HOW

After losing two CEOs in rapid order,

McDONALD’S

McDonald’s revamped the way it does succession.

PLANS

How a global company became best-in-class.

AHEAD

By Deborah L. Jacobs

McDonald’s Corporation had taken initial steps to revamp its succession plan when a tragic sequence of events tested its bench strength. Gathered with more than 12,000 franchisees, suppliers and employees in Orlando, Florida for the company’s 2004 worldwide convention, James R. Cantalupo, the chairman and CEO, died of a heart attack early on the morning of April 19, hours before the day’s proceedings were to get underway.
Board members, most of whom had come to Florida for the convention, were alerted of the news at 5 a.m. and quickly convened an emergency meeting. By the start of the business day, they had appointed Charles H. Bell, a 44-year-old Australian who had spent his entire 28-year career at McDonald’s, as the youngest CEO and the first non-American to head the company. That afternoon, he delivered the opening address that Cantalupo had been scheduled to give.

But six months later, Bell too was gone; he resigned after becoming terminally ill with colorectal cancer. Again, there was a successor in the pipeline. James A. Skinner, who had begun his career at McDonald’s 33 years earlier flipping burgers, was promoted from vice chairman to CEO in December 2004, a month before Bell died.

Skinner was the last surviving author of the company’s “Plan to Win,” a turnaround program designed to address an unprofitable period that led to Cantalupo’s return. The plan, whose other authors were Cantalupo and Bell, listed “attract and retain the best talent” as one of the company’s “must do’s.” The time Skinner took the reins at the end of 2004 following Bell’s brief tenure, there had been four CEOs in just two years.

Since then, the leadership development process has continued to evolve. One crucial step was to create a Global Talent Management group within the human resources department. The group now oversees the succession process for roughly 1,400 positions worldwide — officers, senior directors and directors — the feeder pool for officer roles. David Small, who was promoted to head the group in July after four years of grooming, says that when these jobs turn over, 90 percent are filled from within the company.

Meanwhile, McDonald’s has undergone a wholesale reorganization to implement the principles of the Plan to Win. Responding to competition in the fast-food industry and a growing focus on healthier eating, it made several key acquisitions and began to rethink its business strategies.

Having executives in house ready to become CEO during the back-to-back tragedies of 2004 was essential to revitalizing the company, says Richard R. Floersch, head of the company’s human resources department. If an outsider had been hired instead, there is a good chance that the Plan to Win would have been abandoned in favor of a different strategic path, he says.

Still, for the process to work, “ready now” candidates must be at least as strong as the people they would replace, Floersch says. And that makes some people uncomfortable. In a conversation several years ago, Skinner asked a manager whether his “ready now” candidate met the standard, Floersch recalls. When the manager hedged, Skinner told him that if the candidate did not yet meet all the requirements of the position, then he should be considered a “ready future” — not a “ready now.” If the manager’s position were to open the next day, a candidate should be sought from outside the company, Skinner said.

Catalyst for Change

The succession pipeline that produced Skinner had begun to be reconfigured six years earlier. The catalyst for change was a mandate from the board. In 1998, after Jack Greenberg became CEO, the board asked for a succession plan that would identify two successors for each key spot — “one ready now, one ready future.” The future candidate was to be ready within two years.

With hindsight, the board directive seems prescient. Greenberg, who had beaten out Cantalupo for the CEO job, stepped down at the end of 2002, just before McDonald’s announced its first quarterly loss as a publicly traded company. Cantalupo, a retired executive with 28 years of service, was brought back to head the company but died 16 months later. By

TODAY, THERE ARE “ONE READY NOW, ONE READY FUTURE” FOR 79 PERCENT OF THE
Every December, Skinner, president and COO Ralph Alvarez and senior management now assess the performance of the top officers. They rank each individual's performance during the preceding year using the 20-70-10 model, identifying the top 20 percent of performers, those in the middle 70 percent and the bottom 10 percent.

Evaluations rely on multiple points of view rather than on a single boss's perspective. Supervisors need to defend evaluations to their own peers. And others can weigh in with information about their experiences with the person being reviewed.

An “improve or remove” leadership development plan is then formulated. Ideally, it focuses on what people need to do better in their current positions or to be ready for advancement. Meanwhile, supervisors who are not familiar with the work of the high performers are expected to get to know them.

Calibrating evaluation standards has been crucial to bringing the company closer to its readiness goals, Small says. Today, there to be successful in their current job or the next one.

McDonald's leadership development programs include an educational component. A special accelerated development program, targeted at the top 264 high-potential directors, senior directors and officers, is designed to enhance leadership capabilities. Participants learn to have candid conversations with subordinates during performance evaluations and otherwise hone their skills at coaching and developing talent.

Rather than send employees to offsite leadership development programs at prestigious universities as many other companies do, McDonald's runs its own. These programs combine instruction by the company's executive team with speeches by outside experts. The goal is to provide a natural link between

**TOP 50 POSITIONS.**

are "one ready now, one ready future" for 79 percent of the top 50 positions. The target is 100 percent.

**Getting Better all the Time**

At the heart of the McDonald's succession process is a culture that favors continuous improvement and demands that every employee get better each year. Written guidelines were introduced for employees in the United States, Australia and the United Kingdom in 2008 and by 2010 will apply to all 1.6 million employees worldwide. They define eight leadership competencies that encapsulate the key skills and behaviors needed for business success. "Builds and leverages talent" is one of the items.

For each competency, McDonald's clearly defines what is expected. The guidelines even include a list of "contrary behaviors" like "overemphasizes proving oneself and does not give credit to others" and "does not apply consistent criteria and standards when making talent management decisions."

Talent management is premised on a familiar, predictable format developed from the company's study of best practices elsewhere and adapted for the culture McDonald's is trying to create. It starts with the drawing up annually of an individual performance plan that focuses on an individual's goals and objectives and is reviewed at least once, at midyear. Separate individual development plans describe what individuals need to do leadership development and the company's business strategy, something that might be harder to achieve if executives went off campus for their instruction, Floersch says.

To varying degrees, the same process is followed at lower levels of the organization, Small says. Talent management is so much a part of the corporate culture that it usually extends to the restaurant level as well.

However, there are no guarantees of promotion. Whether someone is promoted depends on many variables. "We're very clear with people who go into our high-potential accelerated programs that this program is not designed to get you promoted; it's designed to help you step up your leadership capabilities, to get you ready in case you're promoted," Small says. The promotion rate for the 264 high-potential leaders is about 40 percent.
McDonald’s rigorous process, with its up or out mentality, may sound harsh and bureaucratic, but the company’s retention rate is high, says Small. The turnover of top talent is less than 2 percent per year, perhaps partly because McDonald’s is creative about letting people move into different kinds of positions, even if those moves are lateral. Perks like incentive stock options and restrictive stock also put some glue on the company’s talent.

Talent Management. Working with Skinner, Alvarez and Floersch, the group drafts a succession plan for the top 30 positions that is presented to the board each July.

Succession planning to develop a company’s future leaders, with the human resources department serving as trustee, has succeeded at other businesses, just as it has at McDonald’s, says Charan. But reaching the point where a company can have “one ready now, one ready future” is the outcome of a “bigger social process” in which people develop relationships working together, he says. In the course of these interactions, they can observe and acknowledge each other’s strengths.

The purpose is not only to find successors but also to create a culture that identifies and nurtures talent, Charan notes. From this process, successors will emerge. In the meantime, this vehicle “muscle builds” the organization with talented people. “The process should go from bottom up also, starting with the line leaders and staff leaders — not just from the top,” he says. “The process is bigger and longer and deeper than just the succession for the top. It is a methodology of building the talent pool for the future.”

While companies often publicize their promotion policies, the specific people who may move up should not be disclosed until a company announces its appointments, Charan says. The board should be informed about candidates for high-level positions, as should the candidates themselves, but no one else should know of the company’s intentions.

Board Involvement

“The most important thing any board does is pick leadership, starting with the CEO,” says Andrew J. McKenna, nonexecutive chairman of the McDonald’s board since 2004. And the company’s board devotes most of its July meeting to the subject. Since the culture at the company favors homegrown leaders, only internal candidates are considered, McKenna says.

The meeting starts with a presentation by Skinner, Alvarez and Floersch on the company’s progress in developing leadership in the past year and future plans. Alvarez and Floersch talk about the performance of the individuals in the top 15 leadership positions and the succession candidates for these jobs. Then Skinner presents his assessment of the candidates developing for his position.

Following these presentations, the board meets in executive session. Since McDonald’s is a global company with 32,000 restaurants in 118 countries, the board looks at talent throughout the world. The objective is to follow the progress of individual candidates — what they have done, what they might be able to do and the likelihood that they will move up, McKenna says.

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To follow up, board members try to get acquainted with those individuals they do not already know. The process is “a great opportunity for the board to become familiar with the candidates for senior positions, and as time goes on, they may well become candidates for the most senior position,” McKenna says.

Jeffrey Sonnenfeld, head of the Chief Executive Leadership Institute at the Yale School of Management and author of “The Hero’s Farewell: What Happens When CEOs Retire” (Oxford University Press, 1988), says there are additional advantages in hiring internally. When the board makes hiring decisions, there is an “unconscious bonding between outside candidates and the nominating committee” that can make the outsider overly dependent on the group responsible for the hiring decision, Sonnenfeld says. Inside hires are more independent and have “a considerably stronger network and knowledge base than even the director has,” he says.

Sonnenfeld notes. In fact, an enduring culture can help people get past a disappointing quarter, he says.

**Does It Translate?**

The willingness of McDonald’s to invest in its people is “in some ways a refreshing model and in some ways a reminder of how many great companies lost their way,” Sonnenfeld says. As recent events in the financial industry illustrate, the “disposable employee mindset matched with excessive short-termism has been destroying U.S. business strength,” he says.

But grooming leaders internally rather than speculating about whether an outsider’s skills are transferable, as McDonald’s does, is something only about a dozen American companies do well, Sonnenfeld says. These companies appreciate that “you have much better performance data from the people within—you know who is riding the coattails of others, who

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**TO FIND SUCCESSORS**

**CULTURE THAT IDENTIFIES AND NURTURES TALENT.**

Boards that favor outside hires are shortsighted in various respects, he says. There is no reason “to believe that somebody else’s leadership development program is going to work better than yours,” he notes. And bringing in outsiders to fill the top positions becomes “a demoralizing thing that goes cascading down the ranks.”

**Personality and Politics**

Even the best-designed succession process, however, will occasionally bump up against workplace dynamics and human frailty. “There’s always a level of threat to this because basically everyone here is expected to find their replacements,” says Small. But, he adds, “This isn’t just a fun exercise or a HR practice. This is critical to running your business. Especially now, intellectual capital is the differentiator. Anyone can go out and copy our business model. They can’t copy the people who know how to run it well.”

The hiring process at McDonald’s fosters a collective culture by selecting for candidates who are willing to put the good of the organization ahead of individual ambition, says Floersch. Team building starts at the restaurant level, where McDonald’s serves 58 million customers per day, he notes. “If you have a lunchtime crush going on, you have to depend on the team, as opposed to one individual in the store,” Floersch says.

At companies where there is an “appreciation for the common good, you don’t have a lot of pride of authorship,” Sonnenfeld observes. When there are successes, the glory is shared. But when things go wrong, “you don’t have a vilification, finger-pointing culture,” like the ones that have surfaced at various troubled companies in recent years. McDonald’s has maintained its succession process through good times and bad, deserves credit for successful teams and who were the stars on failing missions who perform superbly but were given a losing hand,” Sonnenfeld says.

Charan, the author and management consultant, says the process McDonald’s uses is very transferable to other companies, though the details of the process, like the various criteria for advancement, will vary. For example, a company that anticipates 50 percent or more future dependence on markets in China, India or Brazil would want to give future leaders experience in one of these countries.

Peter Cappelli, a professor of management at The Wharton School at the University of Pennsylvania and author of “Talent On Demand: Managing Talent in the Age of Uncertainty” (Harvard Business School Press, 2008), is skeptical that the McDonald’s model will translate to most other companies. In a company that is a leader in its industry, people might be willing to wait patiently on the bench hoping for “a shot at the very big time,” he says. Elsewhere, other opportunities might cause them to jump ship.

This succession model also does not work when a company is changing rapidly because it is restructuring or responding to volatile demand for its products, Cappelli says. “Introducing salad is a trivial change compared to what you see in other industries,” he says. While McDonald’s is “ideally suited for reasonably predictable internal succession,” at other companies “by the time a successor has grown, the business has changed in important ways and the person you had developed for that job no longer fits.”

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Deborah L. Jacobs is a financial writer who has contributed to many national publications, including The New York Times and BusinessWeek.