Pearl Meyer

ADVISOR BLOG

Do Boards Need a Temporary CEO Succession Plan?

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The Wall Street Journal recently ran an article observing that temporary succession planning may become a more pressing issue as concerns arise about the spread of COVID-19. The article then states that finance chiefs are likely contenders to temporarily fill a CEO role, if needed, and outlines several compelling reasons why CFOs are strong contenders.

That got us thinking about a few related issues:

- Shouldn't a properly designed CEO succession plan cover all contingencies?
- How does a compensation committee structure compensation for the temporary successor?
- How does the board communicate the change internally and externally?
- What about disclosure?

First, a key responsibility of the board is CEO succession. A well-designed succession plan should cover both long-term planning and emergency needs. Given that emergency succession planning has always been viewed as important for risk mitigation during a crisis, it is surprising that approximately 40% of organizations in a 2017 NACD report had not identified an emergency successor to the CEO. Now is the time to clearly think through and document your emergency/temporary succession plan, including the succession chain that will be triggered by naming an internal interim CEO.

The good and bad news is that there are no prevailing practices regarding the form and structure of pay for a temporary CEO. The following are a few high-level ideas to consider. These ideas assume the executive will fill the temporary CEO role for less than a year. And remember that it will be easier to disclose and communicate an executive compensation plan that is not overly complicated.

- **Salary**: It is common practice to increase the interim executive's salary while in the CEO role. Raising the salary to the 25th percentile of the CEO pay benchmark for the period the executive will be serving as CEO may be a sound approach. The salary can revert to the prior level once the executive is back in his or her original role.

- **Annual Incentive:** You can employ the same concept here. Raise the target award based on the 25th percentile CEO benchmark levels. The more difficult actions are whether to modify existing goals or add new goals, and the committee should discuss how to incorporate discretion in assessing the temporary CEO's performance.
- **Long-term Incentives:** Depending on the length of time the executive fills the temporary role, the committee may not need to make any adjustments to the "regular" long-term incentive grant. But, depending on the circumstances, the committee may want to consider a one-time grant either at the time the company appoints the temporary CEO, or after the original CEO returns, to acknowledge the additional service provided by the executive filling the temporary role.

Although the expectation in this scenario is that the CEO will return once recovered, the committee should be prepared with back-up plans if the CEO is sidelined longer than expected or is not able to return.

It is also important to remember that while it would be preferable to keep health a personal issue, public companies can't keep these interim modifications a secret. If someone is fulfilling the role of an interim CEO, disclosure will generally be required on a Form 8-K within four days of the decision to do so (or must accompany a press release on the topic). The filing would need to include the person acting in the interim position, a brief description of any contract or compensatory arrangements made with the individual, as well as any new or modified compensation grants in connection with the appointment. Any new or modified contract with the interim executive may be attached to the Form 8K, but must be attached to the next periodic filing.

Beyond the required securities law filings, being ready and able to execute on a message strategy to support the board's actions is also important. Companies must be able to reassure their workforces, as well as other external stakeholders, that having this temporary CEO at the helm is a good thing. This means at the same time required disclosure narratives are being developed, the board should also be working with their corporate communications, HR communications, public relations, and/or investor relations teams to craft the additional needed materials to ensure continuity of messages across various means of communication including internal emails and conference calls, press releases, web postings, etc.

In summary, there are many issues boards should consider if they need to appoint a temporary CEO, but there may well be many more issues to face in the absence of a CEO, particularly in our current global situation. A well-designed succession plan will be immensely helpful in getting a head start with the process of identifying a temporary candidate and addressing compensation, disclosure, and communications issues.

About the Author

Pete Lupo is a senior managing director and head of the Atlantic Region. Pete has worked extensively with compensation committees and management covering a variety of needs including the development of total compensation programs covering the senior leadership team, aligning pay to performance, designing annual and long-term incentive plans, developing board of director pay programs, advising on change-in-control, executive benefits, perquisites, and governance-related matters.

About Pearl Meyer

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