A Board Member's "Go Bag" for the Unexpected CEO Termination

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Succession planning and intensive professional recruiting for the C suite are usually thoughtful and systematic endeavors. But preparing for a sudden change in the office of CEO is not an emergency plan a board of directors typically has in place. Here is a "go bag" of basic principles and proven techniques to help board members transit a fast-moving CEO termination.

Understand the Board's Role

Regardless of everyday lines of authority and reporting, executive management is ultimately answerable to the board, which is charged with directing the corporation's business. When the bombshell of a sudden CEO termination hits, the board members in whose laps the matter lands must quickly marshal the facts and rapidly assimilate the legal landscape.

Right away, the board leader managing the termination should assemble the right inside and outside crisis management team (especially for a public company), including outside corporate and employment counsel, a crisis-savvy outside IR/PR professional, and a very few critically chosen and trusted members of management. Strict confidentiality is paramount for any management "brought over the wall."

Address Each and Every Legal Relationship

A CEO holds multiple legal relationships with the company. As an employee, his or her termination must comply with all laws governing employment terminations (right down to the technical requirements for calculation, preparation and delivery of the final paycheck, payment of accrued vacation, and termination or continuation of benefits).

The CEO is also a corporate officer appointed and removable by the board in accordance with the bylaws. The CEO often holds various officer positions with a company's subsidiaries and other affiliates, which should not be overlooked.

A CEO typically is also a member of the company's board and possibly one or more subsidiaries or affiliate companies or entities. Unless a CEO's employment agreement includes an automatic resignation from all board seats and officer and other fiduciary positions upon termination, board removal can become an irksome bargaining point. Boards cannot simply remove their own members, no matter what, and convening a shareholders meeting to effect a director's removal is inherently cumbersome and impractical (and for removal from a "staggered" board of a Delaware company, the applicable statute requires "cause").

Finally, take a look at the company's debt documents. A CEO termination might breach a financing covenant or trigger a "change in control" absent a waiver (and many times waivers are not free!).

Inform the Board and Formulate the Offer

A protracted fight with an embattled CEO in the public eye is seldom in anyone's best interest. As soon as the board leader has a good handle on the factual and legal bases for termination, the non-executive members of the board should be contacted to let them know of the circumstances, gather their sentiment, and assure them they will be kept regularly apprised.

Again, confidentiality is key and should be explicitly reinforced. A CEO knowing or sensing an oncoming termination will often seek out a presumed "ally" on the board to attempt to serve as a go-between. Considering possible litigation, differences within the board should be resolved through discussion, with professional advice. Dissenters are plaintiffs' counsels' best friends.

A threshold issue is whether the termination, if involuntary, will be "for cause" or "without cause" - typically contract-dependent determinations. Termination "for cause" raises the stakes for both the company and the CEO and may have profound financial and reputational consequences.

A variety of motives may initially cause some directors to favor a "for cause" termination. In most cases, however, an expeditious but consensual exit serves the best interests of the company and the shareholders. If done on an informed basis and after due deliberation by a board with an independent majority, the so-called Business Judgment Rule (BJR) should protect the board's decision to terminate the CEO, even if the pre-negotiated separation package is substantial and the tenure before termination is short.

The CEO's employment agreement should provide the basic framework for a prompt and defensible negotiated outcome. However, a brand-new separation agreement can help to draw together all elements of the separation, accommodate any negotiated changes, and underscore the CEO's post-separation obligations of confidentiality, non-competition, non-solicitation and, perhaps, non-disparagement (though the last of these, if made mutual, can be a two-edged sword and so perhaps not worth including).

A release of all claims, for the benefit of the company and its board, officers, employees, and shareholders is a must. If the CEO's employment agreement does not provide for a release as a condition of separation benefits, the board should still insist on one and stoutly resist any attempt to make it mutual. Later revelations of wrongdoing with remedies foreclosed by a release could be uncomfortable for a board and detrimental to the company.

Tax counsel should be consulted to confirm whether the tax code imposes any limitations on severance benefits and to confirm that any underlying employment documents do not raise tax compliance concerns.

Draft a press release early on in the process and present it as part of the separation offer. Don't leave it as a last-minute item. Use the experienced external IR/PR adviser you have included on your crisis team.

Equity issues must be addressed. A termination will invariably impact vesting and exercisability of equity awards – and the nature of the termination ("for cause" or "without cause") will frequently dictate how those awards will be treated.

Finally, the board (whose non-executive members should be fully supportive before a termination meeting with the CEO is held) should consider the manner of carrying out the termination. Here are some pointers:

- Schedule a meeting with the CEO outside the company's office.

- Be respectful and avoid an aura of ambush if that is possible.

- Have a second board member (someone the CEO respects as a "straight shooter" and a "friend" and not there presumably as just a potential litigation witness) attend and actively participate in communicating that the board believes it is time for the CEO to leave the company.

- Do not leave any impression that it is the beginning of a negotiation process of indeterminate length regarding whether the CEO will depart.

- Deliver the whole package and give a finite but reasonably sufficient time (like 48 to 72 hours) for the CEO's review with the assistance of his or her counsel and time for the CEO to cycle from denial and defiance to acceptance and cooperation. Keep in mind that employment laws may dictate the timing of the execution of a separation agreement.

- Use a weekend to everyone's good advantage, if the termination will occur on or next to one.

- Strictly interdict the CEO's access to the company's premises and any conversations he or she might be tempted to have with other company employees pending a resolution.

- If for good reason the termination must be immediate, the board's representatives should require the turning over of keys and electronic access cards at the termination meeting and specify to the CEO the process for collection of all company property (computer equipment, cell phones, company vehicle, etc.).

- Promptly after the termination meeting, and after having told the CEO it will be done, order the disabling of the CEO's access to the computer and telephone systems (authorization codes), the withdrawal of signing authority (for bank accounts), and the cancellation of any company credit cards.

- Attend to public company disclosure requirements (if you are one) after termination.

Call the Board Meeting

One way or another, a board meeting, or more than one, will be needed. If the CEO is a board member, don't exclude the CEO entirely from any board meeting (but do exclude his or her counsel if counsel's presence is requested or demanded). Courts disfavor using trickery to entice a CEO who is a board member to attend a meeting at which he or she will be terminated without prior notice of the action to be taken. Follow proper corporate procedures to call an executive session of the board and conduct it prior to the start time of the board meeting (or thereafter by recessing the board meeting at any time or times at which an executive session would be useful). Adopt a resolution to accept a resignation under stated basic terms with some leeway for the board's representatives to vary the terms or, if a negotiated outcome is beyond reach, to effect a termination on stated terms. Appoint an interim CEO or authorize an executive chairman to lead the company on an interim basis.

Readiness is Key

Being prepared is the first step in a thoughtful process most board members hope they will never need. Sudden exits by CEOs can come about in several ways and all present their challenges. But being ready for all of them is a worthwhile endeavor – and perhaps a fundamental board obligation.

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