FOCUS ON BUSINESS SUCCESSION PLANNING

Focus on future skills when identifying successors

By IRA S. WOLFE
Special for Lehigh Valley Business

Faced with changing demographics and skilled-worker shortages, many companies will be unable to fill job openings from the CEO to the technician.

Wolfe

"The Perfect Labor Storm" has already crippled many organizations.

Despite over two decades of warnings about the need to plan succession, many companies have ignored them.

In a recent survey by the Institute for Executive Development and Stanford Business School almost half of the companies were not grooming a specific executive to succeed the CEO. For companies that had a plan, 39 percent could not identify a single candidate who was "ready now."

Other surveys paint a much bleaker picture. According to the executive search firm Korn/Ferry, 98 percent of companies believe leadership succession to be important but only 35 percent have a plan in place.

As bad as succession management is at the top, it is much worse as you climb down the organizational ladder.

In these days of lean-and-mean, each position in many companies plays a vital role. The absence of a single worker can compromise the business. An abrupt absence or even a planned retirement can cripple it.

Even when a company creates a succession plan, the failure rate is high.

In today's market where high-potential leaders are in short supply, the prospect of moving up another rung on the ladder may not be enough incentive to keep the successor on your ladder.

Based on both years of research and work with clients, here are seven common reasons that succession plans fail. While in most cases, the research was based at the CEO level, the same sources of failure occur regardless of the position level in the organization.

(1) Successors leave.

Despite all best efforts to identify successors, new opportunities or personal decisions cause the next-in-line to leave the organization.

Once a successor(s) is identified, it is critical that leadership development and retention become the focus. In today's market where high-potential leaders are in short supply, the prospect of moving up another rung on the ladder may not be enough incentive to keep the successor on your ladder.

(2) Incumbent doesn't leave.

This is a major problem, one that is growing more common.

For many reasons, incumbents aren't leaving. The most popular reason is that the baby boomers aren't leaving their positions.

Some need to keep work to fund their decimated retirement plans. Others just don't want to stop working. And a few are incentivized to stay to help navigate the company through unchartered waters.

Regardless of the reason, experienced managers and employees who linger past their expected departure date disrupt succession plans (see No. 1 above).

(3) Successor doesn't perform.

The rate of CEO failures during the first 18 months on the job, as reported by an oft-cited Harvard Business School, is 40 to 60 percent. While released in 2005, few studies since point to much improvement.

(4) Focus on past experience and not future skills.

Too often management looks in the rearview mirror to understand what the company needs for the road ahead. An open position should be filled with people capable of performing the new job well, not a reward for success in the old one or 20 years of loyal service.

New roles or even the same role in a different company carry different responsibilities. Performance and future potential are distinct and independent variables.

It is pragmatic to cite past performance as a good indicator, but the link hasn't been proven. The bottom line is that past performance is no longer a reliable indicator of future success.

(5) Fixed mindset cripples future success.

Potential indicates whether someone will be able to succeed in a bigger role. But it's a person's ability to grow, to overcome setbacks, to embrace challenges that really counts.

Many high-potentials are groomed for the job. The heir-apparent and high-potentials are protected and coddled to avoid injuring their pride and self-esteem. They are not allowed to fail in fear of losing them to the competition.

When promoted or hired into a new role, the successor with the fixed mindset works hard to protect his stature as the anointed one. The focus is on his ability, not the goal.

When confronted with setbacks, challenges, or ambiguity, he blames others. He passes the buck.

Breakthroughs in neurosciences and cognitive-development-and-personality psychology suggest that growth mindset is a more reliable indicator of future success than past performance. That means trashing the resume and focusing on how he will deal with complexity,

please see **SKILLS**, page **15**

Potential successor must have 'skin in the game'

By MICHAEL JOYCE
Special for Lehigh Valley Business

With a well-devised blueprint in place, business succession plans can be win-win scenarios, benefiting both the business owner and the successor.

Joyce

While this advice is from the perspective of a business owner, the suggested actions will enable both parties – the business owner and the successor – to view the plan positively.

In order for any succession plan to be viewed as mutually advantageous, several important protections must be put in place.

Since the relationship between the business owner and the successor is a long-term one, the two parties should ideally share values and visions for the company moving forward. Not unlike in a marriage, business owners need to be sure that they want to partner for life (and beyond) with their successor. Carefully considering a potential successor's way of doing business, then, is important.

Additionally, the business owner would be well-advised to ensure that a partner/successor has "skin in the game." Without it, it's possible the successor would not have as much passion for the enterprise.

But under no circumstances should a business owner just give away equity. Ideally, the successor would be either of the following:

(A) Someone who has been with the business from the ground up and contributed to the original founding of the firm (with all of the hard work, long hours, pavement pounding, etc. that goes with starting a business).

(B) Someone who has paid a large enough amount of money to make him or her feel extremely committed to the business.

In either case, the successor would have the requisite "skin in the game."

THOROUGH, CLEAR LANGUAGE

Another critical step in succession planning is to create a written agreement clearly delineating the plan. Business owners should be thoughtful and even rigorous when developing the agreement, making sure to dot their i's and cross their t's.

The language in the agreement should be clear, unambiguous and thorough.

And, of course, both parties should sign and date the agreement.

CONSULT WITH TAX ADVISER

Tax implications are another important factor to consider when developing a business succession plan. Consulting a competent tax adviser is a small investment to make to avoid unintended tax consequences.

No business owner in transition wants to experience big surprises come tax time, so seeking input from an experienced tax adviser is crucial.

Additionally, business owners should consider utilizing a neutral source to perform business valuations at regular intervals so that the owner knows the present market value of his or her shares.

THREE CRITICAL STEPS WHEN PLANNING FOR SUCCESSION

- **View the relationship** with a potential successor as a marriage. Business owners should ideally share values and visions with their successor – and want to partner with them for life.
- **Make sure** the successor has "skin in the game" – with either long-term sweat equity in the business or a significant monetary investment.
- **Consult a tax adviser** to avoid any unintended tax consequences of a succession plan. The investment in tax advice will ensure that a business owner moving through the succession process will have no big surprises come tax time.

CONTINGENCY PLANS

When planning for succession, business owners should also be careful to think through possible worst-case scenarios. While both parties should go into the succession transition cautiously optimistic, business owners need to have strategies in place to extricate themselves from the plan with a minimum of pain in the event that things "go south."

Having a plan for such scenarios in place – prior to transition – will ensure that the business owner reacts unemotionally and in the company's best interest if faced with a less-than-ideal outcome.

WIN-WIN

If business owners take the proper precautions prior to implementing plans with successors, the result can indeed be "win-win."

Both parties benefit when business owners view the relationship as seriously as a marriage, when the successor has "skin in the game," when a carefully structured succession plan agreement is in place, when tax advisers have been consulted and when worst-case scenarios have been carefully thought through.

Michael Joyce, founder and president of JoycePayne Partners of Bethlehem and Richmond, Va., is responsible for overall investment strategy, management of investment portfolios and financial counseling services. A Chartered Financial Analyst and Certified Financial Planner, he has more than 30 years of experience in the financial industry and seven times has been named one of the top 100 wealth advisers in the nation by Worth magazine. He can be reached at mjoyce@joycepaynepartners.com.