Succession planning

For any CEO, discussing plans for their successor can be a sensitive issue, but by failing to tackle this thorny issue boards could be placing organisations at significant risk.

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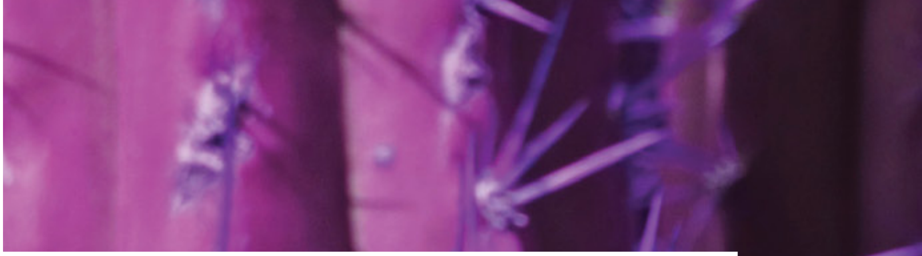
In the gripping TV series *Succession*, viewers are captivated by the fascinating plot lines and rollercoaster journey as the Roy family grapple with the succession challenges after the CEO and patriarch, Logan Roy, suffers a decline in health. As his four children scramble to secure their positions, viewers are enthralled by the machinations, the plotting taking place in the shadows of the boardroom and the impact on the company as a power-struggle and gripping succession battle plays out. While family business succession planning can be particularly challenging, a significant number of boards of directors struggle in this area, from listed companies on the stock market to private companies and non-profit and charity boards.

For a significant number of boards, CEO succession planning is a thorny and often taboo subject that can cause significant tension between the CEO and the board. Many boards do not have a proper CEO succession plan and are vulnerable to significant disruption in the event of an un-planned CEO departure. In one example I have seen, a company was severely impacted by the sudden exit of a CEO who had stonewalled the board for many years on developing potential successors within the executive team. The CEO – out of self-interest and paranoia – had consciously failed to develop the two executive team members with genuine CEO potential with the result that they left. In consequence, the board had to scramble into a rushed external search process for a CEO which ended badly. The new CEO that they hired lasted only 12 months and the company suffered significant damage, both internally and externally. This case represented a dereliction of duties and a serious failure by the board to protect themselves, the shareholders, employees and stakeholders. Over the years, I have lost count of the number of board chairs and non-executive directors who have indicated to me how much they struggle with 'grasping the nettle of CEO succession planning' and – in some cases – facing up to a dominant, controlling or difficult CEO who is frustrating the board's efforts to put a proper plan in place.

During my career, many CEOs have shared with me their genuine, heartfelt angst at the thought of discussing with the board the idea of a new CEO running the organisation in the future. The vast majority of CEOs fully understand why a CEO succession plan is needed and that the board have a formal legal/fiduciary responsibility to do this. Nevertheless, they find it very difficult to internalise that – despite the incredible leadership and contribution they have made, often over decades, and the depth of the relationships they have built with the board chair and non-executive directors – the board and relevant committee are happy to plan for the next CEO. As a former CEO, I empathise strongly with this; board chairs and committee chairs with strong emotional intelligence do too, enabling them to engage sensitively with the CEO.



The stability of the CEO's position

'Do I look like a turkey who is going to vote for Christmas by developing my CEO successor then – at the first sign of serious performance problems – this board will shaft me and appoint the successor that I have carefully nurtured over the years?' This was a particular case that stuck in my mind where I got a serious dose of salts from a CEO in a board evaluation interview. It was in reply to me asking why there wasn't a CEO succession plan in place. Their response represents a genuine concern held by many CEOs that if they either develop a highly capable CEO successor within their executive team or bring in a strong CEO-calibre new executive team member, it makes it far too easy for the board to replace them. While the vast majority of boards would not abuse the trust of the CEO in genuinely partnering with them on a proper CEO succession plan where everyone is 'doing the right thing for the best interest of the organisation', unfortunately, a small sub-set of boards have.

Power balance

A chair of a nominations committee once said to me that the reason why their CEO succession plan was so weak was that their CEO – who was very dominant and stubborn – simply refused to countenance a proper discussion with the committee. In addition, their board chair was too close to the CEO and had 'swept CEO succession planning under the carpet'. This is quite a common problem whereby the board – led by the board chair – is simply not strong enough to insist that a proper CEO succession plan is in place. For me, it is the board chair who has the critical responsibility on behalf of the organisation, shareholders, employees and stakeholders, to ensure that this formal, key responsibility of the board is properly fulfilled. Any modern, progressive board chair will know that ensuring a CEO succession plan is in place is simply not optional. For this reason, it is important that the board chair–CEO relationship sits within 'the Goldilocks zone' of being neither too hot (close) nor too cold (confrontational).

The executive team

A proper CEO succession planning process casts a very bright light on the composition, calibre, capabilities, skillsets and performance of the executive team members. Many CEOs find that this can be akin to opening Pandora's box. When a situation arises where none of the executive team has either the calibre or capabilities required to take on the CEO role – either today or within a couple of years with the right support and development – it asks some very uncomfortable questions about how the CEO is managing and evolving the composition of the executive team. In some cases, situations may be uncovered where the CEO is deliberately not strengthening the executive team with high-calibre executives with CEO potential. This can be out of a fear of disrupting a long-standing, tightly knit executive team, covering up for a long-standing executive team member who is not strong enough or the CEO not wanting to be challenged by a strong incoming executive with new ideas.

Responsibility for succession planning

Over the years, I have been taken aback by how even quite experienced boards and their board chairs struggle with understanding both the importance of, and their responsibilities in relation to, CEO succession planning. In a joint RHR International/*Chief Executive* magazine study of 236 corporate directors, 95% of respondents acknowledged that CEO succession is a critical business-continuity issue. Nevertheless, more than half (53%) rated themselves as 'ineffective' in executing their responsibilities in this area. Many boards have discovered – to their cost – the pitfalls and damage to the organisation of a sudden external search for a CEO because of poor or non-existent succession planning. While there will always be special times when an organisation needs to appoint an external CEO, my experience is that in most situations, recruiting a strong internal candidate has a higher chance of success and optimising the transition. Boards must take great care when hiring an external CEO. In some cases, an externally hired CEO's annual compensation can be 50–100% greater than that of an internal appointment. In addition, many boards have discovered that an outside CEO is less likely to stay long term and has a higher risk of early failure. This can damage confidence in the board and the organisation. Shareholder and stakeholder value can be negatively impacted and key people may leave, leading to further reliance on external talent and a perpetual cycle of failed successions.

The following represent key stages in an effective CEO succession planning process.

Stage 1 – Clear alignment and buy-in between the board, board chair and CEO

This represents the critical foundation of a high-quality CEO succession planning process whereby the board, board chair and CEO are all aligned on the importance of the process to the organisation, the responsibility they each hold in terms of discharging their corporate governance responsibilities and their commitment to put the process in place. In the best cases I have seen, the board chair and relevant committee genuinely partner with the CEO on a thoughtful process solely focused on the best interests of the organisation.

Stage 2 – Clear ownership and process implementation

Ultimately, the buck stops with the board chair when it comes to CEO succession planning. In larger organisations where nominations, governance and sometimes remuneration committees are in place which support this process, driving both in the initial creation of the plan as well as its ongoing evolution remains with the board chair. Once a plan has been developed, it is vital that it is monitored at appropriate intervals throughout the year and updated accordingly. I also find that in progressive boards, the chair involves

all of the board directors, integrating their inputs and keeping them posted on the progress of the committee's work in this area. Clearly, sensitivity is required but, where possible, I would avoid a highly secretive process involving only the board chair and the 'inner circle'.

Stage 3 – Alignment with the strategy and future needs of the organisation

One often overlooked area is ensuring that the CEO succession planning process aligns with the strategic direction and medium to longer term objectives of the board and organisation. There are times when an organisation is either in the early stages of, or is preparing for, a major transition in its market, products/services or growth/scaling. At these times, the board could be required to identify internal or external candidates who may be very different from the current CEO. While it can be tempting to default to an internal candidate who is very much in the image and likeness of the current CEO, this may not be what the organisation really needs for its next steps.

Stage 4 – Development of the CEO succession plan

In the UK Financial Reporting Council Guidance on Board Effectiveness (2018), there is an excellent section which outlines three key horizons that should be considered when planning the succession of executive and non-executive directors. These are:

- contingency planning – for sudden and unforeseen departures
- medium-term planning – for the orderly replacement of current board members and senior executives (for example, in the case of a retirement)
- long-term planning – the relationship between the delivery of the company strategy and objectives and the skills needed on the board now and in the future.

The core activity in the process is the assessment of the current executive team members to build a matrix identifying who would have the calibre, capabilities and experience:

- to take on the CEO role today in either a short-term, interim capacity or on a long-term basis
- to be a potential CEO in two to five years' time with the appropriate development and support.

Analysis of this matrix should result in an appropriate ranking of the executive team members and – depending on the outcome – a clear action plan can be developed based on these horizons.

Stage 5 – Facing up to the scenario of having no CEO succession candidates

One of the most difficult aspects with which a board and CEO must contend is the realisation that the organisation may not have any executive team members who have the calibre, capabilities and experience to take on the CEO role longer-term. At this stage, the board and CEO, working thoughtfully together, need to make a call on one of the following options.

They can bring in a new executive team member who could take on the CEO role either today or in a few years given appropriate support or they can accept that there are no internal candidates. If they select the latter option, they must decide on the contingency CEO succession plan and recognise that in either a planned or un-planned succession event, the board will have to look externally for the longer-term CEO successor.

This is an important decision for the CEO and the board. In my experience, the ideal approach is to bring in a strong senior executive to build an understanding of the organisation, a relationship and trust with the board and executive team and – over a number of years – the foundations for a highly effective transition on the planned or unplanned departure of the current CEO.

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Stage 6 – Evolving the CEO succession plan on an ongoing basis

It is vital that the CEO succession plan represents a 'living plan' that is updated at least annually to reflect both the evolution of the current executive team in terms of changes in the readiness and suitability of existing members, and potential major shifts in organisational strategy.

Summary

One of the most common phrases cited around boards is that the their single most important duty is to 'hire and fire the CEO'. In my experience, strong, progressive boards extend this to 'hire and fire the CEO, oversee the performance of the CEO, support the CEO to excel for the organisation and ensure a clear, thoughtful CEO succession plan is in place'. The CEO's leadership, performance and the example they set on culture has the greatest impact on the performance and long-term sustainable success of an organisation. In the increasingly volatile and complex environment in which every organisation board finds itself, they must remember their critical corporate governance responsibility to ensure the organisation is always prepared for a CEO succession event, whether planned or un-planned. It is vital that the board partners genuinely with the CEO in this process and fully understands the natural sensitivities and concerns every CEO feels, no matter how experienced they are. The transition of a CEO is a major event for an organisation with inherent risks – thoughtful CEO succession planning significantly de-risks the changeover and enables a seamless transition to a new CEO. ■