



## CEO Succession: How One Board Drove Transformation

New Year's predictions are tricky, but one thing we know with certainty about 2016 is that the pace of change in business—propelled by companies seeking new markets and new products and aided by increasingly sophisticated technology—will not abate. Crucial in this environment are boards equipped to serve as strategic assets, providing long-term competitive advantage to the shareholders they serve.

A few results from the most recent Korn Ferry Market Cap<sup>100</sup> (KFMC<sup>100</sup>)—a study of governance changes at the top 100 U.S. companies by market capitalization—offer a glimpse into how board composition is shifting and how boards view recruiting directors with the skills they need. While 17 percent of new directors are 65 and older, 16 percent are 49 or younger. That's a stark contrast to boards as a whole, including both new and incumbent directors, where 51 percent of directors are 65 and older, and a scant 4 percent are 49 or younger. This underscores efforts by the largest companies in America to add next-generation directors who bring the fresh ideas, insights, and skills that are essential in a rapidly changing business environment.

Rather than merely add directors on a one-off basis when there is a vacancy, boards should continuously align their skills and competencies to the challenges of the future—not of the past—in a manner that is highly respectful of the value of the current directors but also keenly aware of the need to refresh the board.

The case study of Harman International Industries highlights this process.

### A CEO's Perspective

When there is a major strategic shift or a transformation anticipated, board succession takes place on an accelerated schedule. To get an idea of how this looks from the perspective of the CEO, we spoke with Dinesh C. Paliwal, chair, president, and CEO of Harman, the Fortune 500 connected-technologies company that serves the automotive, consumer, and enterprise markets. Paliwal was recruited following the announcement in April 2007, of a merger agreement between Harman and Kohlberg Kravis Roberts & Co. L.P. (KKR) and the GS Capital Partners unit of Goldman Sachs Group Inc.

When Henry Kravis and his team at KKR brought in Paliwal as CEO, Harman was undergoing a transition from a family-run company—founded in 1978 by Sidney Harman—to one run by a



Dinesh C. Paliwal, head of the electronics company and automotive supplier Harman, stands next to a concept car at the 2016 International Consumer Electronics Show.

professional CEO and board. Upon completion of the merger, the plan was for KKR to take the company private.

“I started as CEO on July 1 and the plan was to close in late September,” says Paliwal. “However, a few issues were uncovered, and KKR wanted to know why they hadn't seen them.” Paliwal explained them as a result of “operating hands and eyes coming in,” but KKR saw a broken company and, with a challenging macroeconomic environment creating additional headwinds, walked away.

Paliwal, by contrast, saw a turnaround opportunity and chose to remain as CEO. With strong brands and talented engineers, he recognized that Harman had great potential. By strengthening the management team and board, Paliwal could better capitalize on the company's work force and assets to reinvigorate an innovation culture and expand into new product markets and geographies to unleash Harman's future.

### The Right Start With the Board

To ensure he would have license to succeed as CEO, Paliwal, working with lead director Ann Korologos, set some conditions for his tenure. First would be establishing an independent board that adhered to professional governance policies and procedures. That would require replacing some of the directors, including the founder, his daughter, and the former CFO.

Second, he needed to recruit leaders who would understand, support, and help advance his strategy. “We needed a board that would help open doors in Europe and BRIC countries, and provide expertise in turnaround situations as well as HR, retail, and emerging markets, to name a few,” he says.

“Most of all,” continues Paliwal, “they needed to understand Harman and what we were trying to create.” Recognizing the value of a diverse board, Harman attracted leaders and experts of different backgrounds, gender, and nationality—including three women, as well as German, Chinese, Indian, and Scottish nationals. “It’s diversity not for the sake of ticking boxes but to gain expertise and insights from specific disciplines and markets,” says Paliwal.

Finally, Paliwal wanted the board to have a sense of his leadership style and philosophy and how he would transform the company. “I’m a hands-on CEO, and I like to be challenged,” he informed them, “but I cannot be effective if I’m second-guessed.”

### Professionalizing the Board

According to Paliwal, he and Korologos, a key partner in the turnaround, acknowledged that the company and the board needed a “reboot” as it transformed from founder-controlled to innovation-driven public company. “I committed to practicing true transparency, making communications with them and with the organization a top priority,” he says.

Among the processes Paliwal implemented to transform the board:

- **Regular monthly reports** to the board that provide key internal data on business and financial updates, as well as external data on competitive and economic shifts.

- **Executive sessions** at the start and end of each of the five board meetings annually, where Paliwal provides updates and discusses what he describes as his “constant paranoia,” anticipating what could derail current plans, and seeks the same from directors around the table.

- **Feedback sessions following board meetings** on his performance and, later, with the lead director to further discuss what they heard in the executive session. Paliwal also provides feedback to directors.

- **Encouraging directors to reach out** to his direct reports while keeping him engaged in the dialogue.

### Implementing the Transformation

In talking about the transformation, Paliwal emphasizes the “three Ps” of people, places, and pipeline: putting the right people in place, expanding into high-growth regions and visible venues, and ensuring that the innovation pipeline is full. This framework continues to drive Harman’s growth. In the past 12 months, Harman

has acquired six companies and added more than 7,500 employees, mostly software engineers and designers, to its work force. The company has experienced dramatic growth in Asia, Europe, and the Americas; and with the addition of cloud, mobility, and analytics capabilities, it has transformed itself into the technology partner of choice for the connected car, connected home, and connected enterprise.

“Once we put the right people and processes in place, we earned the right to grow,” says Paliwal. The company, which had been suffering significant revenue losses, has taken off under Paliwal’s leadership, expanding into high-growth markets internationally, doubling sales, and returning its financials to health and profitability.

In addition, Paliwal implemented a new IT system that unified 17 separate systems to enable cross-enterprise communication, and he continues to hold regular all-employee calls, write monthly letters, and engage employees in roundtables when he travels.

He attributes much of this success to the culture he has helped to build. “Communications breeds collaboration, which stimulates creativity,” he explains. “It’s a cycle that perpetuates itself if the culture and leadership let it. I’ve held hundreds of town hall meetings, and I let it be known that I want good ideas to be able to rise from anywhere. While I make the final decisions, I say the bad decisions are mine and the good ones are products of our culture.”

### The Next Phase

Paliwal anticipates further board transformation to add the skills and experience that will be required to fuel the next phase of growth.

“Initially we brought in new directors to stabilize the company and set a tone from the top about what Harman stands for—integrity, innovation, and excellence,” says Paliwal. “The governance and communications practices we put in place have served us well, and now we’re bringing in new directors with the skills to drive the next wave of our transformation.”

Paliwal views the evolution of the company and the board as a journey, and recognizes the need for speed, a word he says sums up the company’s culture. “Speed is not a strategy per se, but we have to be better and faster than competitors,” he says.

“The Harman board has contributed to our growth in many ways,” says Paliwal. “It also has helped me to grow by challenging and debating our ideas and assumptions to ensure we don’t miss something. At Harman, we are relentless in our pursuit of improvement. Our board is right there with us, engaged to help me and my executive team stay on top of our thinking process so that together we can ensure Harman’s long-term success.”

—Dennis Carey and Robert Hallagan