Chapter 1

The Case for Senior Executive Assessment

While CEOs and boards undoubtedly realize the importance of hiring for key leadership positions, they are often likely to defer to their subjective opinions and impressions about potential candidates in making such decisions. While this personal experience, intuition, and judgment are useful in the decision-making process, there is little time and resources being invested into services that allow for more objective and systematic appraisals of candidates. The global issue facing executive assessment is twofold. First of all, many CEOs and boards may not even be aware of the options that are available to assist them in the selection process. This lack of awareness is the result of a variety of reasons, many of which boil down to the fact that assessment consultants and firms have had fairly low visibility to date. Second, CEOs and boards may be somewhat skeptical of the executive assessment process in general.

Despite these issues, there is strong evidence that the quality of senior executives has a tangible impact on an organization's performance. The use of senior executive assessment provides a unique platform for addressing critical topics, including personnel selection, mergers and acquisitions, and succession management. Coupled with changes in rules and regulations related to corporate governance, the use of assessment may have added benefit in helping lower corporate risk.

The goal of this chapter is to provide an introduction to senior executive assessment, including the previous obstacles to wide acceptance and potential benefits to organizations that adopt these practices.

Companies know more about their enterprise technology than they do about their enterprise leadership. Many organizations typically expend significant proportions of revenue on testing, introducing, and monitoring their information technology systems. However, they invest less time and resources "getting under the hood" to ensure they have the full picture about the people that actually run (or will run) a given organization.

For example, the installation of enterprise software (such as SAP's systems that monitor finance, manufacturing, distribution, and human resources) often involves one to three years of planning and execution. The introduction of this software is an elaborate process involving extensive testing and retesting. The typical monetary investment for this installation process at a significantly sized company can vary from approximately $1 million to $100 million. Yet the decisions leading to the hiring and promotion of senior executives frequently are made in a far more casual manner (perhaps two days' worth of interviews).

Why is this the case? Why do companies invest more in testing their technology than testing their senior executives? It may be that CEOs and boards want to bring their personal experience and intuition to decisions about senior executives. While they often strive for objectivity and consider data in many business decisions, CEOs and boards are used to using their gut and personal impressions when ultimately making decisions, including decisions about people. For some decision-makers, the unspoken belief is that they will *know* senior leadership assets and liabilities when they see them. They believe they are attending to ethereal qualities that are best detected personally by experienced decision-makers (who will have to live with the decision).

Why CEOs and Boards Tend Not to Know a Lot about Senior Executive Assessment

CEOs and boards either do not know about the assessment options readily available to them, or they are wary of them. The summary in the box below ("Why CEOs and Boards Tend Not to Know a Lot about Senior Executive Assessment") attends to the first part of the problem.

CEOs and boards may have little exposure to assessment methods. Assessment may be known only as pre-employment testing at employee and supervisory levels. However, since 1993 I have asked people whom I am about to interview whether they have ever been through an assessment process previously (for hiring or development, for example). In 1993, approximately 30% of mid-level managers or above told me yes. Fifteen years later, approximately 80% tell me yes. Assessment has been moving up organizational structures through the years. The logical and strategic extension of this trend is that senior executive (and board) assessment will continue to become more common.

In addition, most senior executives have MBAs. Business school served as their introduction to all things important regarding knowledge and tools that were to help executives fulfill their responsibilities and become successful. A casual review of business school curricula yields little content about assessment. Only a handful of programs, such as Case Western Reserve's Weatherhead School of Management, feature assessment overtly.

Also, "employee testing" traditionally has been the domain of Human Resources functional areas. Few CEOs and board members have experienced a rotation through these areas of responsibility. This can also lead to assessment not being "top of mind."

Some important processes, however, do eventually transcend the Human Resources domain. One example is executive compensation. While general employee compensation is still conventionally a part of Human Resources, senior executive compensation often has the attention of CEOs and boards. Therefore, board compensation committees are very active in monitoring and discussing senior executive compensation issues (often through the use of consultants). Senior executive assessment may transcend this Human Resources boundary as well.

Many assessment professionals in the 60s, 70s, and 80s were clinical psychologists. These individuals were practically minded clinicians who wanted to explore a new (and deep-pocketed) client base. Clinical psychologists are trained to use confidentiality in the way they treat information about their clients. This confidentiality extends to the identity of clients. The challenge here is that the cornerstone of most business development in professional services involves demonstrating credibility through the discussion of specific work with specific clients. While people with different backgrounds (education and training) now become experts in senior executive assessment, this clinically based history may hinder the discussion about achievements in assessment conducted in organizations.

Many professional services firms advertise extensively, especially when they believe they can catch the attention of people who are CEOs or who sit on corporate boards. When I watch the Masters or other golf tournaments on television, I am exposed to the names and features of audit, tax, and consulting firms. I have yet to see a television advertisement explicitly about senior executive assessment. The closest advertisement I have seen is a commercial extolling the virtues of assessment as a part of online dating services such as eHarmony!

Senior executive assessment is often a behind-the-scenes activity that serves in support of decisions. It is not flashy or sexy. In that way, again it is a bit like audit or tax consulting. If there was a headline in the newspaper about recent senior assessment triumphs, to be accurate it would read “Board Does Not Consider CEO as a Good Fit Due to Rigorous Interviewing and Sound Testing.” Assessment professionals are rarely in the media.

Networking is another way that consultants gain new business at senior levels. My observation is that most assessment professionals are earnest, salt of the earth people. They are often self-reliant, hands-on, and technical professionals who may not hang around senior executives frequently in their spare time. Exposure of senior executive assessment through networking is thus limited.

Many senior executives enter their roles through recruitment by retained search firms who have traditionally not used assessment methods as a part of this process. Therefore, senior-level decision-makers miss an opportunity to be exposed to assessment in many hiring situations. Only within the past five years is there evidence that major and boutique search firms are integrating more rigorous assessment methods into their work. An unscientific review of these firms suggests that recently 25–50% of these search firms have introduced assessment testing and other methods into their assignments.

Finally, some CEOs and boards possess the belief that it is difficult to find quality talent for senior executive positions. Given this assumption of scarcity, the last thing on a decision-maker’s mind is to use an assessment process toward the end of an extensive search process to decrease the number of candidates. The reverse is true in assessment at lower levels in an organizational structure. Assessment is used in these instances to bring focus to a large candidate pool.

Summary:
Why CEOs and Boards Tend Not to Know a Lot about Senior Executive Assessment

1. It only recently is becoming more prevalent at the senior-most levels in organizations.
2. It rarely is described in business schools.
3. It primarily is hidden within the human resources function.
4. Part of assessment's heritage is in clinical psychology, and clinicians emphasize confidentiality about clients and tend not to promote themselves.
5. External assessment consultants currently do not advertise broadly.
6. It is rarely mentioned in the media.
7. Many assessment professionals are not "well networked" with CEOs and board members.
8. Senior-level recruiting firms historically have not used rigorous assessment methods.
9. It is difficult enough to find good senior executive candidates – there is no need to assess the few good candidates

Why CEOs and Boards Are Wary of Senior Executive Assessment

Everyone has knick-knacks of some type in their office. These can include photos, paperweights, and even signs bearing messages. I have noticed an interesting trend in signs/messages in CEOs' offices. Many of the best CEOs with whom I have worked feature some message in their office that shows their disdain for excuses. One version has the word "excuses" slashed out with red ink and in a red circle, just like the road signs found especially in Europe. The point is they want to bring as much into their control as is possible to try to ensure success. This is why senior decision-makers may not at first glance want to make use of senior executive assessment. They may feel that it takes the hiring process or a favorite candidate out of their hands, for example.

The cornerstone of effective assessment is accuracy. Yet CEOs and boards may doubt that a set of written questions or a professionally conducted interview can adequately capture the personality and drive of a complex and accomplished person. These critics may be concerned about faking and the distortion of responses on the part of a smart person being assessed who is motivated to show themselves in a positive way. They may believe that assessment methods result in insights that are general and undifferentiated, just like horoscopes and astrology.

Many potential consumers of senior executive assessment are very successful themselves. They either implicitly or explicitly attribute portions of their own success to their effectiveness in reading people. They do not want to believe that they should need help in uncovering limitations in a person or predicting a person's behavior. Taking this point further, when executives make hiring decisions that have poor outcomes, they often attribute this failure to the candidates' inability to perform well and adapt. The thinking is such that the hiring failure is not about the hiring executive. Hiring executives in this situation will therefore see no reason to improve their hiring processes.

A large portion of senior assessment work is conducted by psychologists. The image that many people, not just CEOs and those who sit on boards, have of psychologists is often not favorable. The concerns fall into two categories. One is that they are weird, strange, and offbeat. Therefore, the methods they use are weird, strange, and offbeat. The other is that the process is overly technical and mechanical or overly theoretical. Therefore, the process will not feel like a meeting or conversation, or anything that resembles a day in the life of a senior executive. The concern is that assessment will feel like something being done to senior executives, like a medical procedure.

Given the stereotype that these assessment specialists might be weird, the related concern is that the relationship with an assessment professional might not be enjoyable. Even worse than weird, assessment professionals might be dry, serious, and devoid of a sense of humor. The summary in the box below ("Why CEOs and Boards are Wary of Senior Executive Assessment") summarizes these reasons why CEOs and boards may be wary of senior executive assessment.

What Is Senior Executive Assessment?

Senior executive assessment is a process that introduces rigor and objectivity into the measurement of the current capabilities and/or

Summary:
Why CEOs and Boards are Wary of Senior Executive Assessment

1. They fear that they will have less control or influence over decisions.
2. They are not sure of the accuracy of assessment methods.
3. They believe that they themselves should be completely competent in "reading" people – they are not sure what assessment methods can add to a decision.
4. They have a belief that assessment methods will be too weird, contrived, or uncomfortable for those being assessed.
5. They have a belief that assessment professionals will not be able to build rapport or credibility with those being assessed.

future potential of a senior executive (or group of senior executives). This assessment process can be applied to a vast array of decisions and situations (for example, hiring, promotion, succession, mergers and acquisitions, and private equity) that will be discussed later. The different methodological options (for example, interviews and questionnaires) will also be discussed later. Assessment can be conducted by external consultants or internal colleagues, often from Human Resources. Depending on methodology, the individual conducting assessment work may or may not have a degree in psychology.

While many people use the term "senior executive" in different ways, for the purposes of this book senior executives are defined as chief executive officers and their direct reports in organizations that have revenue of $100 million or above (or in the case of not-for-profit or government organizations, having total annual budgets of $100 million or above). This book will not address a small but growing subset of senior executive assessment – board assessment. Typically, board assessment involves the measurement of the composition and mix of a board in terms of knowledge and skills, largely to ensure compliance to governance rules and parameters (although board directors have been asking me recently and more frequently about measuring the decision-making dynamics and interpersonal functioning of a board).

Senior executive assessment is different from assessment at lower levels in an organizational structure in several ways (see the box "How Senior Executive Assessment Differs from Assessment at Lower Levels in an Organization").

How Senior Executive Assessment Differs from Assessment at Lower Levels in an Organization

1. CEOs and boards are the decision-making clients.
2. Duties and responsibilities of those assessed are broader, more complex, and often more substantial.
3. Different characteristics or competencies are important at senior levels (for example, setting strategic direction when faced with ambiguity).
4. Many senior executive position descriptions and contexts are unique. Therefore, benchmarking and statistical analysis using large samples can be challenging. A deep understanding of the unique situation is needed.
5. As clients, CEOs and boards simultaneously expect both rigor and efficiency in assessment methods and reporting.

The Benefits of Senior Executive Assessment

When initiating the business case for senior-level assessment, one approach is to try to prove what many already believe – that the quality of senior executives matters. For example, a study conducted by Weiner and Mahoney[1] examined 193 companies and concluded that the quality of executives related to 44% of variation in profit margins and 47% of variation in stock prices. On the lower end of the continuum and specific to CEOs, Joyce, Nohria, and Roberson[2] found that who the CEO is relates to 14% of the movement in financial results.

Other researchers have tried to illustrate the impact of senior executives by estimating the cost of senior executive turnover or mismatch to a job. According to some research, approximately one-third of executive promotions and hiring decisions are considered a failure.[3] The total cost of executive turnover or mismatch is estimated to be 18 to 47 times that mismatched executive's total cash compensation.[4] This multiplier is likely larger for senior executives in big organizations.

Large business transactions such as mergers and acquisitions (M&A) or private equity/venture capital (PE/VC) investment often involve extensive analysis (due diligence analysis of financials and business processes) before deals are finalized. The emphasis in most due diligence processes is usually not overtly or specifically on people or leaders (although this is changing). This lack of people due diligence can lead to problems and turmoil. In one VC firm's (middle market, $1.3 billion under management) experience in a two-year period, CEOs were replaced in 59% of their investments. While upgrading CEOs is to be expected in a significant amount of VC situations, 59% is extensive.

Regarding M&A, Harding and Rouse at Bain and Company wrote in a recent *Wall Street Journal* article[5] that:

> Rigorous human due diligence helps acquirers get off to a running start. Having done their homework, the new bosses can uncover capability gaps, as well as diffuse points of friction and differences in decision-making. Most important, when critical people decisions are made right away – who stays, who goes, who runs the combined business – an acquired business is more likely to succeed.

Harding and Rouse found that when they took a look at 40 recent M&A deals, "nearly every" acquirer in the 15 deals labeled as successful identified key individuals for retention during pre-deal due diligence or just after the announcement of the deal. Only one-third of the acquirers in the unsuccessful deals identified key employees for retention.

One can extend this analysis by attempting to measure the value of senior executive assessment itself, not just senior executives. In VC transactions, Smart[6] discovered a strong link between the presence and thoroughness of an executive assessment process and the IRR (institutional rate of return) measuring the effectiveness of deals/return on deal investment. He found 80% IRRs in situations involving thorough assessment and under 30% IRRs in situations involving little or no assessment.

Assessment is involved in most rigorous corporate succession programs these days (when there are rigorous succession programs). Byham, Smith, and Paese[7] contrasted company results based on whether succession management programs were "strong" versus "less strong or not strong." They found that 22% of companies featuring strong succession management programs in their sample were in the top quintile in annual return. On the other side of the coin, 13% of companies featuring weaker succession management programs in their sample were in the top quintile in annual return.

Besides examining the relationship between assessment and business results, one could look at whether assessment can promote success in the ultimate criterion in business – execution. Larry Bossidy was Chairman and CEO of AlliedSignal (which became $24 billion Honeywell). Bossidy's career included many successes, much of which revolved around improvements in cost savings and productivity. Bossidy's tenure was highlighted by 31 consecutive quarters of earnings-per-share growth of 13% or more, according to his biography on the company's website. He emphasized seven behaviors as being important for execution success in the book *Execution: The Discipline of Getting Things Done*:[8]

1. Know your people and your business.
2. Insist on realism.
3. Set clear goals and priorities.
4. Follow through.
5. Reward the doers.
6. Expand people's capabilities.
7. Know yourself.

I think it is reasonable to assert that assessment serves as a tool with regard to succeeding in four of the seven behaviors: know your people, insist on realism, expand people's capabilities, and know yourself. Indeed, Bossidy frequently has stressed the importance of effective interviewing and referencing of candidates.

One could argue with the details of these different studies and assertions, but in the end the debate may be a waste of time. CEOs and boards either intuitively are confident that having the right leader in the right place at the right time is important, and/or they know that their job is to always obtain as good a person as they practically can for a job.

The real question was voiced to me recently by the Chairman and CEO of a $5 billion industrial company who is facing the challenge of finding his replacement: how much information is needed by CEOs and boards when making senior executive decisions? My answer to this question is one word: more.

New Expectations about Corporate Governance

A new dimension in understanding the case for senior executive assessment relates to the global shift in perspective about corporate governance. The assumptions about the major corporate failures in the United States during the earlier part of this decade are that poor corporate oversight and undesirable characteristics in senior executives were to blame. While much of the Sarbanes–Oxley Act of 2002 (SOX) in the United States is oriented at a granular level toward finance and accounting, the main themes in this legislation are really about corporate responsibility and internal controls. While not all companies technically are subjected to SOX and there is recent evidence that companies are spending less money on it, SOX and similar legislation in other countries has had a large impact on business policies and procedures.

This impact was best summarized to me by the enterprise head of Human Resources in a $10 billion (in assets) insurance company recently. When describing why he wanted to start a senior executive assessment program, he said that his company's board now "feels the fiduciary responsibility to survey the executive landscape." Fiduciary responsibility. Surveying of the executive landscape. This summary aligns with my observation that boards are now driving increased interest about senior executive assessment. Because boards are interested, CEOs and those who lead Human Resources and Talent Management are becoming more interested in senior executive assessment too (and being put in a position of answering questions about it).

From the board member's perspective, there is clear guidance about the importance of assessment from another important source. The Fifth Edition of the *Corporate Director's Guidebook*, published in 2007 by the American Bar Association (ABA), describes the overall responsibilities of board members. While SOX and this ABA book were written specifically for board members of public companies, much of the guidance can be considered relevant for a private company board member – especially if one is a board member of a closely held company considering an initial public offering (IPO) or facing the general market pressure to comply with the spirit and intent of SOX. Two of the six main corporate director responsibilities enumerated by the ABA relate directly to the need for senior executive assessment:

1. "Selecting the CEO, setting the goals for the CEO and other senior executives, evaluating and establishing their compensation, and making changes when appropriate."

2. "Developing, approving, and implementing succession plans for the CEO and top senior executives."

The *Corporate Director's Guidebook* provides further detail about the board member's assessment-related duties on page 87:

> Consequently, the board must select the CEO with care and due consideration for the challenges facing the corporation. Equally important, the board is responsible for monitoring the CEO's performance over time and must determine whether there is a need for a change in senior management, including the CEO, in light of the CEO's performance and the corporation's challenges.

While the need for attention on senior executive selection and succession is clear, board members appear concerned about their ability to follow through effectively in this area. According to the 2003–2004 governance survey by the National Association of Corporate Directors, directors ranked succession planning as their most important issue. These directors also conveyed that succession planning is the area where they are least effective and need the most help. This is a problem that assessment can solve.

In the *Harvard Business Review*, Ram Charan recommended that:

> Senior executive development should be overseen by the board's compensation and organization committee, which needs to receive periodic reports on the entire pool of potential CEOs and regular updates on those bobbing near the top of it. The committee should spend a third of its time examining lists of the top 20 candidates in the leadership pipeline. In addition, at least 15% of the 60 or so hours that members meet as a full board should be devoted to succession. At minimum, the board ought to dedicate two sessions a year to hashing over at least five CEO candidates, both internal and external.[9]

While making senior-level personnel decisions without rigorous and independent assessment processes may not lead to corporate failure, the risks and downsides I have observed are numerous. Assessment will not eliminate risk, but it will decrease it. The ways in which assessment mitigates risk are listed in the box "Ways in which Senior Executive Assessment Mitigates Risk". Board members in all different types of companies are in the risk management business.

Senior executive assessment helps board members and CEOs be informed about the tradeoffs in executive talent beyond what can be seen in casual observation. It helps decision-makers understand how strong a strength is and how weak a weakness is.

Ways in which Senior Executive Assessment Mitigates Risk

1. Increased detail supporting the defensibility of a decision.
2. Increased understanding as to whether an internal executive is better or worse than an executive outside the company. Assessment professionals can often provide different types of benchmarking.
3. Assessment professionals often drive a clearer understanding of what is needed in roles. Without assessment, a decision process often can be laborious, inefficient, and lacking in focus. This is frustrating in general, but especially when assessment-related decisions are in the press/public eye.
4. Ability to challenge assumptions about what is needed in roles. Assessment professionals can help ensure, for example, that there is not an over-emphasis on industry track record and experience when the situation may not call for this background.
5. Effective assessment pushes decision-makers in their thinking about organizational culture and fit. Without assessment, there can be a lack of clarity regarding whether a successful candidate is supposed to blend into an organizational culture, change it, or both.
6. The communication of development feedback during a candidate's transition to a new role. Without this guidance, successful candidates can miss an opportunity to "hit the ground running."

Summary

Although senior executive assessment has not yet gained universal acceptance among the entire population of CEOs and boards, the evidence obtained to date concerning its usefulness and effectiveness is positive and supportive. While companies have historically focused more attention on evaluating their "hard" capital investments than on evaluating their human capital, this orientation is likely to experience a change in focus in the coming years.

The practice of assessment is strategically positioned to address the needs of a rapidly changing economy and workforce. For example, in the face of economic challenges, decisions about personnel selection and promotion are even more critical as companies look inward to maximize the performance of internal talent. Furthermore, the composition of the workforce and the content of work are changing to address globalization and advances in technology. As a result, companies need a systematic method for gauging whether candidates possess the right combination of skills for leading their teams, setting strategy, and driving performance in a dynamic environment.

Finally, given the increasing rigor being imposed in corporate governance, CEOs and boards are becoming more acutely aware of and focused on effective corporate governance. Executive assessment professionals are able to combine a rigorous scientific approach with business acumen and knowledge of the key issues facing senior executives to help maximize opportunities and reduce the risks facing companies.