
IMPACT OF BOARD SUCCESSION PLANNING ON CORPORATE GOVERNANCE PRACTICES

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ABSTRACT

This study delves into the influence of board succession planning on corporate governance practices within organizations. Board succession planning is the process of identifying and preparing potential candidates to fill upcoming vacancies on the board of directors. It plays a critical role in ensuring leadership continuity, fostering board diversity, and upholding stakeholder trust.

This research aims to investigate how effective succession planning strategies contribute to various aspects of corporate governance. This research will also examine whether organizations with robust succession planning processes tend to have more diverse boards with new experiences and perspectives. Additionally, we will explore how succession planning practices impact stakeholder engagement and perceptions of governance effectiveness.

Keywords: delves, governance, diverse, succession, engagement, perceptions

METHODOLOGY

The study has adopted the doctrinal approach to research, which mainly uses secondary sources. We have consulted as many sources as possible, including books, journals, and various articles from India and other countries. The following techniques have been used to fulfill the goals of our study and collect the necessary.

1. Study of the research books already in existence.
2. Legal books and journals that are both primary and secondary sources.
3. Online browsing.

INTRODUCTION

Corporate governance can be described as a set of principles, processes, and policies that steer the corporation in the direction that it should act. To ensure effective corporate governance, a company employs a set of people who ensure effective corporate governance. A company is a separate legal entity, and it has perpetual existence, which creates a need for board succession that requires proper procedures and guidelines. This procedure and guidelines will be enumerated in the board succession plan after effective board succession planning. The board succession plan comprises the systematic selection, training, and replacement of board members who would provide diverse perspectives, abilities, and skills to the boardroom.

This research explores the relationship between board succession planning and corporate governance practices. It aims to provide a comprehensive analysis of the impact of board succession planning on corporate governance practices.

RESEARCH QUESTION

How does effective and ineffective board succession planning affect corporate governance practices?

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Board succession planning is one of the important aspects of maintaining and sustaining

effective corporate governance practices in a company over a long period of time. It helps build a promising future for the company and its shareholders. Without good succession planning, the next group of board members might not even be as knowledgeable as the previous group of board members, which can affect the company. Effective board succession planning helps in creating a good board succession plan, which is a document that contains the procedures and guidelines for board succession. In India, Section 178 of the Companies Act 2013 states that the development of a succession plan is an object of the nomination and remuneration committee.

Understanding Effective Board Succession Planning

Effective board succession planning is one of the necessary steps in sustainable corporate governance practices. A board succession plan is effective if it considers the following aspects:.

Company's strategy and objectives

The board's succession planning should take place with respect to the company's objectives and strategies. While planning, the committee should define the goals, objectives, and long-term vision of the company and frame the board succession plan. Strategies, goals, and objectives should be used as a framework for board succession planning. This framework helps in identifying skills, expertise, and diversity, which will help in aligning with the organizational goals and objectives.

Diversity and inclusion

Considering diversity and inclusion while planning can foster innovation, creativity, and effective decision-making. It promotes the inclusion of individuals with diverse skill sets, backgrounds, and perspectives, leading to more robust discussions, innovative solutions, and better decision-making within the boardroom. When you bring together a group of people with different skills and experiences, they can look at problems from many angles, ask tough questions, and have more lively discussions. This is especially true for top management teams because having diverse viewpoints helps them come up with better solutions.

Transparent processes and policies

Transparent processes and policies in board succession planning can promote accountability,

fairness, and compliance with regulatory requirements. A company should establish clear procedures and policies for board succession planning, which should be communicated to its members and stakeholders. This procedure should outline the roles and responsibilities of the nomination committee. Transparent succession planning motivates the employees by showing that their skills are valued, and it also builds shareholder trust in the board.

Succession Pipeline Development

Building a strong pipeline of potential board members is essential for maintaining continuity and being prepared for any future changes in leadership. Organizations build a pipeline of potential board candidates who aligned with the organization's goals, strategies, and values.

Organizations can identify potential candidates internally as well as externally.

Organizations should actively try to find and cultivate internal talent through various programs and succession planning initiatives. It should also maintain relationships with qualified external candidates who will bring a diverse perspective to the board. P&G takes pride in its ability to quickly fill important leadership positions. It works to have three potential candidates ready for each top position at any given time.¹

Impact of effective board succession planning in corporate governance practices

Promotion of Meritocracy and Transparency

Effective board succession planning uses a merit-based approach, which ensures that the board is appointed based on qualifications, skills, and expertise rather than nepotism and favoritism. Effective board succession planning is a transparent process that instills confidence among stakeholders, shareholders, employees, and regulators. When stakeholders perceive that the board is appointed on a merit basis, they are more likely to trust the decisions taken by the board.

Apple Inc is frequently seen as a prime example of effective board succession planning. The company is renowned for its meticulous selection of board members, who are chosen based

¹ Adrian Gostick , Developing A Leadership Pipeline: Plan Ahead Or Get Left Behind, Forbes(Nov. 7, 2023,12:42pm),<https://www.forbes.com/sites/adriangostick/2023/11/07/developing-a-leadership-pipeline-plan-ahead-or-get-left-behind/?sh=63607e717ed3>.

on their expertise and contributions to the organization's strategic direction. By maintaining transparency in its succession planning processes, Apple has garnered the trust and confidence of its stakeholders, thus playing a pivotal role in its success as a leading technology company. *"We're a company that believes in working on succession plans, so we have very detailed succession plans—because something that's unpredictable can always happen, I can step off the wrong curb tomorrow. Hopefully that doesn't happen. I pray that it doesn't,"*

- CEO Tim Cook²

Continuity and stability

Effective board succession planning ensures a smooth transition of leadership within the organization. Effective succession planning ensures the smooth running of the organization in the long run when there is a change in the board of directors. The corporation's smooth transition from Bill Gates to Steve Ballmer as CEO exemplifies effective succession planning, demonstrating how a well-planned succession process can contribute to continuity and stability in corporate governance.

Enhanced Board Diversity

Effective board succession planning prioritizes diversity. Which fosters innovation, creativity, and effective decision-making. It promotes the inclusion of individuals with diverse skill sets, backgrounds, and perspectives, leading to more robust discussions, innovative solutions, and better decision-making within the boardroom. It includes factors such as gender, ethnicity, industry experience, and skillsets.

Goldman Sachs' appointment of Adebayo Ogunlesi as Lead Director reflects the company's commitment to diversity and inclusion in leadership positions, showcasing how effective succession planning can enhance board diversity and transparency.

Improved governance oversight

Good board succession planning can improve governance oversight in a corporation. For example, it can help in appointing a good independent director who does not hold any kind

² Apple's succession plan is completely different to OpenAI's, in that it actually has one, <https://qz.com/apples-succession-plan-is-completely-different-to-openai-1851041428/>, (last visited April 15, 2024).

of relationship to the company or the members of the company. These independent directors bring unbiased perspectives to the boardroom. They bring fresh perspectives and offer honest opinions, which makes sure everything is open and fair. Transparency and accountability build trust among everyone involved. By carefully choosing directors who are both skilled and unbiased, companies create a strong foundation for making ethical decisions, which boosts the confidence of the stakeholders and members of the company.

Impact of in effective board succession planning in corporate governance practices

Short-Termism and Lack of Succession Preparedness

Ineffective board Succession planning can only last for a short period of time as the candidates do not align with the goals, strategies, and objectives of the company. It can employ an unskilled person who might cause the downfall of the company. Not planning effectively and focusing only on the present instead of thinking ahead can lead the company into chaos..

General Electric Company (GE): After Mr. Immelt, the new leaders, like John Flannery, didn't do much better. John Flannery, who became CEO after Mr. Immelt, made a work environment where people felt like victims instead of feeling motivated to work towards a common goal. Mr. Immelt wasn't surprised by this because he expected it to happen. In simple words, the new leaders didn't improve things much, and instead, the company culture became negative under John Flannery's leadership.

"Flannery couldn't make a decision"" He was ponderous and always needed reams of data before choosing a course of action ".

- Mr. Immelt³

Conflict of Interest and Insider Bias

Poor succession planning may lead to the appointment of board members with strong connections to current members of the board. This can result in conflicts of interest and insider bias. This act can result in the board losing its independence and its ability to make impartial

³ David Gelles, Jeff Immelt Oversaw the Downfall of G.E. Now He'd Like You to Read His Book. The New York Times, (Feb. 5, 2021) ,<https://www.nytimes.com/2021/02/05/business/jeff-immelt-general-electric-corner-office.html?smi>

decisions.

Reputation Damage and Loss of Stakeholder Trust

When succession processes are seen as opaque or ineffective, they have the chance of damaging the reputation of the organization, which can ultimately lead to losing shareholder trust.

Negative publicity surrounding board appointments or leadership transitions can lead to stakeholder confidence in governance practices, affecting investor perceptions and organizational credibility.

Toshiba Corporation faced a corporate governance scandal in 2015, highlighting the consequences of ineffective succession planning on reputation and stakeholder trust. The company's failure to prioritize transparency and accountability led to significant reputational damage and a loss of stakeholder trust.

Risk of Nepotism and Cronyism

Ineffective board succession planning may lead to the appointment of individuals based on personal connections or relationships and not on their merits. This can result in nepotism and cronyism within the boardroom, which can undermine transparency and accountability in governance practices.

Case Law: In re The Walt Disney Co. Derivative Litigation (2005)⁴

The Walt Disney Company faced shareholder litigation alleging that the board's failure to conduct proper succession planning led to the appointment of Michael Eisner's close friend Mr. Michael Ovitz, as president. The court criticized the board for its lack of diligence in the succession planning process, highlighting the risks associated with nepotism and cronyism.

Lack of Diversity and Independence

Lack of proper succession planning can result in a lack of diversity and independence within the boardroom. When there is diversity on the board, it brings innovation, creativity, and

⁴ In re Walt Disney Co. Derivative Litigation, 906 A.2d 27 (Del. 2006)

effective decision-making to the boardroom, but without diversity, there is no innovation and creativity in the boardroom. Lack of diversity can also bring new perspectives to the boardroom.

Lehman Brothers fell apart in 2008 because its board of directors wasn't diverse or independent enough. The collapse of Lehman Brothers in 2008 is frequently linked to its board of directors lacking diversity and independence. The board didn't properly supervise the company's risk management, resulting in excessive risk-taking and eventual bankruptcy⁵. This situation highlights the significance of having a diverse and independent board, which can be attained through successful succession planning.

CONCLUSION

Board succession planning creates a major impact on corporate governance practices; it can have a have a positive as well as negative impact, and it depends on the effectiveness of the board succession planning. Effective board succession planning promotes transparency, meritocracy, stability, and diversity in the boardroom, which can help increase the long-term shareholder wealth of the company. Ineffective board succession planning will most likely lead to termism, conflict of interest, insider bias, loss of shareholder trust, risk of nepotism, and a lack of diversity, which can destroy the independence and innovation of board members in the decision-making process.

Although effective board succession planning sounds too good to be true, it is hardly implemented by companies, and there is no proper definition for effective succession planning. Few companies, like Apple and Microsoft, try their best to implement effective succession planning and succeed, and some companies, like General Electric, fail in that process.

⁵ Johnson, Mark Anthony, and Abdullah Mamun. "The Failure of Lehman Brothers and Its Impact on Other Financial Institutions." *Applied Financial Economics* 22, no. 5 (2012): 375–85. doi:10.1080/09603107.2011.613762.

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