The Succession Dilemma

Solving the tensions of reshaping the organization to develop CEO successors

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As the date of a planned CEO succession nears, organization redesign can help make sure that a top internal candidate will be as well prepared as possible to make the demanding leap to the top job. However, reconfiguring the organization to give the candidate more responsibility is fraught with tensions between what is best for the business, best for succession, and best for the potential successor. Resolving those tensions isn’t easy. But by systematically thinking them through, boards and the incumbent CEO can determine what redesign – if any – is right for the company’s situation.

Forward-looking companies use a variety of tools to prepare executives for broader roles and greater responsibilities: stretch assignments, rotations through a range of businesses and functions, coaching, high-potential programs, and individual development plans. Deployed well and managed actively over time, these techniques can produce a deep bench of highly competent leaders and potential CEO successors.

As the date of succession approaches, conscientious boards and CEOs benchmark and assess internal and external talent. Ideally, by the time the decision needs to be made, they have done everything possible to prepare the likely internal successors. One tool that becomes more critical as time grows short is job redesign – which at the most senior levels of the organization translates into overall organizational redesign.

For example, if a successor candidate lacks P&L experience, a new operational role may be created that will provide it. Or, if the candidate is deficient in a discipline or function that is expected to become increasingly important for the company’s long term strategy, the organization chart may be redrawn to bring that area under the candidate’s purview. However, the overriding purpose of organizational structure is to facilitate the execution of strategy – not succession planning or individual development. If not done conscientiously and with clear business objectives, an organization redesign could potentially harm the business and introduce unnecessary risk.

For example, a smaller or medium sized company might be organized functionally because it is a cost-efficient and simple way to manage. However, developing functional leaders into CEO successors is challenging because the set of functional responsibilities is significantly narrower than that of a CEO. By re-organizing the company into a business unit structure, the CEO might better prepare the internal candidates to become CEOs, but might also harm the business by unnaturally driving costs up and interrupting effective processes that drive innovation and customer connection.
Unfortunately, there is no one-size-fits-all solution for reconciling these conflicts. Like any difficult business decision, using organizational redesign to enhance CEO succession involves risks and opportunities that must be weighted carefully, in context, and holistically. While there is no right answer, there is usually an optimum answer for the company, effective succession, and the candidate.

All of the familiar organizational structures – functional, divisional, and matrixed, among others – offer advantages and disadvantages for the business and for individual development.

**Divisional Structure** - The many variants of the divisional structure, by region, customer or product, provide multiple opportunities to develop well-rounded leaders who get exposure to different aspects of the business and get to exercise P&L ownership early on. However, a business needs to be big enough to warrant such a division of work.

**Functional Structure** - The functional structure, on the other hand, creates opportunities for the development of leaders with high levels of technical expertise. These structures provide fewer opportunities for the development of cross-functional leaders, and P&L ownership normally resides only at the CEO level. Most companies begin with this structure.

**Matrix Structure** - The matrix structure, intended to combine the best features of functional and divisional organizations, creates opportunities for both functional and well-rounded leaders to develop. It also creates an increasing number of opportunities for cross-fertilization where business leaders can become functional leaders and vice versa. However, discrete P&L ownership can be harder to measure and the structure itself can become complex and costly to administer.

As boards and CEOs work to arrive at this solution, we suggest considering the following:

**No ideal organizational structure exists, so don’t aim for perfection.**

The relevance of structure to development and CEO succession is straightforward. Organizational structure, in addition to facilitating the execution of strategy, answers the important question of who decides what. Because CEOs are the ultimate decision-makers, successors will ideally have had broad decision-making authority in a single role, or will have had specialized experience in multiple key areas of the business. Additionally, because CEOs are measured by financial results, successors can greatly benefit from having direct and measurable P&L responsibility. Boards also benefit as they can objectively measure individual performance and impact through full P&L ownership.
Stay true to the ultimate purpose of organizational design - to produce results by aligning structure with strategy.

The most critical consideration in contemplating any organizational redesign should be the likely effect it would have on the business and financial performance. If the company is not performing well, the board is unlikely to select an internal candidate. The board will view the internal candidates as part of the underperforming team and possibly heed the need to signal externally that a change is on the agenda. So despite the best laid internal plans, boards in these situations will often select an external candidate as the next CEO.

Care, too, should be taken to set up the heir-apparent candidates for success in any new role created as the result of an organization redesign. Candidates should be given “real” roles where their skills are valuable and their results are measurable. Ceremonial or “tourist” roles where candidates are given responsibility in name only, or for a short period of time, is only mildly helpful and can at times be harmful. The cost of failure is exponential with the price being paid by the candidate, the incumbent CEO, the senior team and the board.

Consider tweaking instead of transforming.

It is rare that organizations engage in a massive organization redesign for the sole purpose of supporting a CEO succession program. Large redesigns are more often driven by ambitious business initiatives – a new aggressive growth strategy, a bold attempt at turnaround, or a drive into new markets and regions.

Successful “organization redesigns” focused more narrowly on CEO succession are more likely to take the form not of transformations, but of tweaks, including:

- **Minimizing the CEO’s number of direct reports.**
  This inherently broadens the responsibility sets of those limited direct reports, thus better preparing them to become more rounded leaders and better potential CEO successors.
  - In 2010, Johnson & Johnson promoted the heads of its two largest businesses to the company’s highest executive suite, pitting them in a race to succeed William Weldon as chairman and chief executive officer. Sheri McCoy, who had been running J&J’s pharmaceuticals group, and Alex Gorsky, previously chief of the company’s medical-devices and diagnostics division, were named vice chairmen in the Office of the Chairman with expanded responsibilities. These appointments set the stage for the selection of the company’s next leader, and Alex Gorsky was named CEO in February 2012.

- **Assigning CEO activities to the successor, making the candidate accountable for the outcomes.**
  - At Ford, before being named CEO, COO Mark Fields had already begun taking on many of then-CEO Alan Mulally’s responsibilities, including running the company’s weekly business plan meetings, to facilitate the ease of the handover.
  - At Apple, Tim Cook was Steve Jobs’ COO for the better part of a dozen years, and he was test driven as CEO at least twice during this time with Mr. Jobs out on medical leaves. He was progressively given more CEO-like responsibilities (e.g., putting him in front of investors, managing stakeholders), which allowed for a smooth transition.
  - Before becoming CEO of McDonald’s, Don Thompson served for two years as COO. In this position he was personally mentored and tutored by Jim Skinner, the exiting CEO, to ensure a smooth transition. Mr. Skinner also stayed on for the first 90 days of Mr. Thompson’s tenure.

- **Splitting the CEO’s role to establish a President or Chief Operating Officer role to sit atop the existing functional or divisional structure.**
  By adding one layer atop the existing structure, you are able to broaden an individual’s scope of responsibilities, creating a clear decision path that leads through this executive.
  - In 2005, Bruce Chizen, then-CEO of Adobe Systems, promoted Shantanu Narayen to the newly created position of President and COO. In this new position Mr. Narayen continued to report to Mr. Chizen, but he also assumed responsibility for engineering, product marketing, and sales. Mr. Narayen was named CEO in 2007.
In 2009, Alan Boeckmann, then CEO of Fluor, appointed David Seaton to the newly created position of COO. As a result of this promotion, Seaton was given responsibility for all five of the company’s operating business units and the Project Operations unit. The only executives not under Seaton’s purview were the CFO, the Chief Legal Officer, and the head of HR and Administration.

This kind of targeted job redesign, common in many companies, offers several advantages:

- Concentrated changes are discrete, contained and focused on the top two layers of leadership so they are easier to design and implement.
- Orchestrated changes entail less risk for the broader enterprise and minimize the long-term disruption to the business.
- Substantive changes give the candidate exposure to important outside stakeholders like the Board, investors, customers, and analysts.

Consider not only what you do, but when you do it.

Most boards try to have clear CEO successors emerge within three years of the scheduled transition. Given this relatively tight time frame, few additional development options remain where lessons can be learned and results can be observed. As time is running out, another rotation – to head a major region or business unit – is risky and may not be feasible given business demands and career aspirations across the entire executive team. Moreover, shuffling functional heads among the top team is usually not practical as it often requires a completely different skillset than the candidate has used to date. If the candidate lacks crucial functional experience, the more feasible solution is to put the person in a role where the head of that function reports either directly or indirectly to the candidate, thereby temporarily adding a layer.

Manage the signals a redesign sends.

A redesign that elevates an individual into a high-profile role comes with an “expiration date” and sends unmistakable signals to the public, to other contenders for the CEO role, to the competition, to the company’s customers, and to the markets. Disappointed internal successor contenders are likely to be among the most talented, ambitious, and difficult-to-replace leaders in the company. The incumbent CEO and board should therefore be thinking carefully about how to explain these moves. Additionally, the CEO and board should be prepared for the fact that both competitors and customers alike may view the heir-apparent choice as being indicative of the company’s future strategy and may react accordingly. Market analysts will also pounce on the news of critical structural and role changes that indicate the company’s future direction.

As with all strategic changes, you need to think through scenarios.

Though organizational structure is a static architectural metaphor, the results of personnel and design changes unfold as a story over time, sometimes with unforeseen twists due to the many factors that can affect the outcome. Just as with strategy formulation, boards and CEOs should work through possible scenarios under various sets of conditions and be prepared for them – including the possibility of the heir-apparent performing poorly. If the heir-apparent does not perform as expected, the board will need a fallback succession plan, which might include a temporary “office of the CEO” with a board member playing an executive role, the elevation of another internal candidate, a scanning of the external market for potential candidates, or perhaps some additional organizational redesign.

CONCLUSION

Organization design is a tool that can help boards and CEOs manage the succession process as it forces them to consider timing, business implications, and the readiness of candidates to take different roles. Through recognizing and analyzing the various components of an organizational change for succession planning purposes, the board and CEO will be able to make the best decision for the company, the person, and succession.

When the final decision is made and the CEO is announced, the hand-off should look natural, yet also like a stroke of genius. For those involved in such high impact transitions, we know there are always elements of both luck and skill involved in arriving at that moment. Proper planning is the key to increasing your luck.
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