CEO Succession Planning: A Strategic Journey

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> **Key Board Takeaways**
>
> - Research suggests that CEO succession planning benefits organizations and their chief executives, yet only half of boards do it at all and not all boards do it well.
> - Boards and their CEOs can view CEO succession as a continuous journey with multiple stages, from identifying potential future CEOs within the organization to buttressing a new CEO's early tenure to evaluating the success of past succession planning efforts.
> - Good CEO succession is proactive and future-facing, while also reflective of what's worked in the past and what can be improved. Done right, it:
>   - » Prepares the organization for an inevitable CEO transition
>   - » Drives strategic alignment between the board, CEO, and leadership team
>   - » Provides an impetus for strategic executive development
>   - » Facilitates and increases the likelihood of promotion from within

It's been said that a board's greatest responsibility is hiring the organization's next chief executive. One might presume, then, that CEO succession planning is a board priority. Yet, our discussions with hospital and health system leaders (reinforced by research[1]) indicate that only half have a formal CEO succession plan.

What's holding back the other half? CEO succession planning can be discomfiting for the individuals involved. For the incumbent CEO, succession planning raises the specter of their departure. It can be stressful for potential successors who now operate under the board's scrutiny—their growth and development having become a strategic imperative. Up-and-coming executives left out of the CEO succession planning process are likely to reevaluate their futures with the organization. (Boards can get out in front of this issue through broader executive succession efforts—a topic we will tackle in a future article.)

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The board must juggle these considerations amid its multiple priorities. In our conversations with chairs, board members, and CEOs, we have learned that incomplete or inadequate succession planning usually comes down to board prioritization—or lack thereof. In a post-pandemic era of evolving care models, debilitating workforce shortages, ailing finances, and heightened competition, directors too often relegate CEO succession to the back burner.

Precisely because of these challenges—and the strategic changes they prompt—no board can afford to bypass CEO succession planning. It is a strategic imperative not only for the future, but for performance in the here and now. CEO succession planning should not only begin early (i.e., as soon as possible no matter the current CEO's tenure) but never really cease; it's a continuous process, not an event. It's something a board should do as an element of strong governance—not always urgent but always important. Part of a good CEO succession plan is the constant development of the current CEO as the context around them changes. Even after a CEO's departure, the board should use the occasion to look back upon its past CEO development and transition efforts, evaluate them, and apply lessons learned to the future.

This approach transforms a periodic event into a development journey for the CEO, potential successors, and indeed the board itself—enhancing performance now while preparing for strategic needs in the future. Along this journey the board acquires increasing proficiency in the succession planning process.

The Case for CEO Succession Planning

CEO succession planning—when undertaken as an ongoing process—accomplishes numerous strategic goals:

- First, the obvious: **It prepares the organization for the inevitable, a CEO departure**. Whether via retirement, resignation, dismissal, or illness, up to 20 percent of healthcare chief executives leave their posts in a given year, surpassing figures from most other industries.[2] A sound plan will account for emergency situations and varying contingencies as well as outline what a future orchestrated transition looks like. With a comprehensive plan in place, the organization ensures a smooth transition of leadership and minimizes disruption to the business.
- **It provides a forcing mechanism to drive strategic alignment**. A strong CEO succession process begins with a deep understanding of the organizational strategy, looking ahead three to five years. Often, CEO succession conversations with the board uncover areas where directors are misaligned with one another and/or with the CEO and executive team, prompting the opportunity to create alignment. While that enables the board to agree on future needs and requirements for the chief executive, it also provides benefits beyond succession, improving their ability to support—and if needed, challenge—the current CEO.
- **It adds momentum for strategic executive development**. Baptism by fire is not a viable CEO transition strategy. The board can lay the groundwork for succession through coaching and development on the changing mindsets and skillsets needed at the CEO level.[3] More importantly, the board can link CEO succession to the identification of critical roles (which are rapidly changing in healthcare) and consider executive team composition and long-term career movement—all of which improves current performance while engaging, stretching, and developing your most talented executives.
- **It enables promotion from within—or clarifies the need to look outside**. While externally hired CEOs are often

1 Kathryn Peisert and Kayla Wagner, *Advancing Governance for a New Future of Healthcare,* The Governance Institute's 2021 Biennial Survey of Hospitals and Healthcare Systems.

2 ACHE, "Hospital CEO Turnover Rate Remains Steady" (press release), May 23, 2022; Eben Harrel, "Succession Planning: What the Research Says," *Harvard Business Review*, December 2016; and Molly Gamble, "Hospital CEO Exits Hit 4-Year High," *Becker's Hospital Review*, February 28, 2023.

3 Mike Ettore, "Why Most New Executives Fail—And Four Things Companies Can Do About It," *Forbes*, March 13, 2020.

brought in to "shake things up" or provide new energy and strategic vision, most organizations prefer a seamless internal succession—and benefit from it. CEOs hired internally tend to acclimate faster, have lower incidences of turnover, and even find more success.[4] Boards have the option for the best of both worlds by starting early. Long-term CEO succession planning can identify and bring in leadership talent well before the need, strengthening performance now while enabling new talent time to truly understand the organization.

Getting CEO Succession Right

Not all CEO succession planning is *good* succession planning. What defines "good"? It is:

- **Proactive**: Starts the minute you hire a new CEO, or (ideally) has begun well before.
- **Future-facing**: Reflects where the organization is going, not where it is.
- **Versatile**: Allows for multiple contingencies and regular modifications to account for changing internal or external conditions.
- **Developmenta**l: The individual(s) being groomed for the CEO role should benefit from the process, regardless of whether they ever become chief executive. It is not a horse race to benefit the individual who eventually noses in front.
- **Continuous**: CEO succession planning is an ongoing process that provides an opportunity for the board to engage with each CEO in a collaborative journey.

A hospital's or health system's CEO succession efforts should precede and succeed each CEO's tenure. In between are myriad opportunities for the board to embrace its responsibility for succession:

- Identifying high potentials who may one day become CEO
- Overseeing the development of these executives
- Conducting a search (if needed) and formally selecting the next CEO
- Executing the handoff between outgoing and incoming CEOs
- Directing the launch and onboarding of the new CEO
- Evaluating the success of previous CEO succession efforts to inform future ones

One might argue that this much involvement qualifies as board overreach. We maintain that the more comprehensive the board's management of succession, and the more involved it is in the multiple steps and stages of a robust succession process, the better it can fulfill one of its chief functions: to mitigate organizational risk.

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Supporting the Start of a CEO's Tenure

Foremost among these risks is CEO failure. Just three in five newly appointed CEOs live up to performance expectations in their first 18 months.[5] Some 30–45 percent are regarded as disappointments, due primarily to issues relating to organizational politics, culture, and people, increasing the likelihood of an early exit. The cost of a CEO *failing to launch quickly* can also be negative. More than half of externally placed CEOs and a quarter of internal hires admit that it took them at least six months to have a real impact.[6] The consequences of a slow start include:

- Questions about the credibility of the placement and board's decision
- Lost momentum on important initiatives, due to lack of clarity on the leadership team on strategy, structure, accountabilities, and KPIs
- Loss of confidence both internally and with other key partnerships
- Aggressive response from key competitors

"Given the stakes, it is surprising how little good guidance is available to new leaders about how to transition more effectively and efficiently into new roles," notes Michael Watkins in *The First 90 Days*.[7] All of which makes the case for CEO succession planning that includes robust onboarding and ongoing development for the newly hired executive—and their team.

Looking Back

Finally, we recommend that each board review its succession efforts approximately a year after the new CEO begins. This allows questions to be asked and answered that benefit from hindsight:

- Was the CEO transition smooth and, if not, what hurdles or hiccups can be avoided next time?
- Related to the above, did the outgoing CEO help or hinder the transition?
- Did we lose strategic momentum? Which projects and priorities suffered, and why?
- What was the collateral damage or fallout of the changeover? Did morale or culture take a hit? Did we lose key talent?

The importance of CEO succession planning as a core function of good governance can't be overstated. Yet many boards haven't done it and those that have are often less prepared than they believe.[8] Our advice is to place it as a standing item on the board's agenda and to keep it there. CEO succession is an opportunity to prepare, proactively and holistically, for inevitable turnover at the top while improving performance today.

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4 Scott Keller, "Successfully Transitioning to New Leadership Roles," *McKinsey Insights*, May 23, 2018; Claudio Fernández-Aráoz, Gregory Nagel, and Carrie Green, "The High Cost of Poor Succession Planning," *Harvard Business Review*, May–June 2021; and Development Dimensions International, "Leadership Transitions Report 2021."
5 Strategy& (PwC), "CEO Success Study," 2018.
6 Keller, May 2018.
7 Michael D. Watkins, *The First 90 Days: Critical Success Strategies for New Leaders at All Levels*, Harvard Business Press, 2003.
8 Elena Lytkina Botelho, Shoma Chatterjee Hayden, and B.J. Wright, "Beware the Transition from an Iconic CEO," *Harvard Business Review*, February 1, 2023.