



# Best Practices for Selecting, Working with, and Separating from Hospital CEOs





The strength of a hospital, as with any organization, often is directly related to the competency of the CEO and the health of the relationship between her and the board of directors or trustees. It follows, then, that hospital boards should have policies in place that dictate how they will recruit CEO candidates, how CEO employment agreements are structured, how to work with and evaluate CEOs, and even how to initiate termination proceedings. Although there is no single correct policy or formula for any of the above considerations, there are certain guiding principles hospital boards should keep in mind when deciding what is best for their hospital.

## CEO Search Process

When a hospital begins the search for a CEO, it should take its time to assess what went wrong with the previous CEO, what candidate qualities should be prioritized, and whether the board wants to search in-house or retain an executive recruitment firm. Before any candidates are contacted or evaluated, the board should have a clear picture of the ideal candidate. That way, the board can circulate a call for applications with specific criteria and select the candidate from a pool of applicants that most resembles that picture. Doing this accomplishes two objectives: (1) the board does not waste time with applications from clearly unqualified candidates, and (2) the board has a better chance of hiring the best person for the job rather than the best person from a given applicant pool.

Once the ideal candidate criteria is established, the hospital board next must decide whether it wants to promote from within or retain a third-party recruitment firm. The advantages to hiring from within are obvious – e.g., savings on money and time, the potential CEO's familiarity with the organization and its employees – but boards would be wise to discuss the idea of hiring a third-party to conduct the search for them. These firms may cost more money, but in many cases it can be a worthwhile investment to make, especially if the hospital is located in a small, remote community.

Whatever option a board chooses, once a decision is made on a candidate, the next step is to negotiate a CEO employment agreement. And it is at this stage that the hospital board should take advantage of the opportunity to remedy any of the problems it had with its previous CEO.

## Contract Negotiation and Essentials

Employment contracts and routine performance evaluations of

an organization's CEO are two important mechanisms that hospitals can use to retain qualified CEOs. Employment contracts should identify the CEO's role with the hospital as well as provide the CEO with some autonomy to make tough decisions without the fear of being subjected to arbitrary termination. Some common elements to consider in the CEO Employment Agreement include:

- **Duties of the CEO.** The duties should be expressed in comprehensive and specific terms, since the CEO should be involved in every area of hospital operations.
- **Financial terms and benefits.** The contract should identify the salary, bonus, and any other benefits (e.g., health insurance, life insurance, vacation allowance, payment of professional dues, car/phone allowance, etc.) the CEO will receive.
- **Term.** If the agreement will last a specified period of time, then that period should be included. Likewise, it should state whether the term will be automatically renewed and, if so, how long the renewal periods are.
- **For-Cause Termination.** Clear "for-cause" termination provisions are essential to any employment agreement. The board should also consider whether these provisions, when breached, will result in immediate termination or whether an opportunity to correct course should be provided prior to termination. Common for-cause termination provisions include: (a) misconduct by CEO; (b) continued failure to perform duties/insubordination; (c) conviction of a crime; (d) failure to comply with hospital policies; and (e) other material breaches of the employment agreement.
- **No-Cause Termination.** "No-cause" termination provisions are common and should provide enough time for the hospital to find a suitable replacement CEO. Typically, the CEO will expect some form of severance if the hospital elects to terminate without cause, so it is important to identify the terms of any severance.
- **Mediation; Venue; Governing law.** Requiring that the parties mediate prior to litigation is becoming increasingly



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common and should be considered by the board. Mediation is a non-binding dispute resolution procedure that provides an effective way to settle disputes outside of the courtroom. If litigation is pursued, however, then the agreement should provide both the state law that will govern the dispute and the county where the litigation must initiate.

Although duties, term, termination and dispute resolution provisions are crucial to a successful, functioning employment agreement, the contract item most likely to stall negotiations tends to be how much the CEO will be paid. When negotiating compensation, hospital boards should understand the market rate for CEOs, and should explore creative ways for structuring benefits and pay.

### Compensation

While salaries for hospital CEOs vary greatly from organization to organization, pay appears to be increasing across the industry. According to a report by The New York Times, hospital executives in 2013 earned an average annual salary of \$386,000 (excluding bonuses or other incentives). Another 2013 study found that the average CEO earned approximately \$600,000 per year. According to this study, however, the average salary for a rural hospital CEO was \$118,000, while the average salary for a large teaching hospital CEO was about \$1.7 million. Given these significant variances in salaries, boards should do their due diligence on CEO compensation prior to making an initial offer to a CEO or increasing the salary of an existing CEO.

The contract should also address time spent by the CEO away from the hospital, including vacation, sick leave, holidays and other business. There are countless ways to structure the CEO's paid time off. For example, will the CEO be bound by a paid time off policy which applies to all employees or will she be entitled to additional days off? How often will the CEO be permitted to attend professional meetings and conferences? Who will pay for these expenses? Will there be a cap? Paid time off provisions in a CEO's employment agreement are largely business decisions to be made by the board, but these business decisions can quickly turn into legal issues if they are not clearly outlined in the contract.

Finally, the contract should address the CEO's bonus, if any. According to a 2018 report published by Total Compensation Solutions, 76 percent of hospitals said they pay their CEO a bonus, with the average bonus for a hospital CEO around 33.2 percent of their base salary. Most hospital CEO bonuses were tied to achieving pre-deter-

mined financial goals. Although this method remains common, many hospitals have implemented bonuses tied to quality metrics. The board may want to consider a bonus tied to other performance measures, such as patient satisfaction, survey results, employee satisfaction, or any other issue critical to the success of the hospital.

Once compensation is agreed upon and the contract is in place, the board should focus on developing a working relationship with its new CEO, which requires a clear idea of what roles the board and the CEO are expected to play. This, in turn, involves establishing clear lines of communication and trust.

### Understanding Obligations

The board-CEO relationship requires open communication, not only so each party can understand its obligations, but also so that each party can comfortably approach the other if any issues arise. Communication from the board, to start with, should consist of a candid conversation with the CEO about what the board expects from the organization and from the CEO herself. These expectations should be coupled with the performance metrics that the board will use to determine whether its vision is being fulfilled.

Communication from the CEO should consist of a general plan on how she intends to accomplish the goals laid out by the board. Importantly, the board should resist any temptation to control the CEO's implementation plan. After all, the CEO's expertise is in making an organization's broad, general vision a reality. The CEO has access to day-to-day operations and financial data, so at least some deference is warranted. This does not mean, however, that the board should not ask questions about aspects of a CEO's plan that some of its members may not understand. Without a complete understanding of what each party is trying to do, signals may get crossed, and board members and the CEO may end up talking past one another.

Establishing trust between the board and the CEO should be relatively easy once the lines of communication are open, as long as each party is remaining faithful to their originally stated goals. One way to ensure this is the case is through periodic evaluations. Hospital boards should develop and implement a process for providing feedback to the CEO and evaluating progress on achieving objectives. At a minimum, these evaluations should be done annually with full board participation and should examine criteria such as: (a) net operating margin (i.e., bottom line); (b) quality of care; (c) patient satisfaction; (d) physician relations or engagement; (e) strategic planning; (f) board relations; and (g) compliance with regulations. Once the review



is complete, the board should share the feedback with the CEO, along with ideas for how to improve.

Sometimes, though, these performance evaluations or other events may necessitate a change at the CEO position. Knowing this, boards should have a plan to address these situations.

## Termination of Employment

In the event it is necessary to terminate the employment of an organization's CEO, the board should work with the organization's legal counsel to assure compliance with all laws and relevant agreements. Before termination, the board should review all documents relating to the CEO's employment and benefits to determine what steps must be taken to end the employment relationship and what consequences will result from termination.

Many CEO employment contracts include a provision for payment of severance upon termination of employment without cause. Severance may be structured as a lump sum payment or a payout over a stated period of time. It may also include continued payment of benefits, such as health insurance, over a period of time. The organization should require the CEO to execute a written agreement releasing all claims in exchange for the payment of severance. The agreement should also include provisions regarding non-disparagement by both parties and confidentiality of the terms of the agreement to the extent permitted by law. Boards should consult with

knowledgeable legal counsel to prepare a separation agreement to ensure compliance with relevant employment laws, in particular the Older Workers Benefit Protection Act, which contains specific criteria for release of any age discrimination claims.

Board members may find it helpful to prepare a script for the meeting at which the CEO's employment will be terminated, particularly if it is expected the CEO will react poorly. The directors or trustees involved in the meeting should ensure that organization property and information is properly secured. The board should arrange with a trusted member of the organization's staff (chief operating officer, chief financial officer or other) to have the CEO's network access and passwords disconnected. The CEO should be required to return keys, credit cards, and organization technology (e.g., phone, laptop, etc.) immediately. The board can give the CEO the option of packing up his/her office with supervision or having the CEO's personal items packed and delivered to the CEO at a later time.

The board will need to appoint an interim CEO to manage the organization's affairs while a search is conducted for a new chief executive officer. An interim CEO can be appointed from within the organization or through an executive placement firm. The interim CEO, in conjunction with the board, should notify organization employees of the CEO's departure from the organization and assure the workforce of a smooth transition. And at that point, the search process can begin again.

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