

succession planning is your best defense against activism

*As published in NACD Directorship's
Boardroom Intelligence, June 11, 2015*

By Kim Van Der Zon and George L. Davis

For good or ill, activists now are important players in the investor ecology, with increasingly successful records for changing a board's makeup. At Egon Zehnder, we identified 58 incidents of investor activism against S&P 500 companies over the last two years. Of those, 16 contests involved changes to board composition, urging a "no" vote on the management's slate of directors or proposing, or threatening to propose, an alternative slate. And of those, only six concluded in favor of management, resulting from the activist slate being withdrawn before a vote or management's victory in a vote.

It is not surprising, then, that many boards are evaluating their plans for responding to an activist slate this proxy season. Broadly speaking, however, there are really only two possible courses of action a board can take. One path is to accept the reality of activist scrutiny and build it into the nominating committee's ongoing work. The nominating committee needs to look at the board with an objective eye and identify how its composition might give an activist a foothold,

such as directors with conspicuously long tenures or directors whose experience is unaligned with the company's business and its strategic direction. The nominating committee must then design a director succession plan that identifies, cultivates, and elects candidates with the desired competencies. Doing so is not a guarantee against activist action, but having a carefully chosen board with relevant backgrounds and perspectives deprives activists of a clear weakness to exploit.

boardroom conversations

Because board seats turn over intermittently and because competition for directors is so high, fully executing this strategy can take several years. In the meantime, an activist investor may well decide to put forth its own slate. When that happens, the nominating committee must shift into high gear. In the 16 activist initiatives involving changes to board composition, the median campaign length was found to be only 77 days—just 11 weeks from the initial announcement to some sort of resolution. And six of those 16 initiatives concluded in less than one month.

Of course, the company could stick with its current slate and hope it receives the necessary votes. But once activists have sown the seeds of doubt in the minds of other investors, events have shown that change is more or less preordained. It is simply a matter of whose change will prevail.

Because time is of the essence when faced with an activist slate, it is incumbent upon boards to watch closely for tremors that might precede such an action. Besieged boards might feel blindsided, but successful activist attacks rarely come out of the blue. Seven of the companies that were subject to investor activism on board composition were the targets of initiatives from more than one group. For example, while Starboard's Jeff Smith may be the one credited with replacing the Darden board, that upheaval only followed an initial salvo from Barrington Capital Group. Once the board gets the faintest sense that it is the object of activist interest, it needs to move quickly to examine its composition and reshape it as needed.

When the battle is joined, boards must ensure they do two things. First, they must reach beyond their usual networks in identifying new director

candidates. Expanded networks are more likely to allow the board to draw upon candidates with a wider range of perspectives and experiences. Furthermore, the wider pool of candidates (and connections to candidates) is essential if a company can hope to quickly assemble a slate that doesn't look quickly assembled.

Once the company has its nominees, it then must convince the investor community to give its support. Here it is particularly helpful to steal a page from the activist playbook. Activists know that no matter how good their slate may be, their real power lies in their ability to sway a majority of investors to their side. As a result, the best activists are also the best communicators. They make sure that the story they tell is clear and compelling and then tell that story relentlessly. If management has been less than successful, it is because they have been out-maneuvered in the court of investor opinion. Management must make sure that the story they tell about their slate is even more compelling than that put forth in support of the activist candidates, and it must be told with the same energy and clarity.

The bottom line is that nominating committees must build strong director succession plans that result in boards that are clearly relevant for the challenges and opportunities the business is facing. Their only choice is whether to do so preemptively and with the luxury of time or, instead, with their back to the wall and the clock ticking.

boardroom conversations

Authors



Kim Van Der Zon

Head, Global Board Practice
New York

Kim.VanDerZon@egonzehnder.com
+1 212 519 6000



George Davis, Jr.

Head, Global CEO Search and Succession Practice
Boston

George.davis@egonzehnder.com
+1 617 535 3500

Egon Zehnder is the world's leading privately held executive search and talent management consultancy with more than 400 consultants in 69 offices across 41 countries. The firm provides senior-level executive search, board search and advisory, CEO succession and family business advisory, as well as leadership assessment and development to the world's most respected organizations. Egon Zehnder's clients range from the largest corporations to emerging growth companies, family and private-equity controlled entities, government and regulatory bodies, and major educational and cultural organizations. For more information: www.egonzehnder.com.

Amsterdam	Madrid
Athens	Malmö
Atlanta	Melbourne
Bangalore	Mexico
Barcelona	Miami
Beijing	Milan
Berlin	Montreal
Bogotá	Moscow
Boston	Mumbai
Bratislava	Munich
Brussels	New Delhi
Budapest	New York
Buenos Aires	Oslo
Calgary	Palo Alto
Chicago	Paris
Copenhagen	Prague
Dallas	Rio de Janeiro
Dubai	Rome
Düsseldorf	San Francisco
Frankfurt	Santiago
Geneva	São Paulo
Hamburg	Seoul
Helsinki	Shanghai
Hong Kong	Singapore
Houston	Stockholm
Istanbul	Stuttgart
Jakarta	Sydney
Jeddah	Tel Aviv
Johannesburg	Tokyo
Kuala Lumpur	Toronto
Lisbon	Vienna
London	Warsaw
Los Angeles	Washington, D.C.
Luxembourg	Zurich
Lyon	

© 2015 Egon Zehnder International, Inc.

All rights reserved.

No part of this publication may be reproduced, stored in a retrieval system or transmitted in any form or by any means — electronic, mechanical, photocopying, recording or otherwise — without the prior permission of Egon Zehnder.