Strategic Issues in Succession Planning

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Succession planning, the most important human resources risk, is not taken seriously by most of the companies. What is and how can succession planning help organizations? What are the reasons for its failure? What are the roles and responsibilities of Boards and CEOs? The article brings into light the International and Indian practices in succession planning. The article also explains the important issues involved in succession planning and how they need to be managed.

Introduction

At a strategic level, succession planning is probably the most important Human Resources (HR) risk. The consequences of appointing wrong successor can be much worse than slow growth or decline in market capitalization. Take the case of Westinghouse. A series of wrong CEOs virtually drove this company, once rated on par with General Electric to bankruptcy. Unfortunately, many companies do not take succession planning seriously. The Boards due to friendship, politeness or inertia are reluctant to broach the subject. *Ad hoc* succession plans lead to crises. It is thus no coincidence that many CEOs in major US companies have failed to last even three years in recent times. These include Douglas Ivester of Coke, Robert Annunziata of Global Crossing, Durk Jaeger of Procter & Gamble, Dale Morrison of Campbell Soup and Jill Barad of Mattel. In India, companies like Thermax have faced crises because of poor succession planning. In this article, we attempt to outline the important issues involved in succession planning and how they need to be managed.

What is Succession Planning?

Succession planning is identifying and preparing the right people for the right jobs. Though applicable at all levels, it is at the highest level that the most formidable challenge exists.

Succession planning is typically done in different stages:

- Identification of key positions and when vacancies might crop up.
- Determining the skills and performance standards for these positions.
- Identifying potential candidates for development.
- Developing and coaching the identified candidates.

Succession planning if executed efficiently helps the organization in several ways:

- It engages senior management in a disciplined review of the leadership talent available with the organization.
- It guides the development activities of key executives
- It ensures continuity of leadership and sends the right signals to employees as well as external stakeholders.
- It guides the promotion policies and helps to ensure that the right people are promoted at the right time.
- It facilitates a critical review of selection, appraisal and management development processes of the organization.

This article focuses on succession planning at the CEO level.

The Coke example

Choosing a wrong successor, is a mistake all CEOs want to avoid. Unfortunately, the track record in this regard of even the most successful CEOs is disappointing. Consider the legendary CEO, of Coke, Roberto Goizueta. The aristocratic Cuban had trained his successor, Doug Ivester so well and made it clear to one and all long before his death who his successor was. When Goizueta died of cancer, Ivester took charge in what the markets perceived to be one of the smoothest transitions ever in a Fortune 500 company. *The Economist* commented:[1] "Robert Goizueta will be severely mourned at Coca-Cola, … but he might not be missed. Strangely enough, that would be one of the greatest complements a departed chief executive could receive… Douglas Ivester, Coke's 50-year old president and chief operating officer, is now expected to succeed Goizueta and to carry out the

Guidelines for effective succession planning

- Succession Planning should be customized to suit the needs of the organization. For example, if the skills necessary to manage the company in the changed environment are not available in house, there may be no option but to bring in an outsider.
- Succession planning should be driven by the line function and not HR executives.
- Succession planning should develop key candidates, in anticipation of future openings.
- Succession planning is not just selection. Development through job rotation, mentoring and formal training programs is equally important.
- Succession planning must take into account the culture of the organization.
- Succession planning must be consistent with the future strategic direction of the company.

Succession planning at Lucent Technologies

One company which seems to have taken succession planning seriously is Lucent Technologies. Lucent has divided succession planning into two phases: identifying leadership requirements and the talent available and in the next phase talent development. Most senior leaders develop their own succession planning process. Each senior executive typically identifies three possible successors.

Lucent evaluates possible successors on two primary criteria: performance and the ability to develop and adopt. Some of the important attributes, the company looks for in future leaders include:

- ability to think globally
- ability to focus on results
- ability to perform tasks and projects with speed
- customer orientation
- concern for people
- respect for people
- ability to inspire trust in employees.

A dedicated department at Lucent assumes responsibility for succession planning. This department develops strategies, collects feedback and makes ongoing improvements in the system. Senior executives spend more time on identifying and developing potential successors. High potential managers are given stock options.

same strategy that has served Coke so well. Goizueta deserves the credit for this smooth transition. He was responsible for succession at Coke, and his plans had been laid well in advance." Yet, a couple of years later, Ivester was found unfit for the task and had to resign. An accountant by training, Ivester had a flair for numbers and had the reputation of a street fighter, unlike Goizueta, who had been a strategic thinker and delegator. When they were together, Ivester complemented Goizueta well. But after becoming the CEO, Ivester found it difficult to manage some sensitive issues and by early 2000, had resigned.

Looking back, Ivester's number crunching, financial engineering and technical skills were exceptional but his people orientation and leadership skills were lacking when they were needed most. Take the scare in Belgium when hundreds of people became sick after drinking Coke. Ivester did not go there for a week, a reflection of his inability to appreciate the magnitude of the crisis. Similarly, Coke's failed merger deal with Orangina was mostly due to Ivester's failure in dealing with anti Americanism in France. Ivester also seemed somewhat out of place while handling a racial discrimination suit. Quite clearly, Goizueta had trained his successor well but had chosen the wrong successor in the first place.

The Indian Scenario

The problems associated with succession planning are particularly acute in India, where family managed businesses proliferate. Such companies throw discretion to the winds and spend time on dividing the family silver among the next generation rather than in grooming the right person to take over the top job. Family managed companies would do well to remember that the chosen successor should have the necessary education and skills and be made to work his or her way up the management to gain the maturity needed to appreciate the privileges and responsibilities involved. Alternatively, they should be bold enough to appoint a professional manager, when there is no suitable candidate within the family. Some of the more progressive Indian business houses like Ranbaxy, the Murugappa group and the Eicher group have demonstrated a high degree of professionalism in this regard.

Many Indian companies are now beginning to appreciate the importance of planning successions carefully. At L&T, one of India's leading engineering companies, many of the company's senior managers are expected to retire in the first few years of the new millennium. CEO A M Naik has been attempting to deal with the situation, naming the top 10 percent of his executives as stars and chalking out a fast track career path for them. Naik hopes that by 2005,[3] "L&T will be in strong hands". Before initiating

Why succession planning fails

- High potential candidates are arbitrarily identified.
- The qualities that a successful business unit head has and what he should have as a CEO after promotion are different. Business unit heads may not have strategic vision or the ability to communicate effectively with external stakeholders.
- Many executives make excellent No. 2s and act as a fine complement to their CEOs but fail miserably when they move into the corner office.
- The designated replacement may be far from ready to take over. The evaluation may be more positive than what it should be.
- Promotions are made keeping in view the organizational needs, but totally ignoring the employee aspirations.
- The process lacks transparency and confuses talented people who may decide to leave.
- Outside hires are brought in indiscriminately without explaining the rationale to insiders.
- When one person leaves, instead of moving decisively and appointing a successor, the portfolio is split among two people at the next level, leaving people totally confused.
- The program is perceived as being limited to the 'elite'[2] core.

[1]October 23, 1997.

[2]In many Tata Group companies for example, employees feel that managers from the Tata Administrative Services (TAS) will invariably occupy all the plum posts.

the program, L&T employed the services of an HR consulting firm to list the positions falling vacant and the required competencies. L&T now fills vacant posts with internal candidates wherever possible. In some cases, however, it compares the internal candidate with an external candidate to judge his or her readiness to move into the new job.

The problems which Indian companies face while managing succession planning are well illustrated by one of India's most people oriented employers, Thermax. The Pune-based company has been known to take good care of its employees, making it a favorite employer among many of India's premier technical institutions. Yet, the company was facing a major crisis at the beginning of the new millennium. Roughly five years after founder Rohinton Agha passed away, the entire board of governors had to resign *en masse* as the company struggled to compete in a changing business environment. Thermax's market capitalization declined sharply from Rs.990 crore (on July 22, 1996) to Rs.186 crore (on April 4, 2000). Agha had nurtured and grown Thermax over a long period of time but had not paid enough attention to succession planning. His wife, Anu Agha[4] recalled: "My husband was like an ostrich. He never liked to discuss anything. Once, he vaguely talked about taking over as non-executive chairperson. He didn't discuss a succession plan definitively. But since Abhay Nalwade was the only designated executive director, he appeared to be his obvious choice". Nalwade who was appointed as Managing Director after Agha's death recalled: "It was so sudden that I didn't have the time to think. I feel if succession had occurred systematically, it would have been better. Rohinton never discussed that I would be the successor he had in mind. It's one thing to be a peer and another to be a boss." Now a new Thermax board with company veteran, Prakash Kulkarni as managing director faces the challenge of giving the company a new direction.

What the CEO needs to do

Many CEOs fail to handle succession planning effectively for a variety of reasons:

- They forget the big picture and stay focused on day to day operations.
- They have an exaggerated sense of self importance and begin to think they are indispensable.
- They are poor in building a second layer of management because of an unwillingness to tolerate good people or to delegate.
- They try to avoid conflict and hesitate to send a clear message who the successor is going to be.
- They continue to play a role in the company even after the new CEO has been put in place.

To avoid these pitfalls, CEOs must periodically ask themselves the following questions:

- Is leadership growth keeping pace with business growth?
- Is leadership development keeping pace with the strategic needs of the organization?
- Are vacancies in senior management positions being filled up smoothly through internal promotions?
- Are objective plans in place to identify and develop future leaders?

CEOs would do well to be proactive and take care of the following:

- Identify the key leadership criteria and provide support to potential leaders to meet these criteria.
- Select a few high potential leaders and concentrate the resources available on their development.
- Monitor the results of the succession planning process at all levels of the organization regularly.

What the Board needs to do

The Board has a very important role to play in selecting the next CEO. Indeed, choosing the CEO is probably the most important decision the Board makes. The board should convey to the incumbent CEO in clear terms that his success will also be measured by his ability to handle succession. Also, the board should play an active role in the succession planning exercise and not just leave it to the CEO.

Specifying the criteria, the next CEO should meet, is a challenging task. Many boards confine themselves to generalities such as ability to build a team or ability to manage change. Others concentrate on technical skills to the point of completely overlooking leadership skills. In many cases, future CEOs are judged by their past track record in delivering measurable performance like increase in market capitalization. Quite clearly, a balanced approach which takes into account the requirements of the job in a holistic manner is necessary.

According to Bennis and O'Toole,[5] the Board should assess the soft qualities of leadership by asking the candidate's peers, subordinates and superiors a series of questions to get an idea of the:

- Consistency in the way the candidate inspires trust in others
- Ability to introduce a high degree of accountability
- Ability to delegate
- Amount of time the candidate spends in developing others
- Time spent by the candidate in communicating the company's purpose and values down the line
- Comfort level in sharing information, resource, praise and credit
- Ability to energize others
- Demonstration of respect for followers
- Listening skills

One crucial decision boards face is whether to choose an insider or an outsider. Firms in trouble often look for fresh blood. On the other hand, when things are going smoothly, the board may decide to appoint an experienced insider. According to a study by Nitin Nohria and Rakesh Khurana,[6] outsiders replacing a CEO who had been fired tended to do well. Those who took over

[3] *Business Today,* September 21, 2000.

[4] *Businessworld,* August 7, 2000.

[5] *Harvard Business Review,* May-June 2000

Leadership development at GE

GE is quite clearly one of those few companies which has been able to grow leaders consistently. When GE announced that the successor to the legendary Welch would be selected from a shortlist of three, successors to each of these potential successors were also nominated. Quite clearly, GE has enriched each level of the organization with strong leaders. It must not be forgotten that Welch himself honed his leadership skills at GE under the guidance of his illustrious predecessor, Reginald Jones.

GE's Leadership Development Institute in Crotonville, New York has ensured that activities aimed at developing leaders are closely linked to the company's business strategy. At the end of the year, GE makes an assessment whether corporate leadership development has been able to support GE's different business initiatives.

GE has correctly understood that leadership-development processes have to be action-oriented. In classroom sessions, real time business issues are applied to skill development. Welch himself took the lead in choosing action-learning topics for annual executive-development courses. Participants are asked to do project work and make recommendations. Proposals for running GE's operations in Russia and to launch the Six Sigma initiative both came in leadership development programs.

GE also trains executives in change management by disseminating its accumulated expertise in this area. GE has tied leadership development to succession planning. Potential candidates for senior level positions are appraised both on their bottom-line performance and adherence to core values. Each year, the Crotonville institute trains some 10,000 GE employees. The top 500 people are considered to be corporate resources and sent to manage different businesses around the world based on the business and development needs. GE interviews company leaders around the world to assess future business needs and the leadership characteristics needed in the years to come.

Welch took quite sometime to appoint his own successor. That does not mean he had not given adequate thought earlier. As far back as 1991, Welch had remarked in a speech: "From now on, choosing my successor is the most important decision I will make. It occupies a considerable amount of thought almost every day". Welch's successor, Jeffrey Immelt who has been chosen very carefully after a long screening process, recently took charge.

Source: Fulmer, Gibbs, Goldsmith, "Developing leaders: How winning companies keep on winning", Sloan Management Review, Fall 2000.

from CEOs retiring in the normal course failed miserably. In the absence of a crisis, an outsider often finds it difficult to carry the insiders along. So, in the case of an outsider, it helps if the board sends clear signals that the earlier CEO has been asked to leave and the new CEO has been brought in to rectify matters.

Being the designated successor of a powerful incumbent CEO is very often not a happy experience. The power and influence of the CEO tends to upset the succession planning exercise. The incumbent CEO is aware that allowing the process to go ahead smoothly gives him a chance to perpetuate his legacy, but still hesitates and fails to come to grips with his own mortality. So, when the CEO is powerful and has been around for a long time, the Board should get very deeply involved in the succession planning exercise.

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The successor's dilemma

Some CEOs appoint successors well in advance of their retirement but only to see them leaving prematurely. John Walter, who became the president of AT&T in October 1996 left in just nine months. Disney's Michael Ovitz lasted just over a year as president when a souring relationship with CEO Michael Eisner forced him to leave. In Citigroup, heir apparent Jamie Dimon quit in 1998. The same fate met Merrill Lynch COO Herb Allison who was strongly tipped to become the next CEO.

So, a successor needs to be coached well on how to handle the transition. He should be encouraged to stay in constant touch with the CEO and remain focused on the post that is going to be his instead of falling into emotional traps. The successor must be made to understand that his stakes are much higher than those of anyone else including the incumbent CEO. He must be motivated to seize the initiative and rise to the occasion, displaying the highest possible level of emotional maturity. He should also be made to realize in a subtle way that if he quits, he would harm his own chances of becoming a CEO elsewhere.

The successor should be counselled to put himself into the shoes of the CEO and understand what is going on in his mind. Typically, the CEO goes through three phases after the successor has been appointed. In the first phase, he feels good that he has initiated the process and maintains a good relationship with the successor. Then, the CEO starts feeling uneasy as the successor takes charge and begins to shake things up. The CEO finds he is having to give up control and share his power and

[6] *Harvard Business School,* Working Paper, August 1997.

Guidelines for the Board

According to the famous management consultant, Ram Charan, boards would do well to remember the following:

- The whole board must be fully involved in the succession planning exercise.
- Detailed criteria for the new CEO must be specified.
- Not only insiders but also external candidates must be considered, even at the risk of offending the current CEO.
- Decisions should be made on the basis of personal interaction and not paper reports.
- The board should be prepared to spend sufficient time with potential candidates followed by free and frank discussion about each of them.
- The board should not abdicate the responsibility of choosing the next CEO to head hunters.
- The board should not exclude anyone from the race and must make the final choice a few months before the current CEO will retire.
- The board should never make the mistake of appointing two people as successors, say one as chairman and the other as CEO.
- The board should view succession planning as an ongoing exercise and get going years in advance of the actual transition.

authority with the heir apparent. The issue of facing the post retirement phase also causes anxiety. Finally, the CEO unless he is a person of extraordinary mettle, develops friction with the heir apparent due to a threatened sense of identity and control. At this juncture, an open conflict may develop and the CEO might marshal support from his trusted lieutenants and encourage people to directly come to him, by passing the heir apparent. The successor often responds by being even more aggressive and result oriented. If he succeeds, the CEO feels even more threatened. Ironically enough, when the successor is just ready to move into the corner office, he becomes frustrated by the confusing signals sent by the CEO and decides to quit.

Conclusion

Succession planning is a key strategic issue that needs the time and attention of top management on an ongoing basis. A proactive approach is far more desirable than an *ad hoc* knee-jerk approach. It is heartening to note that some Indian companies are taking succession planning more seriously than others. Hindustan Lever (Lever) spends quite a bit of time and effort on succession planning. Transition from one CEO to another has generally been smooth and there has been no case of any CEO failing badly in the top job. Succession planning at ITC has also been generally smooth, though one CEO, K L Chugh was probably a wrong choice. A fixed five-year term for the CEO has lent an air of credibility to the whole process at ITC. Another Indian company which has got praise for succession planning is Ranbaxy. When Parvender Singh died, his successor, D S Brar, a professional manager took over the reins without much loss of continuity. However, in general, Indian companies have a long way to go in the area of succession planning.

Especially in public sector organizations, succession planning has been a disaster. CEOs have changed frequently and not been allowed to settle down into their jobs. Many of the appointments have been guided by political considerations. The fact that quite a few of the top jobs at PSUs are either unfilled or manned by acting CEOs is a clear indication of the lack of importance attached to succession planning. The crisis at Unit Trust of India (UTI) in recent times has much to do with a totally *ad hoc* approach towards CEO succession planning. In many Indian companies, CEOs spend more time protecting their turfs than in developing the next line of leadership. Unless this attitude changes, many Indian companies may see themselves facing crises from time to time.

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Questions for discussion

1. Why succession planning is an important issue at the strategic level of an organization?
2. Are criteria for choosing CEOs in family managed businesses different from that of professionally run companies? Discuss.
3. "Choosing a CEO is probably the most important decision a Board makes." What aspects should the Board members need to look at, before choosing a CEO?

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