manager to manager

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Can succession planning impact your utility's performance?

Two industry giants, Coca-Cola and McDonald's, have remarkably similar stories with one great difference—their approach to executive selection and development. That difference is reflected in their bottom lines.

Coke has been struggling since its legendary chief executive officer (CEO), Roberto Goyzueta, died suddenly in 1997. According to *The Wall Street Journal,* the company has subsequently gone through a series of leaders and business strategies. Coke's board is seen by some as "meddling" in the company's operations instead of finding the best leader. The latest search resulted from a disagreement between the board and the retiring CEO about the CEO's recommended internal succession candidate.

Another American icon, McDonald's, demonstrates a counterpoint to this executive succession case study. McDonalds's CEO, Jim Cantalupo, died suddenly in the early morning hours of April 19, 2004, the day he was to open a biennial conference of McDonald's owners and operators. By 9:30 a.m., the time that Cantalupo had been scheduled to address the conference attendees, his successor Charlie Bell had been named to the CEO post.

A knee-jerk reaction? Hardly. McDonald's officials said that Bell was the planned successor for Cantalupo and that he had worked side by side with the CEO for 16 months. As the successor, Bell was being developed to carry forward McDonald's strategy. The business strategy, initiated by Cantalupo, was reversing a long slide in the company's financial performance. On the day the board's decision was announced, *The Wall Street Journal* noted, ". . . analysts widely reaffirmed their 'buy' rating of McDonald's stock and expressed confidence in Mr. Bell's ability to continue turning the company around."

WHAT DO THESE SUCCESSION STORIES MEAN TO THE WATER INDUSTRY?

Surprisingly, they mean exactly the same things that they mean to Coke and McDonald's—stable performance and continuity of leadership. Additionally, the water industry's vision, values, and strategies are significant not only to each individual utility but also to the nation and the world. The water industry is among a handful of vital industries that should be doing outstanding succession planning because at least two things are at stake:

- your product is one of the nation's most precious resources, and
- although your employee population is battle-tested, your leadership bench strength is in most cases unexamined.

This could leave your water utility vulnerable to a leadership talent vacuum as current executives retire if the leadership below them is not identified, developed, and "brought into the fold" as McDonald's was. When she became AWWA's president, Katie McCain said in her inaugural address, "Institutional knowledge of utility operations is walking out the doors at dizzying rates! Those of us who will be part of that retirement exodus in the next 10 years need to act now to leave our utilities, or water systems, in good hands and in good shape."

We concur. This article explains how this can be done, based on our succession-planning work with various utilities.

A recent CEO survey conducted by the Center for Creative Leadership and a separate research study of 100 US companies show that succession planning correlates with high-performing organizations, as measured by their shareholder return (financial performance). Here's how one of our utility

WATER UTILITIES ARE EXCELLENT AT CONTINGENCY PLANNING FOR AN UNKNOWN FUTURE—AT LEAST IN THE AREAS OF OPERATIONS AND ENGINEERING.

clients expressed it: "Our succession plans made a considerable difference in the interest level of the utility that ultimately acquired us. As we made our management presentations to potential buyers, we were able to demonstrate the strengths of our current leadership team members and the depth of talent below them. This influenced my utility's perceived value as an acquisition."

Although the dynamics of each industry are different, there is every reason to give high priority to ensuring continuity of leadership through succession planning. Considering global concerns about water scarcity and quality, along with heightened security concerns, excellent forward-thinking leaders are critical not only to the water industry but also to the public it serves.

Other water utilities, as well as other employers, will be competing for the same leadership talent needed by your utility. Working now to develop succession planning and talent management practices could help your utility gain a competitive edge in the key area of retaining and recruiting top leaders.

SO IS MCDONALD'S A UTILITY?

The real question is: "Can utilities afford to view succession as a 'no surprise' event?" Every water utility will face the loss of leadership team members as a result of retirements. However, your water utility may also face a loss of leadership as a result of unpredictable misfortune. Progressive utilities are using succession planning as a best practice to prepare for the transition risk that accompanies a CEO or senior officer departure. A domino effect occurs when any senior officer leaves: one job is vacant, another executive is moved to fill the vacancy, and a second job becomes vacant. At such times, succession planning is used to assess the cadre of top leadership talent. A set of moves based on these assessments yields a stronger team and greater bench strength, as opposed to weakening the net effectiveness of the senior team.

Two best-practice examples of how utility CEOs and their boards of directors faced succession planning challenges not unlike those faced by Coke and McDonald's are described in the following sections.

Accelerated succession planning at an electric utility. A large electric utility client received a severely critical management audit from its state regulators, which led the company to start a corporate management-development function. The function was responsible for, among other things, succession planning. For a number of years the utility focused its succession plans on natural retirement turnover in key positions. Several years later, an industry event caused the board to accelerate the company's succession planning. The board moved swiftly beyond planning for normal retirements to preparing for rapid, unpredictable replacement needs. The time did come when the CEO and nearly half of the senior team were replaced within a few months of one another. The utility followed its succession plans precisely. Like McDonald's, the utility executed a smooth transition of senior leadership. This assured its financial viability and the positive regard of the public, the investment community, and state and federal regulators. This utility now stands as an exemplary industry model of recovery from a potentially disastrous business situation.

Executive assessment used by a water utility to ID viable executive candidates. The forward-looking board of directors and incumbent CEO of a progressive water authority applied long-range planning to its executive-level succession planning. We designed a succession planning process, customized to this water authority, to identify, assess, and develop internal talent early, as part of the utility's CEO succession planning. The process included a "third-party" executive assessment some five to eight years in advance of the anticipated transition of the incumbent CEO. The assessment yielded results that were useful for both selection and development decisions. The assessment results also created information that could be commonly understood and shared by the CEO and the board. The CEO decided to assess the responsibilities of all the senior executive staff who reported directly to him. Some of the CEO's senior executive staff who such function-specific roles that they did not have sufficiently broad experience to advance to the CEO role as their next career move. Because succession planning was completed so far in advance of the projected CEO replacement, these individuals had the opportunity for cross-functional development to broaden its experience and thus improve their candidacy.

Executive assessment enabled the water utility to reap three important returns on its investment. The assessment

- identified member(s) of the current executive team with the highest probability of success as CEO replacement candidates;
- identified and acted on gap-closing actions to improve all candidates' capabilities; and
- focused leadership development recommendations as they applied to the strategic issues of the future.

In order to understand how succession planning helped these companies and how it can help your utility, it's helpful to know how it works.

WHAT IS WATER UTILITY–BASED SUCCESSION PLANNING?

Succession planning is not a list of names of replacement candidates on an organization chart. Many companies still believe they have done succession planning if such a list has been created and filed. Not surprisingly, these companies rarely refer to the list when replacement decisions must be made. Most water utilities begin succession planning when they see a potential risk to the business resulting from a lack of leadership continuity or they identify a concern about being able to recruit and retain scarce talent. Succession planning identifies the current and future leadership talent needs of the business and provides systems and processes for identifying, staffing, and developing talent for the near-term, long-term, and emergency needs of the utility. Some of our clients apply succession planning only at the top of the organization, whereas others extend it to include employees with crucial skills and high potential. It can be used to ease leadership transitions and prepare people to take the reins smoothly. The result of your water utility using succession planning over a period of time is that you will have the right people for the right positions at the right time.

WHAT'S THE RISK OF NOT DOING SUCCESSION PLANNING?

Only your senior team can decide whether any particular risk is a "real and present danger" to your water utility. One risk is that you may find yourself without a viable replacement candidate for a key job. Another is that the "logical" candidate may be missing required skills or attributes. This forces you to decide under pressure whether it is a more prudent to put that candidate into the position despite the readiness gap or to mount an outside executive search. In crisis and without a thoughtful prior evaluation of job requirements and internal candidates, it is difficult to choose the best option. Another situation we find is that—like Coke—the board and the CEO sometimes differ in their views of the adequacy of the CEO's chosen replacement. The earlier this is known, the more time is available to develop and evaluate potential candidates in a variety of ways. This is often done through a formal executive assessment of candidates. The formal assessment enables the board and the CEO to discuss mutually understood and shared candidate information and to decide on ways to close gaps and use strengths. Our clients often close competency gaps through challenging developmental transfers or special assignments, combined with targeted coaching.

For a water utility, another risk of operating without an executive succession plan is that the company will fail to harness and therefore retain its high-potential talent. Employees with high potential are motivated by challenges and opportunities for learning. But for them the learning curve may level off after their first few years or positions. At this point, without a process to identify individuals with high potential and manage their placement, such employees may become disenchanted. This situation becomes even more of a problem as the "war for talent" heats up. As McCain said at a recent industry meeting, "The competition for workers in the generation following the Baby Boomers will be fierce. We need to start right now convincing them that our jobs are important and rewarding."

Outside recruiters are regularly on the lookout for the best and brightest, no matter where they happen to be working at present. Research shows that the most common reason individuals with high potential give for leaving is that they didn't see a future for themselves with their former company. Even when their names appear on the succession plan, too many good people leave because they don't know that they are valuable to their companies.

HOW DO YOU GET STARTED?

Recognize the business priority of starting now. Water companies are excellent at contingency planning for an unknown future—at least in the areas of operations and engineering. When such a crisis hits, there is already a plan in place, roles have been assigned, and all available resources are applied toward doing versus figuring out what to do. The same level of planning and preparation is required to avoid the risk of losing leadership continuity. For example, a client utility applied the same operations level of contingency planning to its leadership continuity four years before an unprecedented leadership crisis. As their president stated "We had some sudden losses at the most senior executive levels that could not have been predicted. Our well-thought-out succession plans enabled us to make replacement decisions in a very short period of time from a strong slate of candidates, who had been previously identified, groomed, and tested on the job."

Start small. A focused effort has a far greater chance of success than trying to "do it all at once." Succession planning for the top executive positions requires time from executives and perhaps even the board. This means that the succession plan must (1) be right-sized to the perceived need of the organization and (2) clearly and quickly yield risk-reduction and performance improvement.

Plan must be clearly tied to the business. Because succession planning must compete for scarce executive time, it must be clearly tied to business benefits. The process that has worked for our clients is for the senior team to create or review the water utility's strategic mandate. By "strategic mandate" we mean the expected future conditions (technology, market, regulations, finance, security) that will affect the utility over the coming three to five years. Organizations regularly discover differing assumptions among members of their senior teams regarding these strategic mandates. These perspectives must be aligned to create a solid foundation and to ensure that the staffing plans are prepared based on the most likely future business leadership requirements. With the agreed-upon strategic mandate in place, there are a number of places to start small:

- Make a three- to five-year succession plan part of this year's strategic planning process.
- Choose one mission-critical issue for which having qualified staff is a significant risk factor or a competitive edge (e.g., strategic versus operational planning ability, experience with and knowledge of infrastructure maintenance issues).
- Create a succession plan for the senior team positions, including the CEO position.

Other water utilities, as well as other employers, will be competing for the same talent that you need. They will steal talent from you if they can. If your water utility starts now to develop its succession planning and talent management practices, it will have a head start on other employers. It will have a competitive edge in leadership continuity by retaining and recruiting talent more successfully than others.

IS SUCCESSION PLANNING A TIME-URGENT PRIORITY FOR YOUR UTILITY?

No one can answer this question except your senior team; here are some additional questions your senior team should answer.

- Are we prepared for an unexpected sudden loss of our CEO or other top officer? Do we have succession plans in place and candidates identified and "ready" or in development?
- Do we have the breadth of experience and background at the level below our executives to run our business for the next five to 10 years?
- Do we have an X-ray of our talent pool that tells us which mission-critical competency gaps to close and how to best retain people with those skills?
- Do we expect to be constrained by a lack of talent in any way over the next five to 10 years?

Ask yourself: "Would my utility be more like Coke or more like McDonald's if we were to experience a sudden loss of any executive team members, including the CEO? What about a predictable retirement? Have we planned so well—identified, evaluated, and developed our backup candidates—that this would be a seamless transition? As a result, would our utility be well-positioned to carry out our future strategies? Can we reduce our leadership continuity risk and therefore our performance risk?

Succession planning is as crucial as capital budgeting or long-term planning. It should be on the agenda for a senior team meeting at your utility soon.

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