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THE STONEWOOD PERSPECTIVE

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So You Are Taking Over From The Founder…

Canada abounds with great entrepreneurs for whom succession is the most significant future threat their companies will have to overcome: Magna's Frank Stronach, Roger's Ted Rogers, Bombardier's Laurent Beaudoin, Four Season's Isadore Sharp. When planned and executed well, as in the case of Microsoft and Dell in the U.S, or Biovail, Cognos, and Tundra in Canada, succession builds on the success of the founder and increases the company's ability to create shareholder value. When not, it can have explosive effects as in the case of firms such as McCain's and CARA.

The transition from a founder to a professional manager is risky business. In the world of executive search, we are often asked to help companies find the right person to succeed the founder. During such projects many successful professional managers will simply refuse to participate, preferring their current roles to the uncertain roller coaster of stepping into a founder's shoes. Yet others will proceed with the dangerously cavalier attitude that these situations do not differ appreciably from others they have successfully addressed in the past.

At the centre of any transition is the founder and it is vital to understand the founder's mindset before even attempting to facilitate a succession. This article covers some of the key issues which require consideration in order to increase the likelihood that the hire will be a success in the long run and that a successful founder transition can be achieved. These include:

How much of the founder's self image is related to being the head of the business? This is an intangible but absolutely critical. People who have made significant sacrifices to build their businesses are less likely to be emotionally equipped to make the transition to retirement or a non-key role. Outside interests in family, hobbies, travel or even other businesses are a key to assessing whether the emotional step is possible. While it may be difficult to determine, any successor needs to understand the founder both at work and in their personal life.

A founder I know had talked about retiring for two years and the succession plans were in place. The partners who were going to take on the management of the business were ready to go and all was in order. The founder, a noted workaholic with few outside interests, including family, took extended holidays to acclimatize himself to being away from the day to day operations. However, upon returning, he appeared unsettled and returned to a very heavy workload. Two months before his planned retirement he announced to an assembled group of partners and successors that he was ***not*** going to step down. The resulting brouhaha was expensive both in terms of shareholder value and personal integrity for all concerned. Many of the supposed successors left the company and took valuable clients with them. The remaining business encountered tough times as clients were ignored during the turmoil, employees became demoralized, and several new employees were laid off. The final result was a smaller, less valuable firm that was put on the auction block at a much-reduced price. The ultimate irony is that the founder had created a human resources consulting firm that earned significant fees counselling companies on succession planning and management of the process.

Another founder I had the pleasure of working with was quite the opposite. He had a strong family life, current and engaging hobbies and other small businesses that needed the attention of their owner. His successor was very glad to find a person who was looking to help him learn the ropes and succeed in his role. After a few months on the job the founder moved very successfully to a clearly defined chairman role, cleaned out his office and moved to a different location. After a couple of years both the founder and his successor are extremely happy with the situation and they have enjoyed some growth due to strong markets and new ideas.

The nature of a founder is to be incredibly passionate about building his or her business and there has to be something or someplace for that person to go to, whether it is neglected hobbies, travel, charity, volunteer work, or board participation. If those plans are tentative or do not exist, it might be extremely difficult for the founder to stay away from the business. Any successor has to understand this about the founder and it will only be through careful due diligence that an assessment can be made. Meeting with other executives, and dining with spouses can be critical steps in that due diligence.

Who is driving the process to replace the founder and what is the ownership structure? Many boards have found their chosen successor sabotaged by a founder that did not want to move out of the top role. Some founders are quite happy to step aside and make room for their successors but others are not. Many founders are forced from their critical roles by a board that is frustrated with some aspect of growth or management style. Stepping into a feud between a founder and other significant shareholders is a minefield and even if a professional manager proves successful it will be a difficult and painful process. If there are core business issues that need to be addressed then the professional manager had better ensure that he or she has the right skills and the mandate to make the changes.

In the end it all comes down to the ownership structure and who has the most votes. If the board is driving the process against the wishes of the founder then any successor had best ensure that they have a majority of the votes at the board. With the increased use of preferred shares in recent years this gets to be a sticky situation and can lead to deadlock. Board loyalties can be mixed and fragile. This is further complicated by the fact that, in some cases, super-majorities are required for some critical decisions such as the hiring of a new CEO or the restructuring of a business.

Successors need to do the appropriate due diligence in terms of the share structure and ownership positions and the various rights that shareholders retain. Once the facts are known, the successor needs to examine the process that led up to the decision to replace the founder and get a sense of the political landscape. Only when those elements are properly assessed and factored in will the successor be able to assess the overall volatility and risk inherent in the situation.

What are the founder's children doing? Like it or not we all have a strong desire to ensure that our children are secure. Individuals who build businesses often have strong and unrealistic expectations to involve their offspring in the family business. Any decision on founder succession will be coloured by that individual's desire to ensure that their gene pool enjoys the benefits of their labour. If all of the children have well-established careers in other industries then there is a good chance that a successful transition to external management is possible. If, on the other hand, the children are working in the business and moving steadily through the ranks, any president or CEO from the outside will likely have challenges.

In 2002 the newly appointed Chairman of Rogers Cable, John Tory, was widely believed to be the successor for Ted Rogers Sr. at the telecommunications giant. But by 2003, John Tory was moving out of the organization and into politics. If he had aspirations of being the CEO of the whole Rogers organization they were certainly not going to come to fruition. Within a few months of his transition another senior executive, Alek Krstajic, was making tracks for the door and commenting that "Ted has put together his team, unfortunately I didn't have the prerequisite for a job there, which is the last name of Rogers." Even if Ted Rogers Sr. was planning to make the transition to professional management, it is very evident that Ted Rogers Jr. will play a key role in that team.

Of note, the current President of Rogers, Nadir Mohammed, has a more philosophical view of the CEO role. He has been quoted as saying that if the time comes that he feels he is not being fully utilized then he hopefully will have earned the right to pursue the many opportunities available in the industry. Ted Rogers Sr. has delayed his retirement twice already and his children are gaining experience every year, so Nadir's aspirations are rightly kept in check.

What was the founder's magic? Founder's shoes can often be incredibly difficult to fill. They are often people that see opportunity where others do not. These are the scientists and engineers that can see a business problem and understand how to create technology and innovation that can be harnessed to solve the problem. They couple that with the drive and energy to take the risk, create the solutions and get them to market. There is no amount of schooling or training to re-create that ability. Any successor had better have a careful look at what the founder does and how he or she does it. If the founder has been the visionary for the product development and this has sustained the company, the successor had better be equally good or know someone that can fill the gap. If the founder maintained all the key external relationships then the successor had better determine quickly if he or she can sustain and grow those relationships.

Any founder will set the tone for the business that can create sustainable value. The extent to which the magic has been woven into the fabric of the business and maintained by the staff will often determine whether a successor can succeed without being a replica of the founder. The irony is that to be completely successful in creating a longstanding business there comes a time when the founder has to be completely redundant. The challenge of making oneself redundant after possibly decades of being the key executive is huge. Successors have to look carefully at how closely the founder influences the day to day business and how much of the business is run in a systematic fashion by other key staff. If all the decisions and key revelations are still taking place in the founder's head, then the magic has not been transferred to the business and the successor will have a tough time.

There are some options in this circumstance and some highly successful founders who built the company on incredible product development have gone back to the lab or a research role, while a successor has run the overall business. If the founder's magic has not been institutionalized then the successor had better figure out a way to replicate or somehow retain it for the company.

Is there a clear timetable for the transition? Many executives have been lured to second in command or COO roles with promises of a succession and a founder that is going to move to a less active role. Often times those promises are made without a firm plan. Any resistance to defining a new role and creating a plan for a transition should be viewed with utmost scepticism. Keeping things vague will pave the way for the founder to re-enter the mandate created for a CEO or worse, never relinquish any true authority. Another key element of this is whether the founder intends to move his or her office. If the person is determined to maintain a physical presence, particularly if there is no management responsibility, then there is a very strong probability that succession will be a failure.

A colleague of mine recently recruited an individual that had been in a COO role for two years following a series of promises by the founder to create a transition to the CEO role. There were promises of equity and increased authority that kept getting delayed or deferred. After two years of vague promises of "someday" the executive was very open to our call regarding a CEO search we were conducting.

An executive I interviewed a couple of months ago had been the CEO of a small manufacturing company in southwestern Ontario, a role in which he succeeded a founder. The entrepreneur/founder had been diagnosed with a severe illness and wanted to undertake some challenging medical treatments and spend time with family. The day before he moved into his office the founder moved out, taking all her furniture and effects with her. She only came back to the plant on occasion and preferred to have lunch with her successor off-site. This gave an incredibly clear signal to all involved that the successor was now the key executive and was going to run the company. What the successor was unaware of though was that the founder transferred her majority ownership stake to her son, who happened to work in the sales and marketing function of the company. Within a year the son was running the business and the chosen successor was back looking for a new role. So while the successor had ensured that he had a clear signal to run the business he neglected to fully understand both the family dynamic and ownership structure. His due diligence was not as complete as it needed to be.

While the transition from a founder to a professional manager is extremely challenging and fraught with risk, there are times when the transition can create an incredible opportunity. As with any new CEO role considerable due diligence is required on behalf of the candidate to ensure that the company has a good management team, is reasonably well managed, and sustainable. In the situation where the candidate is succeeding a founder there is an extra level of due diligence required that will sometimes take the successor into some very personal issues. But with the appropriate due diligence, successors should be able to understand whether the situation is likely to be a great opportunity or a recipe for frustration. According to the Canadian Federation of Independent Business the Canadian economy has a large number of founder-led companies with aging leaders. If a candidate to succeed a founder can distinguish between a recipe for disaster and a chance of a lifetime, then there is a wealth of opportunity in the employment market.

About the Author

Paul Hudson is Vice-President in StoneWood's Toronto office. Paul has eight years of executive search experience including six years with a major multinational firm. He specializes in serving technology clients and has worked primarily on assignments in the software, hardware and professional services industries. His clients have included early-stage companies as well large, established firms.

Paul earned a B.A. in psychology from the University of Manitoba, a B.Sc. in mathematics and physics from the University of Guelph, and an M.B.A. degree from Simon Fraser University.

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