

# Spin-Off Boards: Creating Dream Teams

by Charles H. King and Madeleine Condit

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**Spin-offs of divisions have proven a highly popular way for corporations to create shareholder value over the past few years. They also offer a rare opportunity to create corporate governance value. By starting with a “clean sheet of paper,” the new company can craft a board of directors that targets its exact strategic needs.**

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Since 1792, companies have been trying to gauge their operations to increase their impact on Wall Street. During the past three years, the market has been described as exuberant, risky, over-inflated, and undervalued. The initial public market had been robust up to 2001. Part of this activity is directly related to the record 78 spin-offs that have occurred since 1998.

Dupont, Hewlett-Packard, EMC, Williams Companies, Sara Lee, and AT&T are just a few of the companies to spin off divisions. Yet in some cases, the investors' initial enthusiasm was followed by a major sell-off.

**The spin-off provides a once-in-a-lifetime opportunity to create a “dream team” board. A key factor is the CEO's attitude.**

Each of these CEOs had a once-in-a-lifetime opportunity to create a “dream team” board of directors—free of a fixed mentality, one with the best possible skill set to advise and guide management. Yet not every spin-off board qualifies as a model of good (or even effective) governance.

Why? A key factor is the chief executive's attitude and approach. Those who have the most effective boards are smart enough to recognize what they are lacking—and how it affects what they hope to achieve.

Few CEOs have built a board from scratch, nor do they have the time to do so themselves. They have a new company to run. Not surprisingly, the first step many spin-off CEOs take is retaining a board consultant. Together they create a matrix, examining and establishing every aspect of building a board, and director selection. The process begins with the CEO's vision of his ideal board and wish list.

□ *An ideal board.* Spin-off CEOs see their board as an incredible competitive advantage, a think tank that can help a company quickly capitalize on its solid foundation and continue that success into the future. They want to assemble the best bench of talent the company could never afford to hire.

For many, it is not enough to put together a great board. Their goal is to create a model of good governance. Candidates for these boards must not only be interested in providing guidance to a company but in continually improving governance. Starting with a clean slate lets CEOs establish board culture. To avoid the personality issues that often hinder established boards, recruitment must assess each individual's business style and its compatibility with the boardroom tone set by the chief executive.

A mix of experienced and new directors is critical to spin-off boards. Experienced directors are needed to chair committees and assist the CEO in mentoring new board members. Including less-seasoned or first-time directors ensures leadership continuity. This is a concern of Fortune 500 boards, many with a majority of members near or over age 60. The 2001 Korn/Ferry board of directors survey found more than half of Fortune boards include a first-time director.

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In visualizing the ideal board, spin-off CEOs detail specific skills needed to best provide guidance to the new company. Typically every spin-off board includes members with industry experience, marketing, finance, global, and technology expertise. Among the members of every spin-off board are one or two sitting CEOs or COOs. They bring strategic skills and the ability to communicate the “big picture” to the board. As peers of the CEO, such directors provide a sounding board for the chief executive.

Often the network of contacts which directors possess becomes a consideration in building a spin-off board. One chief executive wanted a CFO for his spin-off board, but this executive had to be a local. A strong tie was sought to the business community where the spin-off was headquartered.

Most spin-off CEOs are eager to create diverse boards. These boards seem inherently diverse in terms of background, gender, industry, and ethnicity. With few exceptions, the modern spin-off board slate includes a woman or minority. Rather than a concerted effort to identify a woman or minority candidate, this diversity is usually a by-product of identifying a proven business person with specific expertise or skill set. One spin-off board of eight members included two women because their skill sets were a fit and their backgrounds indicated they were well-qualified.

□ *Board operations and recruitment.* Assembling a dream team board is only possible when expectations of performance are clearly delineated and communicated to potential directors. To do so, conversations about the ideal board must focus on detailing the board’s practices and operations in the early stages. Since much of the work of the board originates in committees, deciding the number and type of committees affects the size of the board as well as the talent needed.

Spin-off companies are best served by having the full membership set when the company is launched. One CEO felt a five-member board would be adequate in the early stages of the spin-off. Shortly he realized the board was too small to handle committee and full board work, one-on-one consultation to

the CEO and top management, and other related activities. To more evenly distribute duties, two more members were added.

Another CEO worked with his board consultant to create a matrix that detailed duties, skills, and all other considerations in creating the board. The data showed eight directors were needed to equitably handle the duties. Most spin-off boards have seven or eight members.

**Many spin-off CEOs are anxious to add well-known executives to the board, whom they assume will be eager to join. These “wish lists” must then be aligned with market realities.**

With the dream team profiles and board practices identified, many spin-off CEOs are anxious to contact well-known executives, confident that this opportunity will whet their appetite for board service. After conversations with their board consultants, the “wish lists” are refined to be more in line with market realities.

One spin-off CEO’s “wish list” of possible candidates included some of the most sought-after executives in the world. He was intent on building a marquis board, and cited several spin-off and IPO board members including Fortune CEOs as director candidates.

If a well-known executive joins the board of a small company, there is often a personal element involved. The “name” chief executive and a key member of the spin-off or IPO probably have a history—a long-term relationship built on trust and confidence in each other’s business abilities.

□ *Not always the usual candidates.* By understanding the dynamics of the market and the talent available, the spin-off can exercise greater creativity in recruiting the talent needed to the board. Stronger SEC regulation of board involvement in the audit function requires the board to have members with strong finance skills, making a CFO a logical candidate. Previously boards shied away from chief financial officers, viewing them as too narrow in overall

## Arbitron's New Board

### A Board For The Strategy You Have Right Now

*Stephen B. Morris recently built the board for Arbitron, a spin-off of Ceridian. As CEO of this global leader in media information, Morris had specific strategic considerations as to the skills needed and the board culture he wished to create. In this interview, Stephen Morris shares his experience and ideas about building a board from scratch—including having a non-executive chairman.*

#### **The Corporate Board: How did you approach the creation of the Arbitron board?**

**Stephen Morris:** I viewed it as an extraordinary opportunity. Creating a spin-off board is probably the only time you can pick the people who have those skills you want for the strategy you have *right now*.

#### **TCB: You seem to place particular emphasis on “the strategy you have right now.”**

**Morris:** When Arbitron was part of Ceridian, it was a U.S.-based radio data company. As an independent entity, we are evolving as a global leader in media information. All the directors share and focus on that strategy.

With merged companies, the board includes directors from both companies to meet legal requirements. Each company had a different strategy and the directors bring that to the new board. Arbitron, like other spin-offs, has a *pure strategy* status.

#### **TCB: In tackling this extraordinary opportunity, what was your first step?**

**Morris:** Our first step was deciding on the culture of the board. I wanted directors who were more comfortable as active advisors, individuals who would feel free to come to meetings—or me—with ideas. The agenda would have room for comment and vigorous discussion.

#### **TCB: Why did you choose to have a non-executive chairman head the Arbitron board?**

**Morris:** I'm a big believer in having a non-executive chairman for spin-off boards. Setting up a board—the committee charters, the mentoring, everything needed to create a structure for a board—is a tremendous amount of work. A spin-off CEO is learning and leading a brand new company. Having a non-executive chairman in the initial stages is a logical division of labor.

#### **TCB: How did you choose the non-executive chairman?**

**Morris:** First, it had to be someone I trusted completely. Ideally, a high-profile individual who knew the industry and Arbitron. Lawrence Perlman, the former head of Ceridian, was someone I had worked with, whom I respected and trusted. He agreed to be the non-executive chairman.

It has proven to be a great decision. Having a non-executive chairman running the board injects enthusiasm and helps set the tone of the boardroom. The members seem more industrious and energetic when one of their own is in charge.

business experience to be strategic, well-rounded contributors.

However, many CFOs have demonstrated the ability to be a business partner with the CEO and are routinely involved in a wide spectrum of business decisions such as mergers and acquisitions. Those who come up the ranks through the treasury or controller side are ideal choices for chairing an audit committee.

One spin-off board included a member from each of its major customer categories: government, private companies, and public companies. Another board sought director candidates who had previously worked for one of their customers. These talents

brought eye-opening, impartial perspectives about products, services, and communication to board discussions, helping refine strategy and identify areas for improvement.

Depending on the type of industry, regulation, and proposed business activities, some spin-offs pursue former government officials as directors. These candidates bring a broad network of contacts to the company as well as an understanding of the “foreign culture” of government.

Technology figures in every business. Expectedly, most spin-offs want a board member with this expertise. Chief technology officers and chief information officers from major companies, or executives

**TCB: Who else was involved in selecting directors?**

**Morris:** The CEO of our parent company and the head of the nominating committee both interviewed director candidates. They felt it was part of their fiduciary responsibility to be involved in setting up the board for the spin-off.

**TCB: How did that affect the building of the board?**

**Morris:** Their evaluation and comments were incredibly valuable. But their involvement also contributed to what I see as the only downside in creating a spin-off board—the amount of time it takes to interview candidates. These are not one-hour meetings; some last three or four hours. Plus, we had multiple meetings with candidates to gain a real understanding of their business philosophy, personal style, and the strengths they would bring to the board. Geography added to the time invested. Candidates met with me in New York, the Ceridian CEO in Minneapolis, and the head of the nominating committee in Kansas City.

**TCB: What did you find most difficult about building your board?**

**Morris:** Finding a member who could bring the perspective and experience of the radio industry to the table, a person commanding the respect of the industry, who had no conflicts of interest. With our business, everyone in the industry is a customer or a potential customer.

We were fortunate to identify Erica Farber, publisher

and CEO of Radio and Records, a major industry magazine. She has a reputation for being a completely objective reporter, which put to rest concerns about impartiality. Additionally, Erica was a general manager of a radio station earlier in her career, a pioneer in the position. At that time there were probably only five or ten other women holding that post out of the thousands in the country.

**TCB: How long did it take to create the Arbitron board?**

**Morris:** It took three months to recruit our six outside directors. The key is to have a good search firm. It would be impossible for a CEO to identify the type of high caliber people we have on the board. Some of the people we have on the board were not obvious fits. Their background in the industry is overshadowed by their current success and position. Again, the time involved is a factor.

**TCB: What advice would you give other spin-off CEOs in creating a board?**

**Morris:** Look at the most high-powered group you can attract. Not only will their experience and guidance help launch the company more quickly and with greater success, but the composition of the board helps position the company with investors. I experienced this when doing road shows. Investors who seriously evaluate management as part of their business decision process paid careful attention to the Arbitron board.

from technology industries, are good candidates. These executives have broad business experiences enabling them to evaluate technologies as they can benefit the entire enterprise and communicate their findings in an understandable manner.

Spin-off boards must be aware of the distinction between executives with technology backgrounds or technology companies and those from the Internet. Frequently, their skill sets and level of business maturity differ dramatically. Being part of the senior team at a dot.com may not qualify an executive as an expert in technology. Many are more attuned to finance or sales and lack the requisite business experiences that influence a director's ability to

fully contribute within a culture.

The exceptions are those Internet executives who were formerly proven leaders at major corporations. Wanting the challenge of building a new business, they often took top roles at fledgling dot.coms. Their enthusiasm, leadership skills, and business acumen may make them good candidates for spin-off boards, though they may not be able to provide in-depth technical assessments.

Most spin-offs find it advantageous to include a director with global expertise. This is particularly critical for companies with locations and customers throughout the world or for those planning to expand into foreign markets. Rather than target a foreign

national, most spin-offs recruit a U.S. executive who has lived and worked abroad.

Such candidates bring a variety of talents to the boardroom. The last decade saw the number of expatriate executives increase. Unlike their predecessors, once they return to the United States, many successfully assume increasingly challenging executive roles, giving them the broad business experience needed to assume the responsibilities of a corporate director.

□ *Recruiting the dream team.* Envisioning the ideal board is one thing—recruiting its members is another. Since time is usually an issue in creating a spin-off board, anticipating candidates' concerns helps to narrow the field.

Time is a major factor in evaluating invitations for board service. In fact, it is a greater consideration in accepting a seat on a spin-off board than for an established board. A spin-off business usually requires its board and committees to meet more often, and impromptu conference calls are more frequent. Directors who are already on several boards are generally not considered viable candidates.

While qualified prospects consider the contribu-

tions they bring to a board, they also critically evaluate the company. Candidates carefully consider their ability to contribute to the board, as well as what opportunity exists to learn something relevant from the experience. Individuals who are unable to see the position as one of “give and take” are unlikely to accept. Issues of company size, quality of management, leadership style of the CEO and numerous other factors are considered.

At the end of the day, it is often the chemistry between the CEO and the candidate that determines the outcome. When CEOs adhere to a strategic, careful process, they dramatically enhance their ability to build a board comprising the talent they seek.

Building a board for a spin-off is a unique opportunity afforded very few CEOs. When done well, a near-perfect board can result. While rather simple in concept, the challenge is in the execution. With due consideration of the factors discussed, from size and skill sets to chemistry and fit, you can successfully assemble a team of advisors who substantially improve the performance of the business as it moves forward as a new, freestanding public company. ■

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