

# The Board And Effective Succession Planning

by Randall S. Cheloha, Ph.D.

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The basic role of selecting the company's chief executive imposes significant responsibilities on directors. Unless the board is able to take responsibility for CEO succession, implement a sound evaluation and grooming process, and make it part of a total talent development plan, it leaves the future leadership of the corporation to chance.

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The prominence attained by chief executive officers in the United States over the last decade makes succession front-page news. *The Wall Street Journal* comments frequently on the heirs apparent to Jack Welch at General Electric Company. The death of Frank Wells at The Walt Disney Company created a power struggle that ended with Jeffrey Katzenberg departing to start a competing studio, DreamWorks SKG. More recently, the acquisition of CBS by media giant Viacom has prompted speculation about Sumner Redstone and whether the 75-year-old CEO is poised for retirement or just entering his prime.

Succession is about maintaining the continuity of a company and its values. There is no more compelling or critical corporate drama.

What makes succession so critical to corporations and their leaders, and so intriguing to observers? In part, it is the raw transfer of power and the attendant fortunes to be made or lost, but there is more. Succession is about maintaining the continuity of a company and its values. In the life of a company, there is no more compelling or critical drama than the identification of a successor to carry on and lead the work of the enterprise.

This issue is a constant concern for founders of family businesses who wonder about the ability of their sons and daughters to succeed them with the

inheritance of future generations on the line. Surprisingly, the reality is much the same for the chief executive officer of the *Fortune 500* company. Leaders of all types of companies face heavy responsibilities in the nomination, grooming and selection of successors.

Despite the media attention and the frequent public discussion of succession, the actual processes of planning for succession are not well known. There are several reasons for this. In most companies, the details and mechanics of succession are private and remain private.

This is true for both public and private companies. Board members and CEOs are extremely reluctant to reveal the machinations that went into producing a successor. By being open about the process and their decisions, it becomes more difficult to change their minds when business conditions change, or a newly discovered weakness in the chosen successor becomes evident.

Boards are particularly closed-mouthed about the process when the chosen successor fails, which happens more frequently than many wish to acknowledge. According to a *Harvard Business Review* study by Ciampa and Watkins, of 35 organizations in 1992 that chose an outsider for COO (the most likely successor candidate), only 25 percent of the candidates became CEO within the next five years. Hence, a 75 percent failure rate.

Another reason for the lack of information about the succession process is that institutional memory is limited to a few long-serving board members present during the last succession. Like the hierarchy of a receiving line at a state funeral, it may have been many years since the king or leader died in office, requiring that protocol briefing books be consulted to refresh memories.

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Finally, the standing CEOs represent the latest product of the corporate succession process, but may have little insight into the behind-the-scenes maneuvering that led to their ascension. These critical decisions most likely were made by others who have retired or, if still active in the company, may be reluctant to reveal detail. Clearly, guidelines to aid board members and current CEOs are lacking.

Six basic principles can help overcome these challenges and establish an effective succession planning process that supports ongoing success. These "hallmarks" of effective succession planning apply to any organization—large or small, publicly traded or privately owned, for-profit or nonprofit.

The board "owns" the succession process and the CEO "manages" it.

The board should be in a position to make informed judgments.

Succession planning is supported by strong leadership development.

Leadership is defined.

Potential successors are assessed as leaders.

Successor candidates have development plans that "live."

These principles are key to helping identify and prepare successful candidates, as well as limiting the inherent risk of being forced to choose an outsider to lead.

*The board "owns" the succession process and the CEO "manages" it.* This principle is counter-intuitive to many board members, who feel removed from day-to-day operations and the executives who run the company. Some CEOs shield their directors from succession candidates by failing to provide opportunities for board members to interact with these candidates.

Whether consciously or unconsciously, CEOs often fear the successor candidate will appear more capable. Or, they believe the succession decision should be their decision as the most senior official of the company. However, the time perspective of the CEO differs from that of the board. The CEO's concern is the next company transition while the board's concern is perpetuation of the corporation for the long-term.

From a fiduciary perspective, the role of the board is to ensure an effective succession planning process (and successors) are in place. Some boards are unable to execute succession planning because they lack power, serve at the pleasure of the CEO or lack critical knowledge and information. When the current CEO leaves, the board is then forced to react to circumstances.

Consider International Flavors & Fragrances, Inc., a \$1.4 billion dollar flavor and perfume manufacturer. When long-standing 70-year-old CEO Eugene Grisanti announced his retirement, board member Richard Furlaud—age 75—was named interim CEO. Does this suggest the lack of an internal successor? Perhaps.

Compare this situation to the recent death of the president of Wendy's International. While what happened behind the scenes was not discussed publicly, a few months later the board announced an internal successor, John Scheussler, former president of Wendy's parent company and chief operating officer. The stock price for Wendy's has remained stable.

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Straightforward succession decisions are frequently complicated by powerful underlying emotional factors. Succession for the CEO means acknowledging one's passing—handing over the reins to another and, at some level, acknowledging mortality.

This emotional entanglement leads to poor or even failed judgments about potential successors. Many CEOs are unable to relinquish power since their identities and roles have become one and the same. Consider Armand Hammer at Occidental Petroleum Corporation, an example of a prominent CEO who had a hard time stepping down because over time he had become synonymous with the company.

This issue is even more pronounced for the boards of companies where the current CEO also founded the company, such as Bill Gates at Microsoft, Michael

Dell at Dell Computer, Ted Waitt at Gateway, and Herb Kelleher at Southwest Airlines. Each of these leaders built their own companies, which reflect their identities. These CEOs hand-selected most, if not all, of the company's key executives.

However, if managed properly, this situation does not automatically create a barrier to effective succession planning. For instance, the transition of power has started at Microsoft, where Bill Gates has handed over significant responsibility to COO Steve Ballmer, who has had a significant role in reshaping the company's strategic direction.

CEOs are in the best position to judge successor candidates. However, the board's role is vital: to render an independent, objective decision on the candidate.

Standing CEOs are in the best position to work with and judge successor candidates in diverse business settings and circumstances over time. They have contact with high potential talent at distant locations. They alone know the unique challenges and pressures of the job. The board's role is clear as well: to render an independent, objective and emotionally unclouded decision on the successor candidates. Ultimately the board must retain oversight and veto power.

*The board should be in a position to make informed judgments.* To be successful at this they must have access to successor candidates. The CEO needs to provide board contact with potential successors in both social and business settings so directors become familiar with the candidate's leadership style, track record and social skills.

Access to the successor candidates is not enough, however. Directors must have access to the candidates and the business context. Without a clear sense of the company's purpose, direction, strategy and challenges, the board renders its opinion in a vacuum. It is enormously helpful if the makeup of the board represents diverse and relevant business and organization backgrounds for a broad experience base from which to make judgments.

Unfortunately, many companies lack experienced boards who are willing to take action when they see problems. Perhaps their inexperience prevents directors from sensing problems when they exist. Some board members are friends, former colleagues or social associates who serve at the CEO's pleasure. Others lack business/industry experience and are virtually unaware of the competitive environment and pressures the CEO faces daily. And still others prefer not to ruffle feathers or speak up, even when they see undeniable problems.

Many board members have bits and pieces of all these attributes. These boards become dependent on the CEO's judgment about successors rather than form their own opinions. They are too far removed from the action to have meaningful involvement with the company other than formal reports.

To avoid this trap, CEOs must work to ensure their boards serve as a counterbalance to their own leadership—a sounding board of individuals willing to speak up and challenge them. When the board and CEO work together, the odds of identifying and developing a strong successor increase, and the process is grounded in the realities of the business.

Succession planning is not the same as leadership development. Unfortunately, many companies assume that they are the same.

*Succession planning is supported by strong leadership development.* Both succession planning and leadership development enhance leadership. However, these processes are not the same. Succession planning is about preparing someone to assume the CEO role, period. It focuses on a handful of internal or external candidates. The process can be transparent and public, or it can be known to only a select few. Companies may ignore leadership development (and many do) but this does not release the board from the responsibility of having a successor in place.

However, more progressive and sophisticated firms realize that strong leadership development becomes the launching pad for succession planning. Unfortu-

nately, many companies assume that by doing one they are doing the other, ignoring the distinct differences. Effective leadership development does not happen overnight or through good fortune. It takes a huge commitment of time and resources to build and sustain an effective leadership development program and the supporting culture that goes with it.

Leaders like Larry Bossidy, former CEO of Honeywell International, and Jack Welch at GE view leadership development responsibilities as core to the business' success. Welch devotes at least 50 percent of his time to the process, while Bossidy makes leadership development one of three key business processes linked directly to the strategy and direction of the company.

Consider the new CEO of a large Southeastern manufacturing company. He realized during the first six months of his tenure that none of his subordinates had succession potential. This could have been anticipated since the board made a point of recruiting him from outside the company. However, a close examination of the company's leadership development and succession planning process revealed that it had been largely neglected. The CEO, with board support, installed a process to identify and develop future leaders including grooming a successor.

Companies that focus solely on meeting the "letter of the law" by preparing a succession plan, while ignoring leadership development, find that they are penny wise and pound foolish. Such a succession plan merely summarizes a brief discussion between the CEO and the board. Another plan lists the names of individuals who can develop over a three to five year time frame to become CEO.

Many of these plans are superficial. They are based on a positive experience with the successor candidate in a recent meeting, contaminated by political halo and individual bias. They reflect what the CEO role requires now with no consideration for how things will change in the future. The succession plan commits these discussions to paper, generally with the endorsement of the chief human resource executive. These companies later find (often during a crisis) that under serious examination none of the candidates measure up to what is really needed.

Earlier this year the board of the Campbell Soup Company "un-retired" the former CEO, David Johnson, and returned him to the helm of this \$3.7 billion food company. During his tenure, Johnson had turned around the company, but his successor was unable to continue this legacy. Johnson's return acknowledges that there was no internal candidate prepared to assume the leadership role.

□ *Leadership is defined.* While most companies devote extensive efforts to setting clear financial and performance targets, many fail to define leadership. Leadership is a soft concept: "I don't know what it is but I know it when I see it." Admittedly, there are many legitimate interpretations of leadership, and different styles are better suited to one company than another.

A strong and dynamic leader in the steel industry, for instance, would fail at a service organization because of the huge differences between the two cultures in managing people. Harold Geneen was legendary during his tenure at ITT Industries with his command and control, "always keep them guessing" leadership style. This style would fail horribly in the majority of the new e-commerce startups.

Regardless of the definition of leadership agreed upon by senior management, they must make it work and communicate it to others. The company must wrestle with what leadership means to them. Through this process it distills important values that help clarify what is sought in CEO candidates. Failing to define leadership leads to confusion, ambiguity and, eventually, an acceptance of mediocre leaders.

The board brings a long-term view to assessing successors as leaders, but needs regular exposure to candidates to properly make this assessment.

□ *Potential successors are assessed as leaders.* The board's view here is long-term. Can this candidate shoulder more broad and senior responsibilities? Does she have the impact and presence to lead this company? Does he have the intellectual capability to deal with the complex challenges the company

will face? Can this person work collaboratively with the board?

These assessments take place naturally on a daily basis through the course of running the business and social contacts. The best way to judge a candidate is by observing performance on the job. These experiences are limited for board members, whose contact with senior executives typically occurs in the boardroom.

Yet there are many ways to engineer contact between executives and the board. These include informal and formal reports to the board, annual one-on-one meetings between directors and senior leadership on significant matters, and social events where executives mix with board members in a relaxed and informal setting.

However, informal assessments made by inexperienced judges are notoriously weak and influenced by all forms of rating bias. These calls become even more subjective when the firm lacks a formal leadership definition.

To counteract these tendencies, conduct a formal talent assessment at least annually. These assessments serve the dual purpose of providing developmental feedback to successors and detailed input to the board on successor candidates. The actual assessment can be performed by outside consultants who are acquainted with the company, its culture and strategy. Internal managers may also be trained to look for the "right" behaviors and can screen out political biases.

For example, a large European-based consumer products company assessed its top managers annually. They defined the desired leadership behaviors and developed an assessment process to measure them. Managers were sent to Johannesburg, Hong Kong, Miami or London, where an experienced panel of internal human resources managers and external consultants interviewed them. The outcome was a summary report on each candidate's strengths and weaknesses reviewed by the CEO and discussed with the board.

Often, such assessment requires tough decisions. Founding CEO Ted Waitt of Gateway believed his company, which had grown to a market cap of

approximately \$17 billion, was stagnant. He had personally hired most of his executives. Waitt contracted with a psychologist who conducted an extensive assessment of his top executives, including in-depth reviews of their experiences since high school. Their co-workers were interviewed extensively as well. Based on the findings, Waitt dismantled his top team and recruited new talent replacing 10 of the company's top 14 executives.

Succession candidates should undergo a rigorous periodic assessment of their potential to become CEO. Candidates should be judged against the *future* leadership profile of the company and not against the current CEO's profile.

**Shaping a good succession development plan is more an art than a science. It must remain dynamic and alive.**

*Successor candidates have development plans that "live."* The development plan is a brief summary that catalogues successors' strengths and weaknesses. It becomes a blueprint for the CEO and others. Creation of this development plan is more an art than a science. It helps the successor focus on action steps to provide new experiences that stress areas of concern. The challenge is to create a development plan that is dynamic and alive—one that addresses core development issues.

A CEO candidate with an explosive temper is a good example. Although his outbursts had lessened over the years, they emerged during stressful meetings while running a major operating division. Directors and the CEO were uncomfortable, knowing his temper might re-emerge at any time.

To address this issue the candidate was informed about his strengths and weaknesses, an executive coach was hired to work with him on his temper, and board members were briefed about his development needs. The good news is that the combination of the focused attention on the candidate's weakness and external coaching had the desired effect. The candidate learned to deal with his temper and kept his career on track.

A living development plan places the candidate in business situations that provide learning opportunities to meet development needs—opportunities that do not occur in a classroom or seminar. For example, a key challenge for most CEOs is building collaborative relationships with the board, particularly the board chair. This occurs at board meetings that take place at the corporate headquarters, which has its own unique culture.

The top successor candidate at a high-tech company based in Chicago successfully ran a major facility located 1,100 miles from corporate headquarters. Distance made it hard to build relationships with the board and board chair, as well as the senior function heads.

As part of the candidate's development plan, the company created a new position at headquarters that placed him in contact with directors who rarely

journeyed to outlying facilities. As a result, this executive became familiar with the headquarters culture, and developed working relationships with board members and other senior managers.

Healthy succession planning is central to a company's ability to sustain itself and survive. It helps define the company's leadership values, and then identifies and develops those leaders. By following this process, the CEO and the board are in the best position to identify and develop the most capable future leaders. By ignoring succession planning, the firm places itself at risk, and the risks are substantial.

Most successful CEOs and directors and the companies they run did not achieve success by relying on chance to determine their fortune. Effective succession planning dramatically increases the probability of a successful leadership transition, paving the way for the future success. ■