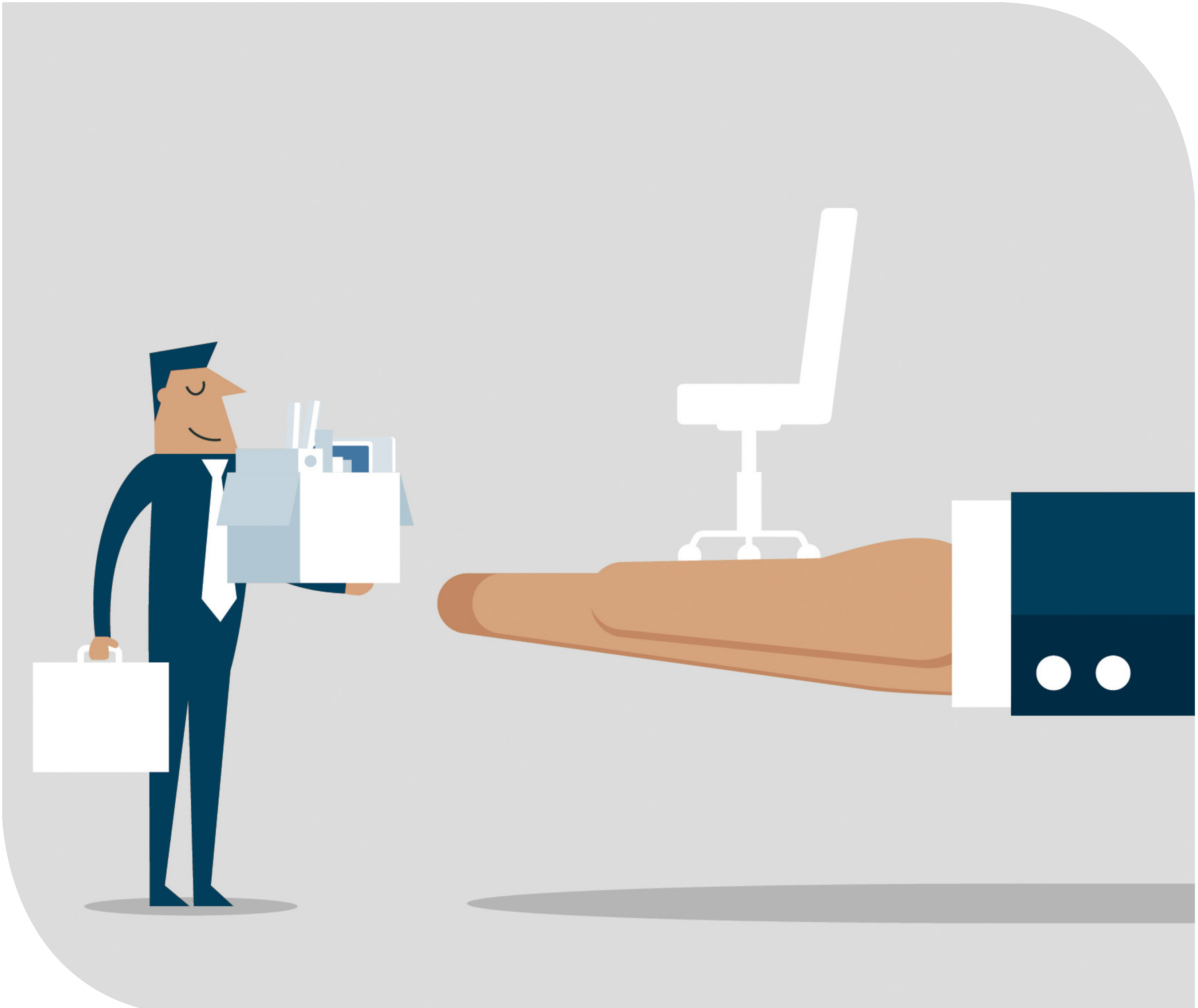


The 5 Stages of Succession Planning

Succession Planning for Small to Medium-sized Companies

Fifth Third Bank

The difference between a well-planned transition and a poorly planned and executed succession can have an outsize impact on any business.

This white paper looks at the five stages of succession planning that private companies typically need to navigate. It covers many different ways to transition a company, from an outright sale to an employee buyout. It also delves the timing of a transition, the communication needed throughout and the importance of internally grooming potential successors. It proposes an order of events, but elements of that order could change based on individual circumstances.

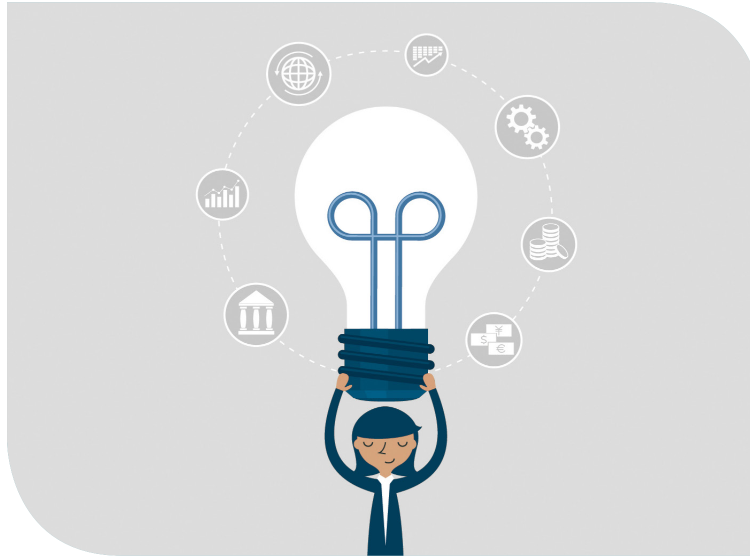
Introduction: Making Planning a Priority

The long-term success of a company depends, in large part, on how well its leadership plans for the succession of its CEO. If the transition is well executed, the business can not only continue on a predictable course, it can thrive under new leadership. When succession planning is an afterthought, however, the risks for a company run high. A poorly-executed exit can damage employee morale; jeopardize customer relationships; disrupt operations; limit access to capital and potentially do lasting damage on the long-term prospects of a business.

Succession planning should be a priority for all companies, regardless of size. Indeed, for smaller companies, disruption of team dynamics, sales and leadership can create a proportionally greater impact than on enterprises. Likewise, boards and investors in larger companies prefer seamless continuity over rocky transitions that shake investors' confidence.

Map Out the Ideal Exit

Business owners dedicate time to outlining strategies to grow their businesses but often neglect to create a plan for handing over what is likely their most valuable asset. Ideally, owners will begin to think through the succession process years before they put the plans in place, with these three steps in as their guide.



Write a Succession Plan

Just as business plans may change to reflect dynamics in the marketplace or within the organization, so too can succession plans. Even so, every business leader should think about and document his or her vision for eventual succession. At the same time, the process of thinking through succession is in itself beneficial, as documenting such plans can help minimize confusion or infighting should something unexpected happen.

Do a Business Valuation

Although succession planning doesn't necessarily entail selling a business or shares, the value of the business—or the metrics by which it is valued—often does play a role in the process. There are many common methods for arriving at a fair value for a company. Different valuation models—asset-based, capitalized past earnings, discounted future earnings, and market value approaches—can yield vastly different outcomes.

By bringing in a qualified, experienced, independent third-party to evaluate a company's market value, a company removes its subjective bias and unearths the same perspective from which its potential leaders, owners or investors will see the value of the business.

Be Strategic about Timing

The timing of a transition is also critical. Good timing makes it possible for leaders to focus on the benefits of the transition instead of casting it in a "sinking ship" narrative. In mapping out their success plans, owners should try to time the transition for a period when the business and its industry are on solid ground.

Explore Different Paths

For private companies, succession planning can take many forms, including the sale of a business or partial buy-in. As part of the succession-planning process, owners should strategize with trusted peers, board and family members to look at the pros and cons of different exit strategies. Common transition plans include:

Selling to a Co-owner

This can be the easiest path to succession, as the co-owner is a known entity to the company and the board. A co-owner will likely know the intricacies of processes and procedures, reducing the transition training time and cost. Some of the top considerations will be how much stake you have in the company going forward, whether you take a position on the board and/or keep an equity stake as a vote of confidence.

Passing the Reins to an Heir

Handing down the business to an heir works well when there is a clear heir who has worked within the company and who has been groomed for the top position. The possibility of more than one qualified heir in the same generation could cause a company-wide disruption, with lines drawn along allegiances. Owners should begin training and assessing early, and be transparent about the ongoing results and ensuing expectations.

Grooming a Key Employee

Promoting a key employee rewards hard work and demonstrates an internal line of succession with a company. It can be good for overall morale if there is a clear choice to rally behind. If the promotion to CEO of one employee leaves other hopefuls mystified and resentful, expect those overlooked to move on to another company, and possibly a direct competitor, if it isn't prohibited by contract.

Bringing in an Outside CEO

The value of an outside CEO often signals a change of course. If a transition includes a needed shift in culture or industry re-alignment, this may be the best option. Take, for example, a legacy business that needs a tech overhaul to remain viable. A new CEO who has successfully led a tech-driven company in the industry would send a stronger signal to employees that positive long-term changes are underway.

Organizing an Employee Buyout

Another little-used option is an employee buyout, in which the retiring CEO, along with an advisory board of key employees and outside professionals steer the company under a democratized model. Though some small companies have successfully transitioned to employee-owner models, this is, perhaps, most time-consuming process and often involves a significant culture shift.

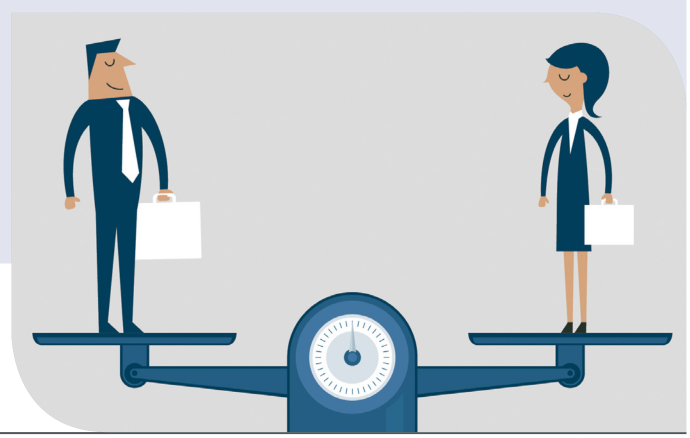
Train New Leadership

Succession plans can and often do change between the time an owner maps out the ideal course of action, identifies viable options and begins to make concrete plans to step aside. No matter how the succession ultimately plays out, it makes sense for owners to think about how to groom the next generation of leaders. Key steps include:

1. Training, mentoring opportunities for internal candidates. Every company should have a process for educating, mentoring and training and measuring a company's potential next CEO. Best practices will align corporate training with the future direction of the company.

2. Matching the candidate's skills with the next phase of the business, which may include fundraising, expansion, sales, etc. Depending on business priorities, leaders will want to weigh the pros and cons of promoting from within versus recruiting outside the organization.

3. Consider other key employee development. Succession isn't simply about the top officer. A succession done correctly will tie key employees to ongoing training, advancement and engagement beyond the succession. Develop these employees through training and valuable work experience so they're ready to take over leadership positions when the time comes.



Communicate Your Plans

As important as considering the right kind of succession plan is communicating it to employees and the marketplace. During succession, a communications team leader should be identified to create a plan for when and how key moments are communicated to different constituencies, such as employees, shareholders, leadership, the board and the general public.

An Internal Candidate

When naming an internal candidate as the new CEO, the transition team should not take for granted that everyone knows this employee or his or her capabilities and ideas for leading the company forward. For example, it's important to communicate why the chief marketing officer, as opposed to, say, the chief financial officer, makes a better fit for the direction of the company. The company may be entering a phase of increasing brand competition and a CMO will be a better choice. Alternatively, if a company is contemplating more rounds of investment in the near future, stakeholders may be more confident in the promotion of a CFO than a CMO.

Communication takes verbal and non-verbal roles, from press releases and internal emails to working lunches and proximity of the successor to the outgoing CEO. Ultimately it's important for leaders to be direct and transparent with their teams. Rumors grow in the dark.

An Outside Candidate

Hiring an outside candidate for the top job takes more communication finesse and listening. It's critical to be transparent with employees early so they don't think their jobs are in jeopardy as a result of new leadership. This includes communicating why the company needs a change of leadership and why now. The will create a well-defined welcome space for the new CEO, who has experience and expertise navigating the changes that the company needs.

The new CEO communication should inspire the team to join his or her vision and want to work toward that end. Constant communication, especially throughout the transition, is key.

See a Succession Through

Planning and communicating are only part of the process. The crux of a succession plan is the execution. This begins with setting clear expectations and creating a process designed to help the next generation of leaders put its best foot forward.

Work Alongside a Successor

On day one of the new CEO's job, he or she will have a guide to how things are currently done and make decisions about whether to maintain or tweak those procedures. Allow time for the new CEO to meet with the board, key managers and sales teams.

Lean on Top Managers

It's important to empower top managers to take on more leadership through the changes. Those who indeed rise to the challenge will become valuable resources to the new CEO.

Set Transition Business Goals

The new CEO should not get a pass on accountability and progress. Set reasonable goals for the first 100 days under new leadership and track progress toward those goals periodically with the board and the new CEO. Setting and monitoring early goals will help the incoming CEO remain on track while in the glow of the new job.

Create a Plan for Post-transition

Succession is an ongoing process for the most successful companies. The role of the CEO and company boards is to grow the company. Large disruptions of leadership can lead to stakeholder doubt and loss of revenue. CEOs and boards can instill confidence by continuously grooming new leaders within the company.

After a major transition has taken place, more communication is needed to reinforce employees in their roles, to maintain the company's culture or to articulate culture shifts. When it comes to post-transition communication, more is better.

Conclusion

At the end of the day, successful transition planning is an ongoing process within a company. Defining where the company is heading and what kind of candidate is best qualified to get it there is paramount. Communication, timing and understanding this transition as an opportunity to preserve and grow a company's value is the right mindset. A CEO's legacy does not end on the day he or she changes titles. The best CEOs know that indeed this just the beginning.