PDI Ninth House
GLOBAL LEADERSHIP SOLUTIONS

WHITEPAPER

Getting Succession Right

Six Essential Elements of Effective Succession Plans

Succession Plan? Uh . . . Do We Have One?

Succession is a perennial and important issue for organizations. Even so, 50 percent of organizations with annual revenues of $500 million or more report having "no meaningful succession plans." Why is that? What makes succession so hard to get right? What keeps organizations from creating succession plans that work? And what can you do about it to start your organization on the right path to readiness?

It's not a new story by any means. Succession planning is one of the hardest HR processes to get right. We've seen the headlines all too often about messy, protracted, clumsy, embarrassing, and highly visible succession failures. We've seen companies stagger under the upheaval from too many changes at the top. For example:

- Morgan Stanley's board let former CEO Phil Purcell force out agreed-upon successor John Mack and then purge most of Morgan's top leaders. Only protests from former executives pressured the board to bring Mack back to put its house in order.
- Home Depot's board passed over its executive team to recruit GE superstar Bob Nardelli, whose lack of understanding of the retail business led to market share losses. Outside pressure resulted in Nardelli's replacement by Home Depot insider Frank Blake.

Fifty percent of organizations with annual revenues of $500 million or more report having "no meaningful succession plans."

If you think these are exceptions, think again. If 50 percent of the big organizations who have the budget and resources to devote to succession have no salient succession plans, then you can only imagine what the scenario looks like for smaller companies. Big or small, is your organization one of them?

Alarming Statistics Hit the Bottom Line

As if not having a plan isn't enough, statistics also show that 40 percent of new CEOs fail within the first 18 months on the job. No wonder people are beginning to call CEOs "the most expensive temp employees in the world!" Clearly, succession—good or bad—has a tremendous bottom-line impact on organizations and is just as important as any business problem faced in today's challenging business environment.

This isn't just an HR issue. It is a vexing, thorny business issue that has the same kind of bottom-line implications that all business issues do. Consider the analysis done by Forbes Financial Columnist, John W. Rogers, Jr.[1] Rogers identified 440 organizations that had been part of the S&P 500 for the past decade. The average tenure for the CEOs who headed these 440 companies was just 4.3 years. This means that on average, these companies had more

[1] John W. Rogers Jr., "A Steady Hand," Forbes, April 7, 2008.

than two CEOs over the past decade. Think about that. Think about the change it implies, the lost continuity, and its impact on the bottom line. Over the decade, the average annual return for the stocks of these 440 companies was 12.2 percent. That's a very respectable return, especially considering the business environment of that period. However, and this is where it gets interesting, 42 of those 440 organizations had the same CEO for the entire decade and the average annual return for the companies with the same CEO was 18 percent—nearly 50 percent more than for the less stable cohort. Think about that. Every dollar invested in the 440 companies would have nearly tripled by the end of the decade. The same dollar invested in the 42 companies would have more than quintupled!

Organizations cannot afford the costs associated with poor performers. Also, with the increasing demand for higher-level skills, they cannot afford to lose valuable senior leaders. In today's economy, it can be fatal to put the wrong people in key roles. Anything less than the best may make the difference between real market victory and competitive parity.

Succession: A Noun That Should Be a Verb

What's interesting about all of this is the irony. New CEOs fail at an alarming rate. Just reading about the mangled successions is embarrassing. The bottom-line value of churn at the top of the house is tremendous. And yet, 50 percent of organizations who are, by any standard, big enough to know better—50 percent—report having no meaningful succession plan.

How do we reconcile this? When it comes to succession planning, why is it that we seem so much better at talking the talk than walking the walk? What makes it so hard to get succession planning right? One thing that doesn't help matters any is the fact that succession is a noun, when in reality it should be a verb.

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Suc-ces-sion (sək-'se-shən)

Noun:

1. The order in which or the conditions under which one person after another succeeds to a property, dignity, title, or throne.
2. The system or process by which business leaders ensure a ready and sustainable supply of the right leaders in the right place at the right time to achieve short-term objectives and long-term goals.

Nearly every organization has some form of "right people, right place, right time" as part of their HR mission statement. No doubt, if you take a look at yours, you'll find something similar. It's difficult to argue with. After all, who wants the right people in the wrong place or at the wrong time? And who would ever want the wrong people in any place at any time? It's hard to argue against succession planning as it is typically defined. But the evidence we have summarized suggests that few organizations are doing anything even approaching a good job with succession planning. Why is something so difficult to argue with so poorly executed? In large part, it's because the definition is 99 percent aspirational and less than one percent prescriptive. It tells us what we want to accomplish but provides scant guidance about how to proceed. It is difficult to impossible to tell from the definition where to dig in or exactly what needs to be done to accomplish the right people, right place, right time goal. Market research and conversations with many PDI Ninth House clients have been clear that a more structured, ground-up approach to succession planning would be helpful.

Six Essential Elements Make Succession Planning Tangible

If you look carefully and deconstruct the classic definition of succession, you can discern six essential and, more importantly, actionable elements:

1. To ensure we have leaders in the right place, we need to know where they will be needed. We need to identify target roles and positions.
2. To ensure those leaders can achieve short-term objectives and long-term goals, we have to determine the requirements of the target roles and positions, and how the requirements of those roles support the mission and strategy of the organization.
3. To ensure we have leaders at the right time, we have to know when they will be needed. We need to assess the risk and impact of turnover in the target roles and positions.
4. To ensure we have the right leaders, we have to identify succession candidates and assess their ability to effectively perform the target roles.
5. To ensure a ready supply, we have to build and execute development plans to close any gaps identified by the assessments.
6. To ensure a sustainable supply, we have to be systematic in our approach and revisit and update succession plans periodically lest the process revert to the frantic, mad scramble it too often becomes when a key organizational role suddenly needs filling.

When it's organized like this, the task of building succession plans seems much more straightforward and easily tackled, doesn't it? The next thing to do is look at the choices and options for how to accomplish each step. Let's start with identifying target roles and positions.

Identify Target Roles and Positions

Often it is easiest to start by identifying the obvious roles and expanding your list until you run out of choices or appetite.

ORGANIZATIONAL IMPACT

What makes a role or position succession worthy? In a word, it's organizational impact. The target roles and positions included in your succession process should be those where getting the right or wrong leader in the role will have a big impact on organizational performance. There are a number of rules of thumb you can use to identify high-impact positions. The most obvious is organizational level. Jobs at higher levels (vice president, senior vice president, executive vice president, C-Suite) have more opportunity to impact the overall organization than those at lower levels. Not every high-level role has the same degree of impact, but generally the higher the level, the greater the impact.

A slightly more subtle version of organizational level is the ratio of job holders to job titles. The ratio for CEO is 1:1— one job holder to one job title. For vice president it might be 3:1 or greater. In large retail organizations, the ratio for store managers might be 500:1 or more. The closer the ratio of job holders to job titles is to 1:1, the greater the need for succession planning. For the most part this ratio will co-vary with organizational level, but not always, such as a chief scientist for a pharmaceutical company.

Other factors that influence the organizational impact of a job are job size and accountability. If you use a job evaluation-based compensation system (e.g., "Hay Points") then you will understand that the same factors that influence a job's "size" influence the impact of the job.

STRATEGIC AND TACTICAL IMPORTANCE

Other factors to consider are the role's strategic or tactical importance. Strategically important jobs are those that are critical to your business strategy. Merchandising jobs in retail organizations often have strategic importance. The decisions that a merchandiser makes today can make or break a retail season. Senior-level professional/technical roles often have strategic importance in high-tech industries like pharmaceuticals, software, or electronics.

Succession processes often also include lower level, but tactically important positions. Regional or district manager roles in a region with emerging local competitors, or the store manager for a company's flagship location can be important enough to warrant inclusion on your list of target roles and positions.

Common choices of positions included in succession planning processes are the obvious ones like C-suite roles. Many organizations expand this list to include the top 25, 50, or 100 roles in the organization. Pivotal roles have strategic importance, but don't forget to think about roles or positions that are emerging in importance or that are likely to become important as a result of changing strategy or turbulent economic times.

HOW MANY ROLES TO INCLUDE?

The question of how many roles or positions to include on your list is largely a pragmatic one. As you have surmised, doing all this work consumes time and resources. One key question: what does your budget allow? Also, consider the supply of leaders. Succession plans are more critical in situations where leaders are in short supply. The harder it will be to find a leader, the more it will pay to be prepared. Here's one place that the reputation of your organization is worth its weight in gold. One of the key benefits of a strong reputation is a more ready supply of leaders who want to join your organization. The final factor to consider is your organizational appetite for risk. Companies vary, just as people do, with some being inherently (by necessity or disposition) more risk averse than others. More risk-tolerant organizations likely will be more comfortable with smaller, more focused succession plans than their more risk-averse peers. If you are just getting started in succession, we advise that you start small, work out the kinks, and then expand.

Define Role Requirements

Next, define the role requirements of each and every one of the target roles. (Now aren't you glad you followed our advice and started with a short list?) The most important thing to keep in mind is to focus on the role. Many companies get this step wrong and create unnecessary issues for themselves by focusing on the attributes of the incumbent rather than the requirements of the role. Just because the current CFO is a great golfer doesn't mean that the role requires that skill.

The goal of succession is not to clone the current incumbent—even if he or she is a stellar performer. The goal of succession planning is to fill the role with a leader who is capable of achieving the short-term goals and long-term objectives of the role and the organization. Roles change, times change, and strategies change. You can't get the right leader for a role without fully understanding the demands and challenges of the role. So let the incumbent fade into the background for a moment and focus on a full and complete description of the role itself.

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THREE KEY ASPECTS TO UNDERSTANDING ROLE REQUIREMENTS

There are three aspects to fully understanding the requirements of a role or position. Keep in mind that these aspects apply to all roles and positions, not just succession-eligible ones. The first is descriptive. A full role description answers the following questions.

- Why does the role exist; what purpose does it serve?
- What are the top priorities of the position? What is the small handful of things the position must accomplish in order to be successful?
- What are the primary duties and responsibilities of the role?

As you work through the role description, it's the perfect time to consider the broader issue of job design. All jobs change over time. Responsibilities are added and shed, often due to the skills and abilities of the job holder as much as any rational organizational reason. As you review the role requirements, try to focus on the core job, not necessarily on the job as it is currently designed.

The second part of determining role requirements focuses on performance metrics.

- What are the key accountabilities of the role?
- How do you measure performance and what primary performance metrics are used? Are these the right metrics?
- Importantly, what are the capabilities and behaviors needed to accomplish the performance accountabilities? What experience gaps or work style characteristics are most likely to derail someone in this position?

The final part of determining role requirements concerns contextual information. These are the issues related to chemistry or job fit. While not formally part of the job description per se, these are nevertheless important factors in determining who, among otherwise qualified candidates, is the best overall fit for the role. These contextual elements include:

- Who the role reports to.
- Who the peers and direct reports are and any useful information about the nature of these working relationships.
- Business and organizational challenges that need addressing; e.g., performance issues, turf battles, strained customer or vendor relationships, local market conditions, etc.
- A summary of the team or work unit culture.

Just as we recommended taking time to consider the role design, this is a good time to consider the design of the local organizational structure. Are the reporting relationships correct? Is the span of control appropriate? Besides finding the perfect person for the role, what else might be done to enhance performance?

Evaluate the Probability of New Demand and Turnover Risk

The next step is to evaluate the probability of new demand for a role (for instance, in a rapid growth situation) and the risk of turnover for each role and, therefore, the urgency with which you need to identify a successor.

RISK FACTORS: TIMING AND IMPACT

There are two dimensions involved when assessing risk: timing and impact. The more obvious of the two is timing. Is the need for a successor imminent or do you have time to prepare? Timing is an important element of succession risk because it indicates how quickly you need to identify a successor and close any important readiness gaps. Factors that affect succession timing are fairly intuitive and include obvious things like changes in business strategy and growth, and personal factors such as age and tenure. Is the individual approaching mandatory retirement age? Has the person been in the role for a long time and is he/she looking for a new challenge? Is he/she a viable succession candidate for one or several higher-level roles? Keep in mind that the relationship between tenure and likelihood of turnover is not a straight line; it is slightly U-shaped. It is a bit higher early in a person's tenure, subsides over the first few years in a role—especially at senior levels—and then gradually rises again.

Remember what we saw as the average tenure of CEOs in the S&P 500? 4.3 years. The failure rate of new CEOs was 40 percent in the first 18 months. Neither of these facts can be true without a heightened risk of turnover early in an individual's tenure.

Incumbent performance is another factor that influences the timing component of succession risk. Stronger performers have more opportunities than poorer performers and so, are at elevated risk of needing successors sooner rather than later. Because these are high-impact roles (or they wouldn't be included in your succession process, right?), poorer performers should be more likely to leave sooner rather than later, even if it means moving them out of the role before they are ready to leave—another U-shaped correlation.

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The other dimension to consider is impact, which refers to the impact that succession will have on organizational performance. Impact is, in part, an assessment of the performance of the current job holder. Finding successors for stronger performers is harder than it is for weaker performers for two reasons. First, the loss of a stronger performer is more acutely felt and it takes longer to find an individual capable of the same or better level of performance. The stronger the performance, the greater the impact. The poorer the performance, the lesser the impact, perhaps to the point where we should consider being proactive about succession. Just because a leader—even a very senior leader—isn't ready or doesn't want to step aside doesn't mean that the organization wouldn't be better off if he or she did. Which is a complicated, roundabout way of saying performance management is just as important at the top of an organization as it is in the middle or the bottom.

Other impact considerations include the quantity, quality, and value of the current job holder's knowledge and relationships, as even the best candidates cannot simply assume all of this as part of their onboarding process. To what extent does the incumbent possess unique or rare expertise that is both critical to organizational success and difficult to replace? In essence, how much organizational impact would there be if this person's knowledge, expertise, and relationships walked out the door tomorrow? Would it be an inconvenience or a crisis causing irreparable damage?

MITIGATE TURNOVER RISK

Let's consider an example. Meet Ellen. Ellen is the EVP of Operations for AccuTech, a global high-tech manufacturing organization. She's a strong performer with a track record of significant accomplishments and has been in her role for just over eight years. This is the third position she's held since joining AccuTech 15 years ago, and at eight years, her tenure in this role is more than twice that of either previous job. It's a key role, Ellen is a strong performer, and based on her track record, she's likely to be thinking about a new role. Now, what can we do to hedge or mitigate the risk that Ellen represents?

One strategy is to buy time. We can do this by considering pay or benefit options that might entice Ellen to stay in her current role longer than she otherwise might. Performance incentives, stock options that only vest after a certain period, or other so-called "golden handcuff" packages might be one way to hedge this risk.

What else might we try? When you ask people about the reasons they leave jobs and organizations, one of the most commonly cited reasons has to do with perceived lack of opportunities, including opportunities to develop and opportunities to grow or advance in one's career. Having a candid performance discussion to understand Ellen's career goals and interests, and find ways to help her develop and deploy relevant skills and abilities might be another way to keep her interested and invested in the organization and her career. Even if it only delays the inevitable or prepares her to leave her current role, isn't it better to lose her to another role than to another organization?

Our other option is to get prepared. We can broaden the pool and/or accelerate the development of potential successors to ensure that if and when Ellen does need to be replaced, we have a ready, capable replacement. This may mean looking considerably farther and wider into the organization to identify the less obvious or nontraditional successor candidates. And if time is too short or the development needs of the most likely successors are too great to overcome in the time available, a last resort is to get the headhunters started on a search in the external market.

So once you have your target jobs identified and the role requirements well defined, you will need to assess the likely timing and impact of losing an incumbent, and then use both the "buy time" and "get prepared" tactics to hedge the performance risks.

Identify Succession Candidates

The next step is to identify succession candidates. You have a target role. You know the role requirements and you've evaluated the succession risk. Where do you find possible successors?

START WITH DIRECT REPORTS

Generally, the most obvious place to look is direct reports. Direct reports often have lots to offer as possible successors. They are in similar roles and they are familiar with the issues confronting the organization. They are privy to the thinking of the incumbent. They are likely to have had similar background, training, and experience. In short, they are likely to have much of what you are looking for in a successor.

CONSIDER BOSS NOMINATIONS

Direct reports are not the only possible succession candidates. Another source for candidates is boss nominations. The boss can be either the incumbent or the incumbent's boss. Both are likely to have opinions and, occasionally, even insight into individuals who might make capable successors.

REVIEW FEEDER POOLS AND LATERAL MOVES

More organizations are also looking to feeder pools for succession candidates. Feeder pools might be high-potential leaders in other parts of the organization or incumbents in jobs that historically have been the source of effective leaders. Don't overlook lateral moves. Not all roles at a given level present equal challenges, nor is it carved in stone that succession is synonymous with promotion. When all else fails, there are always external candidates to consider, but keep in mind the notoriously bad success rate of external hires, especially at senior levels.

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Assess Candidate Readiness

You have your slate of succession candidates. Now what? The next step is to assess the succession readiness of those candidates. Who is ready now and who needs additional experiences or development? A complete assessment of succession readiness needs to touch on three areas. This is not to say that each step requires an intensive or expensive process. Even if it is just a cursory evaluation, you should think about each of the following three components of succession readiness.

Evaluate Three Readiness Factors

PERFORMANCE

It is a rare organization that would consider an individual whose current and historical performance hasn't been strong. Why would you? If a person is not performing their current job up to standard, why would you take the risk of moving them into a bigger, more challenging role? All too many organizations stop here, or otherwise fall prey to what might be called the "trajectory fallacy." The trajectory fallacy is the mistaken belief that just because a person's performance has been strong to this point in their career, it will continue along the same trajectory. Those of us in HR have done more than our fair share to perpetuate this mistaken belief. After all, who hasn't at some point told people that "the best predictor of future behavior is past behavior"? We all have. And it's true, isn't it? Well, only sort of. The true version of this hoary HR chestnut adds a very important caveat. It really says that the best predictor of future behavior is past behavior in similar situations. The more that future situations depart in meaningful ways from the past, the less past behavior can be counted on as a reliable indicator of future behavior. Significant role changes—like those that characterize succession—have the potential to create meaningfully different situations. So, while you'd never consider as a successor an individual who has a troubled or even mediocre performance track record, neither should you accept a stellar performance record as your only indicator of future performance.

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READINESS

If you can't count only on past performance, what else should you assess about a candidate? In a word, readiness. What's the difference between readiness and performance? In some ways, not much; in other ways, everything. Bottom line, what matters is the individual's performance in the new role. Performance has two parts: what and how. Most performance assessments are, rightfully, overweighted towards the what. But when we are interested in future performance, the what information is not available and all we have is the how. So, a readiness assessment is an assessment of the capabilities, experiences, and behaviors known to be associated with performance (what) in the future role or position. This is why defining the role requirements is an essential element of succession and also why it is so important to focus on the requirements of the role and not the attributes of the current incumbents. Knowing what is required to perform the future role successfully provides the template for assessing the readiness of possible successors.

POTENTIAL

The final dimension of a complete succession readiness assessment concerns potential. Does the individual you are considering as a successor have the potential to develop and progress into even higher level roles or positions? If not, you might be promoting a "blocker" into a role you want to use as a career path or developmental stretch assignment for others.

Build and Execute Development Plans

This brings us to the last of the six essential elements: build and execute development plans. Having assessed the succession candidates, you now have a wealth of information about their performance, readiness, and potential. Using this information to discuss career options and build a personalized development plan is essential to ensuring a steady supply of leaders.

Start Today to Get Succession on Track

It can be easy to rationalize not having a working, meaningful succession plan when you see so many others out there seemingly getting by without one. But why would you want to jeopardize the future of your organization? Successful succession management takes work; there are costs, resources, and time involved, especially up front when you're getting started or getting back on track. Yet, once the groundwork is laid, keeping a succession strategy moving forward becomes a whole lot simpler. The payoff is enormous for organizational performance and your bottom line. Isn't it time to get started?