as much as they need to about the skill sets of internal candidates to make a thoughtful decision. Meeting and speaking with candidates at board dinners or seeing them make practiced presentations before the board does not provide the insights required to make significant judgments about a candidate's broad range of leadership skills.

To address this concern, the board enlisted the services of a consulting firm with I/O psychology expertise to conduct behavioral assessments of the three internal candidates. The assessments comprised a "two days in the life" process that placed the CEO candidates in realistic simulations designed to assess how they would perform in situations faced by CEOs. (See Exhibit 2 for the assessment challenges.)

Constructed around a fictitious company, the simulations involved the preparation of a vision and strategy white paper for the company, a meeting with a key member of the executive team, a video

presentation to the worldwide employees of the company, a "live" interview with a TV analyst, and a meeting with two members of the board of directors, including the chairman. When combined with more traditional assessment tools such as personality inventories, cognitive ability testing, and in-depth interviews, the assessment process measured the extent to which each candidate possessed skills critical to successful performance at the CEO level.

In addition, results of the assessment process enabled the consultant to draw conclusions concerning the eight competencies identified by the board as critical leadership competencies for the next CEO.

Performance summaries for each candidate in the assessment process were shared with the members of the board and served to frame questions for the board concerning the capability of each candidate. Was Candidate 1, competent and experienced as he was, too much of a "staff guy"? Did he really have the leadership chops to serve effectively as CEO? Candidate 2 was extraordinarily bright and seemed to be a quick study who could rapidly learn what he would need to do as CEO. Could he learn fast enough? Candidate 3 was very

Candidate 3's high level of self-confidence may have morphed into more than a touch of arrogance.

EXHIBIT 1 Critical CEO Leadership Competencies

The critical set of competencies required for CEO leadership in addressing the strategic challenges facing the company are as follows:

Passion for Operational Excellence: Driven by a sense of urgency and desire to achieve world-class performance on all relevant customer service, operational, and financial metrics. Provide focus, make the tough decisions, and align the organization to achieve this objective.

Strategic Perspective: Stay abreast of broad technological, social, governmental, economic, and industry trends. Develop and implement proactive, innovative, and pragmatic strategies to ensure that the company continues to achieve performance objectives.

Seasoned Judgment: Possess the balance, objectivity, and wisdom needed to make key human and business decisions.

Inspirational Leadership: Demonstrate an approach to leadership that engages and mobilizes all parts of the company in a unified pursuit of its mission, vision, values, strategic objectives, and growth in shareholder value.

Personal Integrity: Possess unquestioned personal integrity and engender trust by maintaining a core set of ethical values and bringing them to life in all interactions with stakeholders.

Financial Acumen: Possess an in-depth understanding of balance sheet and income statement financial issues and know how to use financial information to shape, drive, and

monitor the effectiveness of organizational strategies.

Team Builder: Attract, develop, motivate, and retain highly talented individuals to the leadership team and deploy them in a manner that will optimize achievement of short- and long-term strategic objectives. Foster the development and implementation of human capital and organizational strategies that result in high levels of talent and performance throughout the organization.

Personal Impact and Savvy: Possess the personal presence, stature, and interpersonal skill required to communicate effectively with the internal and external stakeholders of a public company, the investment community, and the board of directors.

— Robert C. Muschewske

confident and performed well in the assessment process, but he was very disappointed that he had not received the highest possible score on each aspect of the assessment process. He became very defensive when he received feedback on his performance and gave indications that his high level of self-confidence may have morphed into more than a touch of arrogance.

The assessment results were very helpful to board members, who began to understand the strengths and development needs of each candidate. They used the results as an additional source of information to complement their own impressions and discussions with each candidate. As one board member later commented, “It was one data point, but it was a very useful one.”

Peer and direct report rating of candidate leadership capabilities

Board members also realized — as do many boards — that they lacked an important piece of information; i.e., the manner in which the actual leadership capabilities of the candidates were perceived by their peers and direct reports. To address this concern, a multi-rater feedback instrument was distributed to the peers and direct reports of each candidate. The results were consistent with the findings of the assessment process. Candidate 1 (the “staff” guy) was seen as a highly capable individual in his area of functional expertise who had pleasant interpersonal skills; he was not seen as a high-impact strategic leader with the skill to drive results. Candidate 2 (the “bright” guy) was

EXHIBIT 2 Key Strategic Challenges for the Assessment

The following strategic challenges facing the company were developing following in-depth interviews with members of the board of directors and selected members of the executive leadership team.

Challenge 1: Achieve Operational and Financial Excellence

The fundamental challenge facing the next CEO will be to provide the leadership required to take the company to the next level in achieving its mission, stated as follows: *The company aspires to industry leadership in both market share and financial performance through world-class service delivery and operations.*

Significant progress in achieving this Mission has been made during the past four years. All agree that the company is no longer in financial difficulty. It has the potential to be a great company, but much work remains to be done in the following areas:

1. Become the lowest cost service provider and manufacturer. Focused attention needs to be directed in the following areas to achieve this objective:
 - Maximize shared practices and “best in class” approaches.
 - Establish and implement a comprehensive productivity management system that addresses all critical metrics and promotes operational discipline.
 - Institute a consistent focus and follow up

on cost reduction and control initiatives.

The company understands that its costs are higher than its key competitors, and that its centralized organizational model differs from the more decentralized structure of competitors. The rationale that the company’s current cost structure and organizational model is an investment ensuring future operational efficiency and effectiveness needs to be continually examined and tested.

2. Identify additional opportunities for growth. Pursue value-based tuck-in acquisitions in the core business.
3. Employ rigorous capital allocation discipline. The company needs to:
 - Identify underperforming assets and either initiate improvement programs or dispose of the asset.
 - Direct capital allocation toward markets with the highest ROI.
 - Stay the course with board-approved capital allocation priorities.
4. Implement state-of-the-art employee recruitment, selection, development, and training programs. The industry has not attracted A-level talent. Continued growth and profitability of the business will require that talent be upgraded at all levels, with particular focus on the management levels of district manager and above.

5. Continue to strengthen relationships with regulatory and other governmental agencies. The business of the company intersects with many governmental jurisdiction policies and practices. The company needs to maintain a proactive and constructive leadership role in dealing with these issues.

6. Continue to build relationships with all stakeholders: customers, host communities, and shareholders. The company needs to:

- Differentiate itself in the marketplace.
- Reassure all stakeholders that it adheres to the highest standards of business practices.
- Convince shareholders that it is striving to achieve its market value goal to be in the top quarter of S&P companies over \$30 billion in market value.

Challenge 2: Anticipate and Develop Proactive Strategies in Response to Changes in the Industry

Although the fundamental challenge is to achieve world-class levels of operational excellence, it is also critically important to maintain a strategic perspective. The crystal ball is not clear concerning how the industry will change, but all are convinced that change of some undetermined scope and magnitude will take place in the next decade. The company needs to anticipate those changes and develop proactive strategies to address them.

— Robert C. Muschewske

seen as having performed well in two high-level staff positions, having superb interpersonal skills, being “smart as hell,” and having the potential to be CEO, despite the fact he had never managed a P&L. Candidate 3 (the very “self-confident” guy) was also seen as exceptionally capable in his staff role and very bright, but it was noted that he could be too tough on his people and had a tendency to be a micromanager.

Vision and strategy white papers

At this point in the process, board members were deepening their perceptions of each candidate. Some were drawing tentative conclusions concerning a preferred candidate. Some were crafting questions they wanted to pursue as they got to know the candidates better. However, it was still an open question as to who was the best candidate, and they were eager to take the next step in the process.

Next, each candidate prepared a three- to five-page vision and strategy white paper outlining where they would take the company if they were the CEO. Board members wanted to know their vision for the future of the company and what key strategies they would implement to achieve that vision. Each paper was distinctly different. One was tactical in tone. The second had more of an operational focus, and the third was much more strategic. It should be noted that not only did the papers provide insight into the thinking of each candidate, they served as a superb educational tool for board members. Each paper contained rich and unique views of how the company could evolve in serving the needs of its customers and enhance shareholder value. The diversity of thought broadened board members’ views of both the opportunities and challenges facing the company, and it exceeded strategic planning discussions that occurred in regular board meetings.

The papers served as the basis for one-on-one interviews between candidates and members of the board. As one board member commented, “This is where all of the data came together.” The behavioral assessment results, the multi-rater information, the career history, the performance data, prior perceptions ... all came together as they discussed the vision and strategy white papers with each candidate. Each director began to crystallize a view of who would best be able to serve as the next CEO.

Making the final selection decision

The board members met as a group with the consultant to discuss their views of the three candidates and to make a selection decision. It was a lengthy and thoughtful discussion focused on the challenges facing the company and the strengths and development needs of each candidate. As the discussion progressed, it became clear that the board members were reaching consensus, and eventually unanimity, on one candidate. Reference was made throughout the discussion to the skill sets measured in the assessment process and the eight critical leadership competencies the board had identified at the beginning of the process.

The board chose the candidate who convinced them that he had the highest level of *Passion for Operational Excellence*, despite the fact that he did not have direct P&L experience in leading an organization to achieve that objective. Perhaps the most critical factor in their decision, however, was their view on who possessed the number two competency, *Strategic Perspective*, at the highest level. Achieving operational excellence was critical in the near to medium term, but as experienced leaders in their own right, all board members knew that making significant changes in strategic direction is always a possibility for an organization. Selecting a leader who could “see around corners” and set the organization on a new course when needed was imperative.

The right choice

The new CEO has been in the position for a little over three years and the board is convinced that it made the right choice. Financial performance has improved dramatically. Their competitive position in the marketplace has moved to number one. Further expansion of the business in new markets is moving close to full implementation.

As the board looked back over the process it used to make the selection decision, one member commented, “Intellectually, this was an excellent process, as good as it gets. The best I have seen in my long experience working on boards.” ■

Boards often do not know as much as they need to about the skill sets of internal candidates.

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