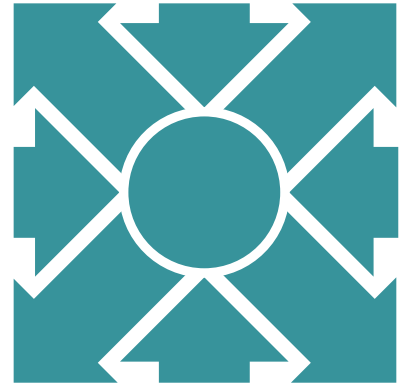


SEARCH



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Corporate Governance and Transition: Using governance systems as transition tool

Over the past 10 years governance at the head of companies has become a very hot topic in which search firms growingly play a key part.

It is now fully accepted that good governance plays a major role in optimizing the management and performance of a company. The definition of responsibilities between top managers and a clearer division of authority and decision-making between the Board and Senior Executives is also better managed.

In this context the contribution looked for from Boards of Directors, executive members and Independent Directors alike, has been very significantly increased. Key decisions, including major nominations and hires, determining the remuneration of senior officers, approving the strategy of the company are made at board level by specific committees.

The days of Board appointments being made through the old boys' network are over as the demands made upon board members in terms of implication, accountability to shareholders and personal responsibility have become much higher. The levels of diversity, professional qualification and added value expected from Board members have grown significantly. It is now commonplace for there to be a number of independent Directors appointed with very specific skills, experience and professional qualifications. As a consequence, the recruitment process for directors has been very much refined, often involving professional search firms and a much more rigorous assessment and selection process than was previously the case.

For any top level position the transition between two incumbents carries risks which need to be managed extremely effectively and carefully prepared beforehand – even more so when changing the CEO of a company which is highly unsettling for shareholders, clients and employees alike. Partnering with the right Executive Search firm can contribute significantly to reducing uncertainty and risks by ensuring the client has access to the best talent in the market when no suitable candidates are available internally. In the longer term a good Search partner has a key role to play in helping a client to build a strong internal talent pool of high-potentials from which to recruit the future business leadership.

In that context, in addition to guaranteeing better and more independent decision-making and management, governance systems and their fine-tuning is growingly used as a transition tool at the head of companies.

This issue of Search looks at how governance systems can facilitate the process of transition at the head of companies. Charles-Henri Besseyre des Horts looks at the theory behind transition and governance while Jean-Cyril Spinetta, Chairman of the Board of Air France-KLM and Chairman of the Supervisory Board of Areva, will share his hands-on experience of setting up a smooth change at the head of major groups.

Julien Rozet

President of the Management Board
Alexander Hughes

Governance in Transition Periods

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CHARLES-HENRI BESSEYRE DES HORTS

ARTICLE

These changes raise some key concerns about the distribution of power between the board – as supervisory body – led by the Chairman and the senior management team – as executive body – led by the CEO. One of the most important questions indeed is the combination or dissociation of the functions of Chairman and CEO. Moreover, the arrival of a new CEO (and/or Chairman) is likely to deeply influence changes in the strategy and the structure of the firm right after the arrival since the first 100 days are viewed as critical for the success of the transition². These two main issues will be addressed in the remaining of this article.

The 1992 Cadbury report in UK and more recently a number of other reports and legislative texts in various countries have underlined the necessity for listed firms to clarify the roles of their governance structures (the board and the senior management team) and the key people (chairman and CEO) leading these structures. The situation is, by far, not homogenous between these countries because of different

cultural traditions and regulatory environments. Among the countries advocating a clear separation between governance structures, Germany has one of the toughest regulation requesting companies over 2,000 employees to create two separate councils: the "Management Board" (in charge of managing the company) and the "Supervisory Board" (in charge of controlling the managers). This legislation was first introduced in 1945 and modified in 1966 following the tradition inaugurated by Bismarck in ... 1870 who imposed a control of large steel makers firms by the Prussian state in the Supervisory Boards³.

France has adopted a similar position with the "Nouvelles Régulations Economiques" (NRE) 2002 law clarifying the roles of the governance structures in favour of a clear separation of these roles:

the controlling role, for instance, of the "conseil d'administration" (e.g. the Board) has been strongly reinforced as well as the strategic role to provide inputs regarding the definition of the firm's business orientations⁴.

Beyond the governance structures, relative positions and roles of the key people - namely the Chairman and the CEO - are very significant about the evolution of governance rules. With the publication in 1992 of the Cadbury report, United Kingdom has been one of the country that has been strongly advocating for a clear separation of the roles between the Chairman and the CEO resulting in the fact that, today, 95% of the FTSE 100 companies have an independent Chairman⁵.

Similarly, other countries like Switzerland emphasize the need to separate the two functions of ...

¹ Bayart, B. : "Plus du tiers des groupes du CAC 40 ont changé de gouvernance", 30 nov 2009 (www.lefigaro.fr)

² Bolmeijer, M. : "CEO transitions : planning your first 100 days", *Leader to Leader*, Winter 2007, 50-55.

³ Gomez P-Y. : "La gouvernance la plus libérale est française", *Le Monde*, 3 nov 2009.

⁴ Godard L. Schatt A. : "Faut-il limiter les cumuls des fonctions dans les conseils d'administration ? le cas Français", *Direction et Gestion*, n° 213, mai-juin 2005, 61-72.

⁵ Pozen R. : "Before you split that CEO/Chair...", *Harvard Business Review*, April 2006, 26-28.

... Chairman and CEO: over 80% of Swiss companies indeed split the two roles⁶. Other countries like the USA have recently experienced remarkable changes in the

distribution of roles between the Chairman and the CEO as reported in table below when considering that 70% companies had, in 2003, a combined CEO-Chairman⁷:

Status	Percentage
Chairman and CEO are combined	26%
Chairman is an independent outsider	6%
Chairman and CEO are separated but Chairman is an insider/employee or an affiliated outsider	22%
There is no disclosure of the separation of CEO and Chairman positions	18%

Prevalence of board leadership structures at S&P 1500 companies (August 2009)

The case of France is interesting because of the aforementioned 2002 NRE law requiring companies to split the roles of Chairman and CEO: a recent 2009 study conducted by the audit firm Ernst & Young shows that more than 50% of the CAC 40 companies have separated the two roles and, moreover, that 25% of the interviewed panel (281 listed French companies including CAC 40 companies) have a dual structure: "Directoire (Management Board)" and "Conseil de Surveillance (Supervisory Board)"⁸.

These numbers show a sharp increase of the dissociation of the two roles from the situation experienced by French companies during the late 1990s where about 75% of the firms had a combined CEO-Chairman. But these results should be taken with caution since the most recent changes in 2009 indicate a revival of the "combination" solution as exemplified by the case of the insurance leading company AXA where Henri de Castries has become Chairman since October 2009 combined with the role of CEO he already had for ten years!

To conclude on this issue of combination and dissociation of governance structures and key people, it seems very difficult to

assess the real impact of any of the two solutions on corporate performance. Studies conducted in the USA, UK, France, Switzerland or Spain do not demonstrate statistically significant differences between combined or dissociated roles of Chairman and CEO⁹.

The decision to adopt one or the other solution (combination vs. dissociation) is likely to be more founded on cultural, regulatory, and business reasons than on ethical reasons. But, whatever the choice is, the transition to the new situation as represented by the change of the CEO should be very carefully managed.

Beyond the governance combination and dissociation issue, the change of a CEO – particularly if he or she combines the roles of CEO or Chairman – often represents a key challenge for the firms such as in the case if the French pharmaceuticals leader, Sanofi-Aventis, that witnes-

sed the arrival of a new CEO in September 2008 who replaced the previous CEO who had stayed in his position for only 20 months!

To support this example, the average CEO tenure has been cut by half during the last decade in US firms (6 years vs. 12 years)¹⁰. Therefore, in the growing number of CEO changes situations, and in order to achieve a successful transition between CEOs, a recent Harvard Business Review article¹¹ suggests a number of practical advices for the departing CEOs such as the following ones as examples:

Yield the stage: let your successor be the public persona of the enterprise

Leave your ego behind: you are no longer obliged to comment on everything

Take some heat: be willing to accept responsibility for the challenges your successor faces

Set a time to go: agree on a specific timetable for your departure and stick to it.

Conversely, the incoming new CEO is facing some other important challenges to adjust to his or her new role. Most studies demonstrate that the first three months of a new CEO are critical for the success of the transition. The famous "100 Days plan" has become a standard high-impact transition tool for new CEOs.

As suggested by an experienced coach in CEO transitions¹², the new CEO should follow a roadmap – the adapted 100 Days Plan – that consists of managing the transition ...

⁶ Schmid M.M, Zimmermann, H. : "Leadership structure and corporate governance in Switzerland"

⁷ Jaeger J. : "Considering the split between the Board and the CEO", Compliance Week, nov 2009, 58-59.

⁸ Ernst & Young : "Panorama des pratiques de gouvernance des sociétés cotées françaises", septembre 2009, 40p. <http://www.ey.com/Publication>

⁹ Pozen R., Harvard Business Review, 2006, op.cit

¹⁰ Siverstone Y, Lawson N. & Mindrum C. : "Learning's Place during CEO Transitions", Chief Learning Officer, September 2007, 24-28.

¹¹ Friel T. & Duboff R. : "The last act of a great CEO", Harvard Business Review, January 2009, 82-89

¹² Bolmeijer, M. Leader to Leader, Winter 2007, op. cit.

Charles-Henri Besseyre des Horts

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He is teaching in several Groupe HEC's programs and has been and is actively involved in a number of international training and consulting (in the USA, Canada, China, Australia...). His research interests focus on the relationships between human resources management and business strategy, the international HR strategies in multinational companies and the development of innovation processes within organizations.

He has published several books one of which ("*Vers une gestion stratégique des ressources humaines*" "towards a strategic human resources management") received the 1988 award for the best socio-economic management books. Professor Besseyre des Horts has also published a variety of articles both in academic and professional journals.

- through several phases: a negotiation phase, a honeymoon phase, a political consolidation phase and an implementing change phase.

Some of the items in the 100 Days plan will include:

- > Learning about the organisation and the business context
- > Consolidating the political power base (with the Board and senior team)
- > Setting expectations with a new strategic agenda
- > Launching a change effort such as reorganisation and culture shift
- > Communicating to and mobilising the troops
- > Etc...

But, what is most important for the new CEO is to build his (her) own 100 Days plan preferably with some help, if possible, of the previous CEO as suggested in the aforementioned Harvard Business Review article.

To sum up, it is possible to stress the importance of some key decisions you may take to improve governance in transition periods in your own organisation:

- 1) choose the appropriate governance format: combination or dissociation
- 2) if dissociation has been selected, decide whether you do so through the separation of governance structures ("Management Board" and "Supervisory Board") or through the split of roles CEO/Chairman, and
- 3) facilitate the dialogue between the departing and incoming CEOs (or Chairman) in order to capitalize on each other's experience.

As demonstrated in the famous simulation "Prisoners' dilemma", a win-win attitude is far more productive in tense situations, such as transition periods, than any other attitude (win-lose or lose-lose). This article has been an attempt to develop such a win-win attitude. ■

Our third annual global partner's meeting



In May, all countries and region heads of Alexander Hughes and our two partners firms in the Americas and Asia gathered in Hong Kong for our annual Global Partners Meeting. It was the occasion to exchange on cultural aspects of different regions covered and communicate on our common tools and strengths.

In conjunction with this meeting, Consultants have met more than 25 international companies not only in Hong Kong, but also in China, Japan, South Korea and Taiwan to showcase our global capabilities.

Alexander Hughes, along with Nosal Partners in the Americas and SES in Asia, founded a unique three-firm global partnership serving clients globally through 56 offices in 40 countries employing 160 Consultants and over 300 people.

Jean-Cyril Spinetta

Chairman of the Board of AIR FRANCE-KLM
and AIR FRANCE, Chairman of the Supervisory
Board of AREVA

TO START THE INTERVIEW, WE WOULD LIKE TO KNOW YOUR PERCEPTION OF CORPORATE GOVERNANCE AS FAR AS THE CHAIRMAN AND CEO ROLES ARE CONCERNED?

Corporate governance is indeed a critical issue for most companies. Curiously in a rather rigid country like France, the regulation "NRE" New Economic Regulations, that was passed in 2001, has introduced one of the most flexible legislation among the major countries as far as corporate governance is concerned: companies may choose between the combination or dissociation of the Chairman and CEO roles with the possibility for the Board to change the governance format at anytime depending upon the context. Lafarge or Axa are examples of major French companies where dissociation was first chosen before recent decisions of recombining the two roles.

This situation cannot exist in the United Kingdom where the dissociation between the two roles has been implemented in all companies following the recommendations of the famous Cadbury report in 1992. A similar situation prevails in Germany and the Netherlands where dissociation is the rule. On the contrary, the combination of the two roles is the most common situation experienced by US companies.



JEAN-CYRIL SPINETTA

WHAT ARE THE CONSEQUENCES OF THE GOVERNANCE STRUCTURES' CHOICES ON CEO TRANSITIONS?

As I mentioned earlier, the law in France or other countries, where the Chairman and CEO roles are separate, has dramatically increased flexibility in governance structures and certainly facilitated the CEO transitions: the outgoing leader (often combining the roles of Chairman and CEO) may easily keep the Chairman role while the new incoming leader can take the active role of CEO as permitted by the dissociation situation.

The case of Sanofi-Aventis is an example of this approach where the dissociation has been chosen to allow a smooth transition between the previous CEO, JF Dehecq, and his successors. Thus, the dissociation of the two roles may be viewed as a transition tool between leaders (past and present). But this situation is not the reality everywhere: in the United Kingdom, for example, where the Chairman cannot be the previous CEO.

ARE THESE TRANSITIONS ALWAYS SMOOTH? DO YOU HAVE ANY ADVICE?

In general, these transitions between CEOs occur without any major problem but there are situations where some disagreements and conflicts may happen largely because the previous CEO does not want to really abandon an active role. One advice I can give is to control the emotional dimension of the transition. From this standpoint, the British managers control this emotional dimension better than in a Latin environment. The case of Unilever is interesting in the transition that occurred few years ago: when the compensation of the Chairman (the ex-CEO) was discussed, it was decided that the amount should not compensate for more than one-third of the time (about 80 days a year).

In this context, the main role of the Chairman is to make sure that the Board is able to evaluate and influence the strategic objectives and actions taken by the CEO and the management team. I personally think that this rule of one-third of the time is a wise one. As a consequence, the same person may have more than one Chairman position as demonstrated by my own example at Air France and Areva or the German case of the Chairman of Siemens who is also holding the Chairman position of Thyssen group. ●●●

... DO YOU HAVE FURTHER IDEAS TO FACILITATE THE TRANSITION BETWEEN LEADERS?

One important idea is to keep the disagreements secret, if they exist, between the two leaders. They have to work out some solutions before any issue becomes public. One symbolic action of the outgoing CEO – becoming the Chairman – I would recommend is to move his (her) office to another location in order to clarify the roles as I did myself in Air France where I moved to a Paris office. Again, I want to point out that the responsibilities of the Chairman are clear and, according to the law, there should not be any overlap with the CEO's responsibilities: management of the board activities, leadership of committees (nominations, compensations...), concealed influence role with various internal and external stakeholders, and representation role like, for example, representing the company at the European Union in Brussels.

Regarding specifically the business strategy proposed by the management, the role of the board, under the leadership of the Chairman, is to approve (or sometimes disapprove) it.

TO CONCLUDE THIS INTERVIEW, WHAT FINAL SUGGESTIONS COULD YOU GIVE TO OUR READERS TO IMPROVE THEIR CORPORATE GOVERNANCE STRUCTURES AND PROCESSES?

I do think that, in most of the cases, corporate governance is fine. However, I am more in favour of dissociation with an active role of the Board as suggested in the "NRE" law. The functioning of the Board can be improved by the nomination of directors. Regarding the case of

directors, I do think that we should have more of them – representing the workforce's interests – in our Boards where important decisions are taken. Human capital issues are more and more important, especially in services industries, like airlines such as Air France-KLM, where the engagement of personnel is critical for the business success. But the role of director, elected by the personnel, is not easy since confidentiality must be respected by this individual who also is an employee who may be impacted by the board and management decisions.

A final comment is concerning the time limit of the corporate governance structure: there is no rule, the collaboration between the Chairman and the CEO may last a rather long time as demonstrated today in the case BNP Paribas or Axa where Mr Bebear, the Chairman, recently decided to leave the leadership to the CEO. The quality of the relationship between the two leaders is the key determining factor in the success of the corporate governance structures in these two companies. ■

[BIOGRAPHY]

Graduate of the Paris Institut des Sciences Politiques and the Ecole Nationale d'Administration (ENA). Since January 1st 2009, JEAN-CYRIL SPINETTA has been Chairman of the Boards of Directors of both AIR FRANCE KLM and Air France. Formerly, he joined Air Inter as Chairman and C.E.O. in 1990, where he remained until 1993. Then, he was Chairman and C.E.O. of Air France from September 1997 to January 2009. He became Chairman and C.E.O. of the AIR FRANCE KLM Group in September 2004.

Jean-Cyril Spinetta was also Chairman of the Association of European Airlines (AEA) for the year 2001. He was elected Chairman of the International Air Transport Association's (IATA) Board of Governors for 2004-2005. He also served as Non Executive Director of Unilever PLC and Unilever NV from May 2006 to September 2007, currently sits on the Boards of Directors of Alcatel-Lucent, Saint-Gobain and since April 2009 has been chairman of the supervisory board of Areva.

Jean-Cyril Spinetta is a Commander de la Légion d'Honneur, Commander de l'Ordre National du Mérite, Officier des Palmes Académiques and Commander in the Dutch Order of Orange-Nassau.

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