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FROM FOUNDERS TO FIRMS: AN EXAMINATION OF THE INSTITUTIONALIZATION OF CEO SOCIAL CAPITAL

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Bret Ryan Fund

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The dissertation of Bret Ryan Fund was reviewed and approved* by the following:

Tim Pollock
Associate Professor of Management
Chair of Committee
Dissertation Adviser

Wenpin Tsai
Associate Professor of Management

Don Hambrick
Smeal Chaired Professor of Management

Forrest Briscoe
Assistant Professor of Management

Michelle Lowry
Calderwood Faculty Fellow Associate Professor of Finance

Denny Gioia
Chair of Management and Organization
Professor of Organizational Behavior

*Signatures are on file in the Graduate School

ABSTRACT

This dissertation provides a new theoretical framework introducing the concept of social capital transfer and explains how and when it occurs among individuals and organizations. I draw from a variety of areas of research to accomplish this task, including social capital, embeddedness, and upper echelons literatures. The structure of my dissertation will be as follows: Following an introduction into the core concepts of my work in Chapter 1, I will seek to develop the theoretical foundations of the broader concept of *social capital transfer* based on the social capital literature in Chapter 2. This discussion will be wider in scope than the Founder-CEO context I wish to emphasize, but the broad background is necessary to lay the foundation for empirically examining the topic within this specific context. Chapter 3 will discuss the relevant literatures that speak (or fail to speak, as the case may be) to the issue of social capital transfer in transitional events within a firm, especially with executive succession. From this discussion I develop hypotheses that will be tested empirically in the subsequent chapters. Chapter 4 will describe the methodologies to be used and the advantages and disadvantages subsequent of these methodologies. Lastly, Chapters 5 and 6 will report the findings of the empirical work and summarize the benefits that can be derived from this project.

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This work, while solely authored by me, is the product of countless personal interactions with my friends, family, colleagues, teachers, mentors, and practitioner contacts over the course of these recent years. In fact, it is interactions such as these that serve as the basis for my chosen topic of inquiry. In this volume, I examine the notion of social capital and its ability to be transferred from an individual to an organization (and vice versa). My interest in social capital (and its transfer) stems from my own contemplations and observations about how my personal network allows me to not only create and accomplish work beyond my own capacity, but also affords me the opportunity to do so in such a way that this work can and hopefully will outlast my brief moment in this journey we call life. It is therefore important to acknowledge a handful of the key individuals in my life who have made this particular research possible.

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My parents are of course to blame for my good genes (assuming, as I would like to believe, that I have them) and for my ambition and tenacity. My Mother always told me I could accomplish anything I set my mind to and in this case I have. My Father showed me what it meant to work hard for things and I hope I can live up to his example. My brother TJ has always been one of my closest friends and has talked with me for many hours about my work and how it applies to the real world. His advice and counsel has often provided new ideas or ways of thinking about issues or problems that I was grappling with in my research.

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Chapter 1

Social Capital Transfer: Introducing a New Concept

A fundamental issue of concern for both practitioners and academics alike is how organizations are influenced by the individuals that compose them. While some theories of the firm have injudiciously “black boxed” or atomized the individual actors who make up the firm (Williamson, 1975; Popkin, 1979), other theories have tended to over-emphasize or exaggerate the impact that social actors can actually have on organizational outcomes (Polanyi, 1944; Scott, 1976). Over the last twenty years, upper echelons research has attempted to bridge these polar worldviews. The upper echelons perspective argues that the firm is a reflection of the values and cognitive biases of its top management team (TMT), or dominant coalition. Thus, these actors play a significant role in shaping the organization's outcomes (e.g. performance and survival) (Hambrick & Mason, 1984; Finkelstein & Hambrick, 1996).

Within the upper echelons literature there has been a particular stream of research focusing on board interlocks and director networks which has empirically demonstrated that directors take their personal relationships with them when they leave (e.g. Palmer, Friedland & Singh, 1986). This stream of research illustrates an important fact of organizational life: while organizations can benefit from the social capital of their individual members, personal social capital does not necessarily become corporate social capital. While research has explored whether these broken ties have been reconstituted (e.g. Palmer, 1983; Stearns & Mizruchi, 1986), little has been done at either the board or executive level to seriously explore the processes through which these reconstitutions occur. A recent exception is a study by Westphal, Bovie, and Chng (2006) which examined how, by establishing a personal friendship with the CEO of a partner organization, a new CEO can effectively rectify an inter-organizational tie that had been broken by the removal of the founding CEO (Founder-CEO). While this research provides insight into one way in which organizational leaders may attempt to retain the social capital of a departing leader, it does not provide a comprehensive understanding of what firms can do to institutionalize a previous manager's social ties.

Upper echelons research has recently begun to focus on these issues—particularly in the context of new ventures. However, the pool of research examining the topic is limited. Much of the research concerning the Top Management Team's (TMT) ties in a start-up environment focuses on how functional experience and critical social ties affect a firm's strategy and action (Beckman, 2006; Beckman, Burton, & O'Reilly, 2007; Shane & Stuart, 2002; Roure & Maidique, 1986). While these studies provide insight into and evidence of the notion that founding teams' network ties do matter, they do not explain the process through which an individual's personal social resources become the social resources of a new venture. Thus, these studies provide little insight into how a firm is able to leverage the personal social resources of one of its key members. Further, they do not increase our understanding of the practices and organizational structures that might be used to assimilate and institutionalize these social resources. Increasing our understanding of these methods would help to reduce organizations' dependence on individuals for access to critical resources typically available only through social capital.

These omissions in the current literature leave a significant theoretical gap. Filling this vacancy in research will benefit practitioners as well as academics. Specifically, it is critical to increase our understanding of the mechanisms an organization can employ to institutionalize the critical social capital of its top managers that may affect its growth and survival. This important topic has not been adequately examined in either a start-up or large corporation contexts. For the purposes of this study I have chosen to restrict my efforts to the start-up environment—specifically to venture-backed firms—in an effort to understand how these mechanisms play out in the early years of an organization's existence. Prior research has identified these early days as a critical formative period that affects a firm's future growth trajectory (Baron, Hannan, & Burton, 1999; Nelson, 2003). Actions taken during this period may lead to more extreme outcomes for the firm depending on the manner in which the founder transition was carried out.

The succession of a Founder-CEO provides a rich context in which to examine the institutionalization of a CEO's personal social capital, as it introduces two issues that a new venture must resolve and/or make use of. First, the potential loss of a Founder-CEO (due to his or her replacement) may mean the loss of critical external resources that are needed for the firm's continuing growth and survival. Second, the injection of a successor CEO into the organization may disrupt old social structures within the company that had previously cultivated loyalty and shaped the firm's internal culture under the founder. Either of these problems can seriously affect the life and performance of a young venture; as a consequence, the Founder-CEO transition process becomes paramount in the eyes of the investors who manage it (Levensohn, 2006; Gordon, 2004.). I will explore these two issues in more detail in the following chapters in order to first provide the theoretical lens through which to examine the subject (Chapter 2) and then to formulate (Chapter 3) and test (Chapters 4 and 5) hypotheses that provide empirical evidence showing the critical importance this topic occupies in relation to both academics and practitioners.

Scholars have argued that the transition from a Founder-CEO to an outsider is potentially the most critical succession event in the history of the firm. Hofer and Charan (1982) stated, “After the starting difficulties have been overcome, the most likely causes of business failure are the problems encountered in the transition from a one-person, entrepreneurial style of management to a functionally organized, professional management team” (p. 2). Furthermore, Carroll (1984) found that the departure of a founder had a disproportionately negative impact on the likelihood of organizational survival. Clearly, the loss of a Founder-CEO affects the new venture’s ability to continue to grow and survive, but what the literature does not adequately address is *why* this appears to be the case. One reason may be that the venture is dependent on the Founder-CEO for critical resources that are provided through the use of his or her social ties. This research project will explore the importance of founders' social ties to new venture survival and the extent to which Founder-CEO succession puts these valuable social resources at risk. Furthermore, this study will begin to consider mechanisms for guarding against these risks.

As has been previously noted, although Founder-CEO transitions may lead to negative implications for the organization, the replacement of a Founder-CEO is intended to increase a firm’s value rather than to weaken it. Venture capitalists (VCs) must believe that such a change is needed in order to take the organization to the “next level” through more professional leadership. One venture capitalist has noted that a majority—almost two-thirds—of venture backed start-ups replace their Founder-CEOs (Levensohn, 2006), and a recent academic study similarly put this number at a little over sixty percent (Hellmann & Puri, 2002). Such a prevalent and critical event necessitates scholarly attention in order to ensure that such transitions are carried out effectively and efficiently. The role of VCs in a venture-backed firm generally goes beyond the obvious financial intermediary role and extends to a broader role in the professionalization of the company (Hellmann & Puri, 2002). In such a capacity, the venture capitalist can enact changes in the organization that can either strengthen or diminish the firm's ability to conduct an effective transition. One important aspect of managing this transition may concern how to appropriately capture and utilize important social contacts brought into the firm by a successor CEO. Thus, it is important to understand how both the loss of a Founder-CEO and the introduction of a professional CEO influence a firm's ability to access important resources embedded in the personal social networks of its managers.

At this point, it is important to recognize that the incoming CEO will bring additional social capital that is specific to that CEO which will benefit the firm. However, for the purposes of this study, I have restricted my focus to the influence of the social capital of the Founder-CEO on subsequent performance of the firm. Focusing on a Founder-CEO in the unique and singular event of Founder-CEO replacement provides a rich context for examining more thoroughly the institutionalization of that individual's social capital. For example, when Steve Jobs was persuaded out of his CEO position to make room for a more professional manager, he was allowed to retain a position of authority in the company because the board recognized his deep, rich ties to key personnel in the company. He possessed a wealth of internal social capital and was looked at as a spiritual leader by many of the employees. Complete alienation of Jobs from the firm could have sent shockwaves through a growing but still fragile organization and so the board and incoming CEO decided to keep Jobs inside the company. As time went on however, Jobs, feeling he was illegitimately pushed out, did not allow for an easy transfer of his social capital (especially internally) to the current top executives or show his support for their actions. Ultimately, he tried to mobilize his internal social capital in an attempt to retake his former CEO position in a coup-like fashion. Once all of this was discovered he was forcibly ostracized by the organization. Consequently, he took many valuable, high-level employees with him to start a new company. This was a notable loss for Apple and the organization did appear to suffer as a result. When Apple dismissed Jobs in such an unfriendly manner, it risked the loss of key relationships that were held by the founder, which may have led to the firm's subsequent disappointing performance. After many years of this seemingly stalled performance and near extinction, the company ultimately brought Jobs back and returned the CEO's chair to him. This example illustrates the far-reaching effects the loss of a Founder-CEO (and therefore his or her social capital) can have on an organization despite the important and valuable social capital that is brought in by the succeeding CEO.

Studying the institutionalization mechanisms that occur during a Founder-CEO transition will also provide insight into the way an organization changes its management of social relations (internal and external) as it continues to grow and develop. Indeed, Pennings and Lee (1999) have commented:

> Entrepreneurs, new ventures, and small firms differ markedly from large corporations in terms of the links they maintain. The links that bind them might vary from those that are heavily endowed with trust to those that fit the arm's length relationships. The large corporation is prone to have arm's length relationships with external actors, but…they often invest in boundary spanning systems in which personally mediated links are discernable. Small firms are more likely to develop bonds of trust and mutual adjustment with external actors such as suppliers and clients, although some conditions give rise to arm's length relationships. (p. 45)

Bringing in an outsider as CEO may signal a "new way of doing business" for some suppliers and/or clients, and therefore could lead to the loss of critical resources that these external actors provide. Additionally, an outsider CEO could also be seen as a threat to the internal fabric of an organization as many of the employees of new ventures are fiercely loyal to the founder(s). In fact, one venture capitalist I have spoken with on the subject noted that this tension often spilled over into the investors who were overseeing the transition. He commented that "as an investor you know this guy has got to be replaced in order to increase the valuation of the company so that you can secure your next round of financing, but at the same time, you often times have gone 'native' and you really want to see this guy win and take this company all the way." This loyalty to the visionary founders of companies is often strong and not easily transferred to the incoming successor CEO.

The preceding discussion illustrates a few of the important motivations for studying and understanding the process of transferring or institutionalizing personal social capital in order to increase a firm's corporate social capital. It is therefore important to be specific about what is meant by "social capital." Throughout this project I will use the definition provided by Leenders and Gabbay (1999), who define social capital as a set of resources—tangible or virtual—that accrue through the actor's social relationships and ultimately facilitate the attainment of goals. This definition is useful because it goes beyond traditional uses of the concept which often treat social capital as if it is synonymous with an actor's social network. Leander and Gabbay's definition restricts the term to apply only to those social relations that provide some benefit for the attainment of goals (which in the present study are specified at the organizational level—e.g., growth, performance and survival). It also assumes that the benefits provided by the social relations are productive and necessary for the attainment of the aforementioned goals. This definition also suggests it is important to measure organizational social capital in ways that go beyond simply aggregating individuals' personal social networks, as has been the traditional approach (e.g. Pennings & Witteloostuijn, 1998; Burt, 1992), and to differentiate between social ties that may not be equally beneficial at the individual and organizational levels.

In order to examine this particular phenomenon, I will first seek to develop the theoretical foundations of the broader concept of social capital transfer based on existing social capital literature. This discussion will occupy Chapter 2 of this dissertation and will broaden its scope beyond the Founder-CEO context. At the same time, this discussion will lay the foundation for empirically examining social capital transfer within the Founder-CEO context. Chapter 3 will discuss the relevant literatures that speak (or often don't speak) to the issue of social capital transfer in transitional events within a firm, such as executive succession, and from this discussion I develop hypotheses that will be tested empirically in the subsequent chapters. Chapter 4 will describe the methodologies to be used and discuss what advantages and disadvantages are provided as a result. Lastly, Chapters 5 and 6 will report the findings of the empirical work and summarize the lessons that should be learned from this project.

Initially, I carried out a comparative case analysis of two firms that had undergone a Founder-CEO transition. I also interviewed key personnel involved in the process. These interviews allowed me to become more intimately involved in the details and challenges surrounding succession events in a young startup. These discussions also helped inform the relevant theories and literatures that were drawn on to appropriately examine the subject of social capital transfer. I also used this data to inform the questions I used on my survey instrument. These interviews also allowed me to ask many of the executives/venture capitalists I spoke with to pretest the instrument for me. Once the survey was complete, I identified my sample through the VentureXpert database and sent out the survey to collect the data. I sent the survey to multiple respondents for each firm in an attempt to get a second perspective on what had occurred during the succession events in question. The analysis and empirical findings resulting from the survey responses are reported in this dissertation.

As a result of this work, my dissertation seeks to contribute to multiple theoretical and empirical literatures while focusing clearly on a particular phenomenon of interest. First, it promises to contribute squarely to the upper echelons literature by adding further evidence to the idea that TMTs influence organizational outcomes. It also contributes to the specific stream of research embedded in the upper echelons perspective that examines the influence of CEO ties on organizational performance and survival, providing new evidence in the understudied context of venture-backed start-ups. Second, my dissertation also contributes to the entrepreneurship literature as it provides greater insight into the Founder-CEO replacement process and the ways in which management of this process influences the company's social capital. Finally, my dissertation contributes to the social capital literature by bridging the micro-macro divide and enhancing our understanding of the processes of social capital transfer.

Chapter 2

Institutionalization or Individualization: Social Capital Transfer between Individuals and Organizations

2.1 Introduction

Frank Quattrone began his career with Morgan Stanley (MS) and quickly rose to prominence by courting young tech startups looking to IPO in Silicon Valley. This was accomplished by using the organizational ties that Morgan Stanley had in place and creating personal ties with Morgan Stanley's clients. By 1994, he was well known and well connected both within Morgan Stanley and among technology entrepreneurs and venture capitalists in Silicon Valley. He attempted to use the advantages provided by his now personal social ties in order to obtain greater control over analyst research at Morgan Stanley, but was ultimately stymied by the firm's top management. An embittered Quattrone then took this opportunity to show that he, not Morgan Stanley, now owned the client relationships by moving his operating unit to Deutsche Bank. Not only did he take his external set of relationships with him, but he also persuaded at least eight of his team members from Morgan Stanley to follow him to Deutsche Bank. Morgan Stanley was unprepared for such a grandiose departure and suffered as a result.

The preceding example demonstrates how an individual member's social capital—defined as resources embedded in a social structure that are accessed and/or mobilized in purposive actions (Lin, 2001)—can have both positive and negative implications for an organization. This fact has been documented not only by countless "real world" examples, but also by theorizing and empirical testing in scholarly research (e.g. Chung, 1996; Kratzer, Van Engelen, Leenders, 1998; Lin, 2001; Oh, Labianca, and Chung, 2006). Group or organizational social capital can also affect individual-level outcomes (e.g. Putnam, 1993, 1995; Burt, 1997, 1998; Podolny and Baron, 1997). What is not adequately understood however, is whether the individual or the organization can claim greater ownership of a given set of social capital and how (or if) that set of social capital can be transferred among individuals and the organizations of which they are a part.

At the heart of this dilemma exists the problem of defining the levels of analysis (Lin, 1999). On what level social capital resides has always been a fundamental debate among scholars. One group of scholars has argued that the primary investors in and beneficiaries of social capital are the individual actors (e.g. Lin & Bian, 1991; Burt, 1992; Portes & Sensenbrenner, 1993). These theorists agree that the aggregation of individual returns can also benefit the collective, but the focus of their analyses are on how the individual actors invest in and capture value from embedded resources.

Another group of scholars have approached the topic of social capital by focusing strictly on the group level. This work has appeared not only in the institutional perspective but also in the network perspective. These scholars (e.g. Coleman, 1990; Bourdieu, 1986; Putnam, 1993; Adler and Kwon, 2002) acknowledge the essentiality of individuals interacting but maintain their focus on the elements and processes in the production of social capital as a collective asset. This particular controversy begs for theoretical models that can simultaneously incorporate the interactions of individuals and organizations within and across levels. I attempt to address this problem through the examination of a specific social capital problem by using theoretical insights from both perspectives as well as by developing a new theory to explain how these levels can interact with and influence one another.

This dissertation seeks to provide new theoretical frameworks for conceptualizing social capital transfer and also to provide explanations for how it occurs among individuals and organizations in various environments. Specifically, I seek to address a few important questions: First, can organizations own or control social capital? Second, how would this corporate ownership differ from individual ownership/control? Finally, once ownership/control has been established, can it be transferred? My dissertation seeks to address the above questions first by examining individual versus collective social capital ownership/control. Following this discussion, I examine in more depth the concept of social capital transfer and its effects on organization (or individual) outcomes. I conclude with some thoughts and suggestions as to how this concept can be applied in empirical settings.

2.2 Literature Review

2.2.1 The Social Capital of Individuals and Organizations.

The concept of social capital has a long history. As a result, it has spawned many different streams of academic research. In order to appropriately assess which perspective is best suited for grounding this particular study, it is imperative to review the two primary branches and the strengths and weaknesses associated with each of them. I will first present the institutional view of social capital and discuss its implications for researchers and practitioners. I will then examine the networks view of social capital and its implications. Finally, I will discuss a recent development in the social capital literatures that attempts to integrate the prior contributions into a more process oriented view. To begin this overall discussion, however, it is important to trace the concept of social capital back to its earliest beginnings in the literature.

Social capital has a long intellectual history in the social sciences (see Platteau 1994; Woolcock, 1998; Adler and Kwon, 2002). Its first real introduction dates back more than eighty years to the writings of Lyda J. Hanifan, the superintendent of schools in West Virginia in the 1920s. Hanifan (1916: 130) first used the term 'social capital' while writing on the importance of community participation in enhancing school performance. The explanation she attached to this use of the phrase has helped to shape our use of the term today:

> …those tangible substances [that] count for most in the daily lives of people: namely good will, fellowship, sympathy, and social intercourse among the individuals and families who make up a social unit... If [an individual comes] into contact with his neighbor, and they with other neighbors, there will be an accumulation of social capital, which may immediately satisfy his social needs and which may bear a social potentiality sufficient to the substantial improvement of living conditions in the whole community. (p. [insert number])

After its initial introduction by Hanifan, the idea of social capital disappeared for several decades, but was reintroduced in the 1950s by a team of urban sociologists (see Sealy, Sim, and Loosely 1956). [first name] Homans (1961), an exchange theorist, and [first name] Jacobs (1961), an urban scholar, brought it back again in the 1960s, and an economist (Loury 1977) returned to the idea once more in the 1970s. None of these writers cited earlier work on the subject, but all apparently felt the need to use the same terminology to convey the vitality and significance of community ties (actor to actor or business to business). James Coleman (1987, 1988, 1990) and [first name] Bourdieu (1980, 1994) have both produced seminal works that have become the most well known foundations of social capital. Much of this early work took place in the field of sociology. Social capital continues to be an important stream of research in this field, but the topic has spilled over into other fields of academic inquiry such as economics, management, political science, and education. In fact, this concept is present in most fields of the social sciences. On one level, this impact across a diverse group of social scientists may seem to be an exciting opportunity for cross-disciplinary research; however it also creates the problem of having a ubiquitous term that means different things for different audiences. The danger is that the term becomes overused in everyday language and undervalued in scientific endeavors. In order to combat this disintegration of the concept, social scientists have sought to bring rigor and discipline to the way in which it is defined and measured. The institutional and networks views of social capital are two primary results of this endeavor.

2.2.1.1 Institutional Perspective.

The institutional view of social capital argues that the life of community networks is largely the product of the political, legal, and institutional environment. Where other perspectives largely treat social capital as an independent variable giving rise to various positive and negative outcomes, the institutional view instead puts the emphasis on social capital as a dependent variable. This view argues that the very capacity of social groups to act in their collective interest depends crucially on the quality of the formal institutions under which they reside (North 1990). The institutional perspective further asserts that emergent qualities, such as high levels of generalized trust, in turn correspond to superior rates of economic growth. It also stresses that the performance of the firm itself depends on its own internal coherence, credibility, and competence, as well as on its external accountability to the larger institutional environment in which it is situated.

Much of the research in the institutional perspective has stemmed from the field of political science and has centered on policy-related issues. Within this discipline, two major methodologies have been employed in attempting to research this concept, namely comparative case analysis and cross-sectional studies. Despite varied methodologies employed by the institutional view, the research has yielded remarkably similar results.

The very strength of the institutional view lies in its ability to address macro policy concerns. However, in this strength also lies its weakness in that it lacks a micro component. While this view has provided broad statistical evidence for the importance of social capital, the subtlety, richness, and enormous variation gleaned from the case studies of institutional environments and groups is lost. Also lost are the voices of those most directly affected by institutions—namely, the individual actors.

2.2.1.2 Networks Perspective.

In an attempt to account for these issues, a second perspective on social capital—the networks perspective—has arisen. This view stresses the importance of both vertical and horizontal associations between people, as well as the relations within and among other organizational entities such as community groups and/or firms. Building on the seminal work of Granovetter (1973), the networks perspective recognizes that intra-community (or "strong") ties are needed to give actors and organizations a sense of identity and common purpose (Astone et al, 1999). This view also stresses, however, that without inter-community (or "weak") ties that cross various social divides—e.g., those based on religion, class, ethnicity, gender, socio-economic status—strong horizontal ties can become a basis for the pursuit of narrow sectarian interests. In recent popular literature, the "strong" ties have come to be called "bonding" social capital, and "weak" ties are commonly referred to as "bridging" social capital (Gittell and Vidal, 1998). It is argued that different combinations of these dimensions are responsible for the range of outcomes that can be attributed to social capital. This more nuanced perspective regards the tension between social capital's virtues and its vices as a defining property of the construct.

The networks view of social capital, most closely associated with the work of Ronald Burt (1992, 1997, 1998, 2000, 2002), Mark Granovetter (Granovetter, 1984), Nan Lin (1999, 2001, 2002), and Brian Uzzi (1997, 1999), is characterized by two key propositions. First, social capital can be a double-edged sword (Adler and Kwon, 2002) in that it can provide a range of valuable services for actors (Burt, 1992; Fischer &

Pollock, 2004; Powell, Koput, and Smith-Doerr, 1996; Maurer and Ebers, 2006), but those same ties can place considerable non-economic claims on an individual's sense of obligation and commitment that may have negative economic consequences (Uzzi, 1997; Gargiulo and Benassi, 1999; Pollock, Porac, and Wade, 2004). Group loyalties may be so strong that they isolate members from information about employment opportunities or other important knowledge resources. Second, the sources of social capital need to be distinguished from the consequences derived from them. Imputing only desirable outcomes to social capital, or equating them with it, ignores the possibilities that these outcomes might be attained at another group's expense, that given outcomes may be sub-optimal, or that desirable outcomes attained today could come at the price of significant costs tomorrow.

These results have given rise to the logical conclusion that there must be two basic dimensions of social capital at the organizational or group level: 'strong' intra-group ties ("bonds") and 'weak' extra-group networks ("bridges"). Both are needed to avoid making tautological claims regarding the efficacy of social capital (Burt, 2005). Accordingly, the networks view argues that groups can be characterized by their endowments along these two dimensions of social capital and that different combinations of these dimensions account for the range of outcomes associated with social capital.

While the networks perspective has driven a considerable amount of productive research in the past two decades, it is now being critiqued for focusing on only one level of analysis at a time and for its static orientation. As mentioned previously, recent work (Adler and Kwon, 2002; Kim et al, 2006; Hagedoorn, 2006; Koka, Madhaven, &

Prescott, 2006) has called for a more dynamic view that spans both time and levels of analysis. The conceptual models addressed in this project seek to contribute such a view.

The view put forward in this research seeks to address two major controversies that have been noted in the literature. The first controversy is the levels of analysis problem (Lin, 1999). The basic debate among scholars has questioned on what level social capital resides. One group of scholars has argued that individual actors invest in and profit by social capital (e.g. Lin & Bian, 1991; Burt, 1992; Portes & Sensenbrenner, 1993). These theorists agree that the aggregation of individual returns can also benefit the collective, but the focus of their analyses are on how the individual actors invest in and capture value from embedded resources. Another group of scholars have approached the topic of social capital by focusing strictly on the group level. This work has appeared not only in the institutional perspective but also in the network perspective. These scholars (e.g. Coleman, 1990; Bourdieu, 1986; Putnam, 1993; Adler and Kwon, 2002) acknowledge the essentiality of individuals interacting, but maintain their focus on the elements and processes in the production of social capital as a collective asset. This particular controversy begs for theoretical models that can simultaneously incorporate the interactions of individuals and organizations within and across levels. This paper attempts to address this problem by examining a specific social capital problem using theoretical insights from both perspectives and by developing a new theory as to how these levels can interact with and influence one another.

The second major controversy debated in the literature centers around whether social capital lies in bridging ties (i.e., structural holes), bonding ties (i.e., the network closure argument), or both. Not surprisingly, many of the social scientists that have argued for an individual-level focus on social capital have also argued for the "bridging" explanation for social capital (e.g. Burt, 1992; Granovetter, 1973). Essentially, these scholars argue that social capital is a function of brokerage opportunities. Such opportunities allow an actor to control the flow of information between people and also to control the projects that bring people together who were not joined previously. Another set of scholars (e.g. Coleman, 1990; Bourdieu, 1986; Lin, 1992) have argued that network closure provides social advantages to some, which can be understood as social capital. Such network closure in a collective serves to reproduce group solidarity and to preserve a group's dominant position (Bordieu, 1986). This closure at the group level serves to also maintain and enhance trust, norms, authority, and sanctions (Coleman, 1990). Most recently, network theorists (most notably Burt [2000; 2005] and Lin [2001]) have acknowledged that both bridging and bonding relationships can be seen as a source of social capital. What the literature still lacks, however, is comprehensive and cohesive theoretical models that integrate the two dimensions of social capital. In fact, Adler and Kwon (2002) explicitly stated:

> First, organizational research would benefit if we overcame the tendency to bifurcate our social capital research into a strand focused on external, bridging social capital and a strand focused on internal, bonding social capital. External ties at a given level of analysis become internal ties at the higher levels of analysis, and, conversely, internal ties become external at the lower levels…Many of the phenomena we study as organizational researchers involve both forms of social capital simultaneously. (p. 35)

For the purposes of this paper, I will attempt to address these two controversies in a very specific subject of inquiry—namely social capital transfer. I have chosen this topic as it draws on the understanding provided by both the institutional and networks views of social capital. It also promotes a more dynamic and multi-level approach in examining the phenomenon. Lin's (2001) definition of social capital put forward earlier restricts the term to apply only to those social relations that provide some benefit for the attainment of goals.It also assumes that the benefits provided by the social relations are productive, meaning that the goals would not be attainable in its absence. This definition also suggests it is important to measure organizational social capital in ways that to go beyond simply aggregating individuals' personal social networks, which has been the traditional approach (e.g. Pennings & Witteloostuijn, 1998; Burt, 1992), and to differentiate between social ties that may not be equally beneficial at the individual and organizational levels.

2.3 Individual versus Collective Social Capital Ownership/Control

As Barnard (1938) stated, "the individual is always the basic strategic factor of organization" (p. 139). As such, individuals can exist independently of organizations, but organizations cannot exist without individuals. With this in mind while carrying out organizational research, how does one account for the individual members of the organization? This question has plagued academics for many decades. Most recently, Felin and Foss (2005) have renewed the call for organizational scholars to take "individuals and micro-foundations more seriously" (p. 442). These authors appropriately point out the weaknesses associated with many of the previous attempts by scholars to engage in multi-level research. Felin and Foss first note that many multi-level theories often amount to simply borrowing psychological theories and then applying them to the firm. Second, they note that many scholars tend to view all levels of analysis as complementary, which can lead to erroneous conclusions. Finally, they argue that there is still considerable debate about when exactly researchers can rigorously move from one level of analysis to another. To direct future endeavors, Felin and Foss propose that we need to consider "the individual as the fundamental level" (p. 448).

Coleman (1990) addressed this very issue fifteen years earlier when he argued that there are three basic components to any social theory. First, there is the relationship between the collective (or what Coleman terms a "system") and an individual actor before a particular action has been taken. Next, there is the relationship between an individual and an action he or she chooses to take. Finally, there is the relationship between the individual and the system or collective after the action has been taken. In order to see how these factors interrelate, Coleman compared social theory to a social simulation game where the two basic components are the players and the structure. The players (individuals) have within themselves some principle of action which Coleman believes is purposive in nature. The structure set in motion by these actions combines them to produce the behavior of the system. To understand macro-level phenomena, then, Coleman argues that we need to understand how individuals are influenced by a system (or collective), how they act (or react) as a result of that structure/influence, and also how those individuals' actions influence the system.

In light of the macro-micro issues raised by scholars in the field, I maintain that the social capital possessed by organizations cannot be simply an aggregate collection of the social capital of the individual members of the firm. Such a conceptualization would be problematic as it assumes that all members contribute equally and that no redundant contacts exist among members. Violations of either of these assumptions would call into question the utility of aggregation. Indeed, not all members of an organization contribute equally in their external relations or in their participation in the organization (e.g. Cohen, March and Olsen, 1972). Likewise, redundant ties among members of an organization have been extensively studied (e.g. Granovetter, 1985; Burt, 1992) and have been shown to be less efficient (Hansen, 1999). It may also be the case that some individual-level ties have little or no instrumental value for the organization itself. If individual social capital cannot be simply aggregated to the organizational level, can an organization actually possess social capital collectively that can be examined separately from the individuals that comprise it? If we take as our starting point the previously mentioned definition of social capital—resources embedded in a social structure that are accessed and/or mobilized in purposive actions—in relation to the individual actor level, we can then imagine a group level construct that also fits within this definition but imposes additional constraints. Oh, Labianca, and Chung (2006) presented one way of conceptualizing this idea. They argued that group-level social capital is a meta-construct composed of the set of resources flowing through relationship conduits (an individual's social capital) together with the configuration of the conduits themselves (see also Seibert, Kraimer, & Liden, 2001). This two-part definition recognizes the resources supplied by individuals such as information, trust, and political support that are made available to a collective or organization. This definition also acknowledges the fact that the social structure (hierarchy) of an organization's members also become an asset of the organization. The inclusion of a firm's social structure also acknowledges that some members' social capital will be more valuable to an organization's goals than others—a point which has not hitherto been considered in the aggregation approach to conceptualizing social capital at an organizational level.

Pennings and Lee (1999), in seeking to describe the relative utility of an individual's social capital within organizational boundaries, categorize members into three groups: a core group, a regular or associate group, and a temporary or marginal group. They described each group as follows: The core group consists of essential employees who are long-term employees and owners. Their fate is usually tied to that of the organization. The regular or associate group consists of rank-and-file employees who have been involved in the organization for some time and face good prospects to join the core group. However, many members who participate in that tournament will plateau, become sidetracked, or perhaps even be terminated. The temporary or marginal category includes temporarily hired workers and employees of sub-contractors. These are workers who fill jobs that do not require firm-specific skills. They have little chance of progressing into another category. (p. 47-48).

Pennings and Lee (1999) then argue that the social capital associated with the core group is more important for the organization that that of the regular group or of the marginal group. They posit that this is so because 1) the core group is more likely to use their social contacts on behalf of the organization and 2) the core group is also more likely to maintain more valuable contacts for the organization due to their more central access to the organizational structure and their holding of more powerful positions. Essentially, what Pennings and Lee have done is to conceptualize social capital at the organizational level as a mixture of individual members' social capital and organizational hierarchy. The importance of this multi-level approach has been outlined above.

This concept of hierarchy in relation to a collective's possession of social capital has been furthered explored by Lin (2001). In describing the use of social capital in hierarchical structures, Lin argued that the strength of position should have greater effects on social capital than the strength of network location (p. 165). He outlined four general parameters of hierarchy: number of levels, distribution of occupants across levels, distribution of valued resources across levels, and the sum of all occupants and resources in the structure. Under unequal conditions such as small number of levels, different sized levels, and different resources across levels, position would have a larger effect than an individual's network location. Such conditions might lead actors to undertake more expressive actions (homophilous) in order to maintain the collective social capital reinforced by the current hierarchical structure.

If we accept that social capital held at the organizational level differs from individually held social capital in that it incorporates hierarchical structure, one might still question whether hierarchy is enough to allow an organization to claim ownership over social resources conceptualized as social capital. In order to answer this, it may be useful to differentiate between the social capital accrued by an organizational member through his/her personal ties and the social capital he/she accrues through his/her position within the hierarchy of the organization.

Social capital arising from personal ties consists of those sets of resources which stem from and are maintained by the unique personality and human capital belonging to the individual actor. These relations can include familial relations, ties of friendship from prior organizations and/or events from the actor's life not immediately relevant to his/her current membership of the organization in question, and even some ties with others inside or outside the organization that have been developed by virtue of the current position the individual holds within the organization but have transcended the boundaries of organizational interactions.

The social capital arising from organizational positions consists of those sets of resources which stem from and are maintained by the occupant of a given hierarchical position. For example, in long-term alliance partnerships, organizations will often have alliance managers in each firm who will interact with one another. The unique personalities who occupy those positions may change over time, but because of the institutionalized trust between the two firms, positional access to the other firm remains the same. In such conditions, the social capital of various hierarchical positions throughout the structure can actually belong to an organization independent of the individual members who occupy the positions themselves.

Having now argued that organizations can own/control social capital and have described how it is different from how it is owned/controlled at the individual level, I will now focus on the notion of transferring social capital between individual and organizational levels. Specifically, I will explore whether or not such transfer is possible, under what conditions it might occur, and its effects on organizational or individual outcomes.

2.4 A Theoretical Approach to the Concept of Social Capital Transfer

In our approach to examine the question of whether ownership/control can be transferred once it has been established, it is necessary to build off of the theory and definitions presented in the previous sections. For convenience to the reader I have summarized the key points of this theory in Figure 2.1 below:

2.1

	Social Capital at the Individual Level	Social Capital at the Organizational Level
Description	Resources embedded in an individual's social structure that are accessed and/or mobilized in purposive actions (Lin, 2001)	Set of resources flowing through relationship conduits (an individual's social capital) and the configuration of the conduits themselves (Oh, Labianca, and Chung, 2006) .
How Social Capital is Controlled/Accessed	Personal friendships, trust, reciprocation, reputation, etc.	Organizational hierarchy, institutionalized trust and norms, compensation, etc.
How Social Capital is Most Often Manifested	Interpersonal Relationships	Inter-organizational and Individual-Organization Relationships

2.1: Individual versus Organizational Social Capital

Transfer is defined as "to cause to pass from one to another and to take over the possession or control of" according to the Merriam-Webster's dictionary (Merriam-Webster, 2007). By allowing an entity (individual or organization) to take over possession or control of an actor's social capital, the actor has by definition transferred his/her social capital. In order to understand the processes whereby a form of capital can be transferred from one level to another, it is important to review briefly how social capital can be developed at each level and what would constitute a transfer of social capital from one individual/organization to another.

2.4.1 Development and Transfer of Social Capital at the Individual Level.

As discussed previously, social capital at the individual level can be conceptualized as social resources in an individual's network (consisting of family, current and past friends, etc.) that are tied to the unique personality or individual. For most, if not all, of these relationships, trust functions as a critical element in the continuation of the relationships themselves (Lewis & Weigart, 1985). In fact, trust enables social interactions to occur on a simple and confident basis where, in the absence of trust, the insurmountable complexity posed by uncertainty would paralyze action (Simmel, 1964). Since interpersonal trust is a foundation for ongoing social interactions, it is important to recognize its role in the development of personal social capital.

Interpersonal trust has both cognitive and affective foundations (McAllister, 1995; Lewis & Wiegart, 1985). Cognitive-based trust is based on "good reason," thereby allowing people to make "leaps of faith" (Luhmann, 1979; Simmel, 1964). Affective-based trust consists of emotional bonds between people (Lewis & Wiegart, 1985) which stem from expressions of genuine care and concern for ego, beliefs about the intrinsic value of the relationship, and beliefs that these sentiments are (or will be) reciprocated (Pennings & Woiceshyn, 1987; Rempel, Holmes, and Zanna, 1985). As individuals develop one or both of these types of interpersonal trust foundations, the unique resources of the alters become accessible to the ego. Under such conditions, an individual is able to develop social capital that is attached to the actor and rather than to a particular role or position that the actor may have occupied during the initial interactions that led to the creation of interpersonal trust.

An individual's social capital, arising from her interpersonal relations, can be an important asset for a firm and may affect its performance (e.g. Bamford, Bruton, & Hinson, 2006; Bolino, Trunley, & Bloodgood, 2002; Koka & Prescott, 2002). While these social resources allow the individual to accomplish his or her organizational duties better than another individual occupying the role, if that individual were to leave the company or move to another position within the company, access to those unique social resources could be lost to the organization and therefore to the successor of the position. In order to transfer access to those important resources from the individual, an organization will need to institutionalize the actor's personal social relationships into inter-organizational or individual-organization relationships. This can be accomplished by various transfer mechanisms that will be described later. At the moment it is important to conceptualize the transfer of social capital occurring through institutionalization of interpersonal relationships into either inter-organizational or individual-organization relationships.

2.4.2 Development and Transfer of Social Capital at the Organizational Level.

Social capital at the organizational level also has trust as a foundation—albeit an institutionalized form of trust. This connection between interpersonal and inter-organizational trust is based on institutionalizing processes within a hierarchical structure. For example, in alliance relationships, when representatives from the two firms interact repeatedly over time, the initial relationship develops into deeper, more cooperative arrangements (Gulati, 1995). Though individual boundary spanners may come and go, role definitions are stable and enduring (Ring and Van de Ven, 1994). Structures and routines are developed and new occupants to the position are socialized in order to preserve the inter-organizational trust that has been created (McNeil, 1980; Zucker, 1977). In sum, trust structures are created and recreated within and between the interpersonal and inter-organizational relationships.

Individuals can also benefit from an organization's social capital. For example, within hierarchical structures, a position closer to the top of the structure has greater access to and control of valued resources not only because more valuable resources are intrinsically attached to that position, but also because of the position's greater access to positions at other (primarily lower) levels (Lin, 2001). Obtaining such social capital provides increased advantages to the individual actor beyond his/her own personal social capital as it evokes not only the resources embedded in the position itself, but also the power, wealth, and reputation of the organization (Lin, 2001). In order for an individual to transfer these valuable organizational social resources to him/herself, s/he must engage in a number of actions to move the relationship beyond the formal confines of the institutional boundaries that will be describe in more detail below. Presently, it is important just to note that an individual can transfer social resources from an organization to him/herself.

2.5 A Model of Social Capital Transfer

After exploring the ways in which social capital can be developed and transferred at both the organizational and individual levels, I now examine under what conditions and how each level of social capital can be converted into the other type. This conversion would effectively transfer the social capital from one level of analysis to another (individual to organization or vice versa). In predicting when social capital is likely able to be transferred and what processes are required for such transfers, I argue that two factors are important: interdependence and temporal embeddedness. I will now discuss each of these factors in turn.

2.5.1 Interdependence.

For the purposes of this paper I define interdependence as the extent to which an individual and an organization mutually depend on one another's social capital for positive performance. At its most basic level, the relationship between an individual and an organization is an exchange relationship. One party (an individual) offers a set of resources (social, physical, and intellectual) while the other party (the organization) provides other resources (social, physical, or intellectual) desired by the first party. The goal of such interactions and exchanges is to create value for the parties involved. As these two partners interact, the relationship can develop and expand the interdependence of the two parties (Dwyer, Schurr, and Oh, 1987). For example, as individuals and organizations make investments in one another over time, they thereby demonstrate good faith, which further develops the relationship and their relative interdependence (Anderson and Weitz, 1992; Johanson and Mattson, 1985). This interdependence can ultimately lead to affective commitment on the part of both partners (Kumar, Scheer, and Steenkamp, 1995). For the purposes of this paper I focus on the interdependence that is developed based on the social capital of each party.

For illustrative purposes, I refer again to the earlier example of Mr. Quattrone. When beginning his career, Quattrone used Morgan Stanley's reputation and network of contacts to provide him access to individuals in a relatively neglected market. The organization invested in him by providing him the necessary resources to explore this neglected market space. Quattrone capitalized on these resources and began to provide value for the firm as he was able to bring in lucrative IPO deals for the company. Over time, The social capital resources being utilized led Quattron and Morgan Stanley to make further investments in each other. This process enabled each to create value for all parties involved. This interdependence did not remain symmetrically high, however, and in the end one party was able to claim greater benefit from the social capital resources that had been developed, on which I will elaborate later. While the ultimate outcome in this case was not positive, this story does illustrate that individuals and organizations can invest in one another based on valuable social capital resources in order to achieve a state of high interdependence as defined previously. It also illustrates that over time this interdependence can become asymmetric, allowing for one party to gain the advantage over the other. This asymmetry among partners can reduce the partners' affective commitment to one another, ultimately putting their interests in conflict (Geyskens, Steenkamp, Scheer, & Kumar, 1996).

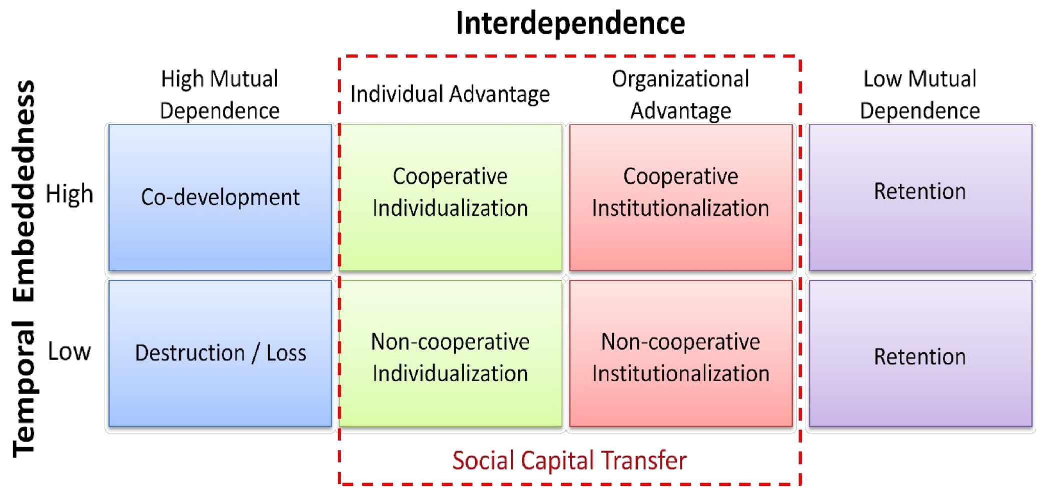
2.5.2 Temporal Embeddedness.

Accepting the idea that interactions between individuals and organizations over time can create a mutual dependence on one another's social capital resources, I introduce the concept of temporal embeddedness. Temporal embeddedness is different from interdependence as I have defined it here in that it has less to do with the degree to which two parties depend on one another (although it is assumed that this interdependence does, indeed, exist) and more about whether or not one or both parties will choose to cooperate in transferring social capital resources between the two actors. At any point, either party could terminate (or redefine/restructure) the relationship with the other party despite the potentially negative fallout that could ensue. Therefore, each partner must continually choose whether or not they will act cooperatively when developing and transferring social capital resources.

Temporal embeddedness is defined as the general sentiment towards the other party based on past interactions and the likelihood of future interactions. Prior work has demonstrated that past interactions may affect current behavior in terms of choosing whether or not to cooperate in the present (Rapoport, 1988). The basic argument is that positive past interactions will make an actor more likely to cooperate in the present with another party than if the actor had negative past interactions or no prior experience with the party (Gautschi, 2002; Gulati and Gargiulo, 1999; Swinth, 1976; Deustch, 1958). While the past informs an actor to the efforts and incentives of the other party in the present, the future allows the actor to control and sanction the actions of the other party (Buskens, 1999). These future-oriented effects have been referred to as reciprocal behavior (Blau, 1964) or conditional cooperation (Taylor, 1987). The basic argument here is that if two parties expect to interact with one another in the future (whether directly or because they are part of a larger community [e.g. industry]) they will be likely to act more cooperatively and less opportunistically (Gulati, 1995; Burt and Knez, 1995; Baker, 1990; Raub and Weessie, 1990; Axelrod, 1984; Smith; 1982). Therefore, the temporal embeddedness an actor experiences is based on both the history of prior interactions with the other party as well as the likelihood the two parties will continue to interact in the future. A long history of positive interaction combined with a sense that these interactions will continue long into the foreseeable future will produce high levels of temporal embeddedness, while little or no past interactions combined with no expectations to continue to work together in the future will produce low levels of temporal embeddedness.

The combination of temporal embeddedness and interdependence predict if and how social capital transfer will occur. Since each of these concepts contains variations (e.g. high-to-low levels of temporal embeddedness) I have created the following matrix displayed as Figure 2.2. This matrix depicts six possible outcomes of the effort to transfer social capital across levels based on variations in temporal embeddedness and interdependence.

2.2



2.2: The Role of Interdependence and Temporal Embeddedness in the Transfer of Social Capital across Levels

In Figure 2.2, we see seven types of outcomes from an attempt to transfer social capital that can be initiated either by an individual or an organization: co-development, cooperative and non-cooperative individualization, cooperative and non-cooperative institutionalization, retention, and destruction/loss. The first outcome, co-development, allows the originator to maintain access to these valuable social resources while simultaneously developing access to these resources at either a higher or a lower level of analysis through either the individualization or institutionalization transfer processes. The next four outcomes are the basic forms of social capital transfer processes: cooperative individualization, non-cooperative individualization, cooperative institutionalization, and non-cooperative institutionalization. These processes have been touched on briefly previously in this paper but will be explained in more detail below.

Another possible outcome depicted in Figure 2.2 is the destruction or loss of social capital to both the recipient and the originator which is obviously the worst outcome for both parties and does not represent transfer of any kind. Finally, the last two cells predict retention of social capital. Under conditions of low mutual dependence and either high or low levels of temporal embeddedness it is predicted that the two parties will merely walk away with the same social capital with which they began. This scenario can be classified as retention because the originator retains access and does not allow a transfer to occur. Since the individualization and institutionalization outcomes presented represent the basic processes of social capital transfer, I will first explore these two concepts in detail and will then briefly discuss the processes of co-development and destruction.

2.5.3 Individualization of Social Capital at an Organizational Level.

It is often the case that social capital associated with an organizational position will precede an individual's personal social capital. Occupying a particular position might allow for some level of transfer to occur. Katz and Kahn (1978) describe these organizational roles as the building blocks of the organizational social system and the summation of the requirements with which such systems confront their members as individuals. They further argue that a person holding any given position in an organization is linked to some other set of members by the expectations this set of members have of whomever fills that particular position. In having these expectations, this set of members effectively upholds the functional requirements of the system. An organization can be viewed as consisting of a number of such sets—one for each position in the organization. Gabarro (1987) discusses how hierarchical roles (or positions) can serve as a foundation for the formation of working (personal) relationships. He stated the following:

> Roles and role expectations are part of the context of all social interaction, but they are even more persuasive and are more explicitly defined in working [personal] relationships, particularly when they occur within or across organizational hierarchies. Most working relationships develop between people by virtue of their roles. In this respect, people begin [an] institutionalized role relationship, often before they have begun to develop an actual [personal] relationship. (p. 180)

Garbarro (1979) also argues that this development of a personal relationship beyond the required role relationship occurs as role occupants establish an "interpersonal contract" based on mutual expectations, trust, and influence. As actors interact with others through role sets within the organizational context, they come into contact with other individuals to whom they develop ties that can be called on even when the actor no longer occupies that particular role. This process of developing interpersonal relationships beyond the requirements of the defined working relationship can transfer individual loyalties away from the company toward the individual actor representing the company. It is argued that individualization has occurred in such a situation.

This individualization can occur in the context of high or low levels of temporal embeddedness. As depicted in Figure 2.2 above, when an individual and an organization enjoy a high level of temporal embeddedness, such as a long history of past positive interactions and an expectation that the interactions will continue in the future, cooperative individualization will occur. Cooperative individualization suggests that the organization is supportive of the actions taken by the individual to individualize the social capital of the organization despite the risk of loss. The opposite condition, non-cooperative individualization, occurs when a low level of temporal embeddedness is present and suggests that the organization is unsupportive of the actions taken toward individualization and is concerned about the loss of key social capital resources. In such conditions, the organization may make an effort to prevent the individual from appropriating the social capital if the action has not yet been completed. For clarification purposes, I present two examples of individualization: one cooperative and the other non-cooperative.

2.5.3.1 Cooperative Individualization.

An example of cooperative individualization can be seen in the relationship between Pixar and Steve Jobs. Pixar was started by a group of PhDs who were interested in bringing computer animation to individual consumers. These researchers were hired into LucasFilm in the late 70s. They then created a department known as Industrial Light and Magic (ILM). Over the years, ILM worked closely with Disney to implement a computer animation system to aid Disney animators in their drawing by automating the more tedious copying of the drawings and renderings. In 1984, John Lasseter, who had been employed at Disney (*Tron*, *Where the Wild Things Are*), joined the company to help them create some short films. At this point, ILM and Disney began to work together more formally. In late 1984, Lucas was experiencing some financial concerns and was looking to sell ILM as it was expensive and it seemed as though the division was decades away from being profitable. All potential deals with interested investors ultimately fell through until Steve Jobs visited and negotiated a suitable price. For almost a decade, Jobs focused more on his other company, NeXT, and left Pixar to run under the direction of [first name] Catmull, one of the original founders,. During this period, Disney and Pixar agreed to produce 3 feature-length films. Jobs remained uninvolved at first, but soon became increasingly more interested in the affairs of Pixar. In 1995, Jobs stripped the title of "President" from Catmull and positioned himself as the leader of the company. Jobs held this position for only a short time until NeXT was acquired by Apple in 1997. At this time, Jobs returned leadership to Catmull in order to quickly assume the CEO title at Apple. While Jobs was still a majority investor in Pixar, he focused his attention on reviving Apple. Pixar continued to work with Disney in producing a number of blockbuster hits and was ultimately acquired by Disney in [year]. In 2004, Apple and Disney became partners and entered into an agreement to make the digital music from Disney's movies available on Apple's iTunes. Such an arrangement might not have been possible had Jobs not been able to use the Disney relationships he had established during his involvement with Pixar. Specifically, Jobs individualized a portion of the social capital held by Pixar by displaying dynamic leadership and by establishing interpersonal relationships with key Disney leaders during his tenure as president of Pixar.

From this foregoing example it is evident that Pixar and Disney had a long standing relationship that allowed them to collaborate over the years which led to institutionalized trust between the organizations. While Jobs was initially largely uninvolved at Pixar, he later increased his involvement to the point where his past interactions with Disney helped him to forge new ties between Apple and Disney even after he had left Pixar to lead another organization.

2.5.3.2 Non-cooperative Individualization.

The story at the beginning of this article about Frank Quattrone is an excellent example of a case wherein an actor was able to individualize or transfer organizational social capital to himself. When he started at the San Francisco branch office of Morgan Stanley in 1981, most of Wall Street considered Silicon Valley a backwater. Despite the prominent sentiments from the financial community, Quattrone became obsessed with the tech industry and used his position and Morgan Stanely's network of clients and alumni to begin his own networking among the venture capitalists and entrepreneurs at industry events such as Comdex. Some of his colleagues even criticized his behavior and felt that he was losing touch with the crux of his job. While receiving a fair amount of criticism from other investment bankers, his hard work began to pay off in the late 80s and early 90s as he began to develop his own reputation among Morgan Stanley's network which allowed him to line up some of the most prominent IPOs of the time, such as Silicon Graphics and Cisco Systems. Morgan Stanley quickly promoted him in an attempt to keep him happy with the firm in order to retain this new and extremely valuable social capital. These promotions led to Quattrone assuming leadership of the Morgan Technology Group in 1991. Given this increased authority, Quattrone placed the first investment banking office ever in Silicon Valley. Quattrone continued to use his ever increasing positional resources to expand his personal network. As mentioned previously however, this appropriation of positional social capital by Quattrone meant bad news for Morgan Stanley when he exited the company in 1996, taking with him valuable clients and employees.

In 1998 he repeated the experience once again, only this time he moved from Deutsche Bank to Credit Suisse First Boston (CSFB). At CSFB, Quattrone and his team led 138 high-tech IPOs from 1998 to 2000, nearly as many as the two biggest underwriters—Goldman Sachs & Co. and Morgan Stanley—combined (Business Week, 2003). CSFB, without Quattrone, could not have achieved such access to so many high-tech deals. Likewise, if Morgan Stanley had been able to retain Mr. Quattrone, it might have ensured its position as the premier high-tech IPO underwriter.

The example of Quattrone together with several others like it illustrate how an individual can use positions embedded in an organizational hierarchy to serve as a context for facilitating social interactions which allow an actor to develop social relationships beyond the expected interactions of the company. As individuals use hierarchical positions to aid in the development or transfer of organizational social capital—including not only the resources embedded in the position itself, but also the power, wealth, and reputation of the organization (Lin, 2001)—they effectively individualize or transfer that social capital to themselves.

2.5.4 Institutionalization of Social Capital at the Individual Level.

Institutionalization is the process whereby new norms, values, and structures become incorporated within the framework of existing patterns of norms, values, and structures (Kimberly, 1979). This process is one that lends stability and predictability to social relationships and enables them to persist. It is especially visible in the context of formal organizations, where developing mechanisms to sustain planned change efforts is frequently a problem (Goodman & Bazerman, 1979).

In order to protect themselves from such shocks, organizations can engage in various tactics that help facilitate the transfer of an individual's social capital to the organization. This notion of transfer has as its core the concept of changing control over the target object. Returning to Coleman's (1990) three basic components of social theory, the second component—the individual-action relationship—is the only place where action occurs and where the "system level" exists solely as emergent properties characterizing the systems of action as a whole. In order to understand what is happening on a system or collective level, we need to understand the interdependence among actors at the individual level. According to Coleman, this interdependence among actors is brought about because actors in a system have control over a certain set of resources and they have interests in resources controlled by others. This interest in others' resources motivates efforts to acquire them for oneself, which spurrs some social interaction or relationship. This idea of control over a set of resources can be maintained by an individual or shared by a collective. Such social capital controlled (or held) by an individual can be absorbed by a collective, transferring ownership of the capital from the individual to the collective. This transfer of control can be shared by both the individual and collective simultaneously, or it can be completely institutionalized at the organizational level. For example, a new organization looking to replace its social capital laden Founder-CEO may opt to keep the founder within the organization as a liaison after replacement in order to obtain control over those resources. Alternatively, the organization could seek to institutionalize the desired relationships through contracts or any number of mechanisms that ultimately seek to cut the Founder-CEO out of the relationship completely.

Figure 2.3 below provides some examples of how an organization can obtain control over the valuable social capital resources that are possessed by an individual member. As stated previously, individuals vary in their contributions to a firm's value in many ways, including human capital, financial capital, etcetera. Understandably, their ability to bring social capital important to accomplishing the organization's goals must also vary. As such, the following model presupposes that an organization will exert effort to obtain the resources of only those select few individuals who possess social capital that is of value to the firm at large. Loss of those individuals can have serious negative outcomes for a firm, which justifies these efforts at appropriation.

The goal of an organization seeking to appropriate an individual's social capital is to obtain some amount of control over a desired resource. Prior research has argued that social capital flows to individuals through bridging and bonding relationships (Adler and Kwon, 2002) and so an organization will need to select appropriate mechanisms to retain the integrity of the relationship and to preserve the social capital at risk. The bridging of relationships is exemplified by a power structure that allows a broker to bring together parties who might not otherwise interact. In order for an organization to transfer important relationships mediated by a member, the firm needs to renegotiate the existing power structure in order to give itself more control over the individual and his or her relationships. Bonding relationships are marked by dense, embedded ties. For an organization to transfer these important relationships to itself, it needs to establish redundant ties with the individuals or organizational partners it hopes to retain. Two mechanisms of institutionalization, reorganizing power/authority structures and establishing redundant ties, seek to convert personal ties into organizational ties.

Earlier it was argued that social capital at an organizational/collective level exists through the establishment of a social structure comprised of individual members who brought important social resources that a firm could use to accomplish its objectives. The two institutionalization mechanisms being argued for here are devices that can be used to alter or enhance that social structure in such a way as to obtain more control over the particular resources it desires, and by so doing transfer the ownership or control of the individual's social capital to the organization. In order to depict how this phenomenon has occurred in the observable world, I offer two examples that illustrate the effective use of one or both of the mechanisms presented. The first example, FinSoft, characterizes cooperative institutionalization and demonstrates the use of the second mechanism—creating dependencies or redundancies—in order to transfer important relationships from the founder. The second example, WebSoft, characterizes non-cooperative institutionalization and demonstrates the practice of changing the power/authority structure mechanism in order to appropriate important social capital held by the founders. While both companies sought to use both mechanisms in the actual transition, the individual circumstances varied such that in each case, the firms found a different mechanism to be most efficacious..

2.5.4.1 Cooperative Institutionalization.

FinSoft. FinSoft was founded in 1995 to develop and promote trade order management software that would be customized to its clients. The founder's first big customer came in 1996 and he began to hire more developers and account managers from his personal network to handle the extra work. In 2000 the company took on its first round of financing from Goldman Sachs and brought in its first outside board member.

In 2002 it became clear to the COO (a personal friend of the CEO) that the Founder-CEO was beginning to check out of the day-to-day operations of the business and it was time to carry out the anticipated exit of the founder. The Founder-CEO, the COO, and other key board members and senior managers looked for the right way to execute the transition. In 2003, another round of financing from Goldman Sachs was set up to provide liquidity and to allow the Founder-CEO to cash out. In 2004, the COO and the Founder-CEO formally planned and announced the succession. By 2005, the Founder-CEO was out and the COO was in and a number of initiatives were undertaken to transfer important social capital away from the Founder-CEO to the COO (new CEO) and/or the organization.

One such transfer of valuable social resources through the creation of dependencies or redundancies occurred as the new CEO personally hand-picked an expanded set of senior managers. The new CEO had already been part of the company for years and had personal relationships with many of the employees, but select groups were fiercely loyal to the Founder-CEO, and the new CEO did not have the necessary credibility in these circles. One such group was the software developers. In order to capture the important social capital in this group and to assure that no devastating exits of key employees or cultural backlashes occurred, the new CEO promoted a prominent leader from their midst and made him the new COO. This not only appeased the developers but it also helped to transfer the loyalties of the new COO to the new CEO, as the newly promoted COO owed the new CEO a debt of gratitude.

2.5.4.2 Non-cooperative Institutionalization.

WebSoft was founded in the late nineties to develop software applications to enable internet commerce. The original developer of the software ran the company and had hired a group of developers whom he knew and trusted from his personal network of friends. The company ultimately reached a point where future growth and competitiveness depended on an infusion of external capital and resources. Accordingly, the company brought in two venture capitalist investors.

While growth was the goal in this case, it was also the problem. As the company grew, the Founder-CEO was told to hire in a number of new individuals and to put together a stronger management team. As the founder began to do this he had to extend beyond his personal contacts and bring in recent graduates as well as some displaced, experienced software engineers. The more the company grew, the more apparent it became that the founder was unable to meet the demands of his CEO post. His management was described as "pulse management" because it was unstructured and chaotic. He would come in and stir things up and then, as quickly as he came, he would leave, not to be heard from for some time. It became clear to the venture capitalist investors sitting on the board that it was time to replace the founder.

Upon approaching the founder, the VCs were met with resistance and the founder (still a significant owner in the venture) refused to give up the post. After a few weeks of easing the founder into the idea, the VCs successfully convinced him to step down and take a job as a Senior VP over development. Immediately, the board hired in a more seasoned CEO. It was essential for the founder to remain in the company as many of the developers were fiercely loyal to him to the point where they might walk out if the founder was forcibly fired. By doing this, the VCs and other board members had effectively reorganized the power structure of the company. However, two months after his demotion, the founder sought to hijack the board after a disagreement about the strategic direction of the company. The VCs then discovered that the founder was having some financial challenges and used this as an excuse to setup a liquidity round. This provided some cash for the founder to get back on track financially, but also allowed the VCs and other likeminded investors to capture majority block ownership in the company.

Soon thereafter, the CEO began to have some trouble from the development side. Many of the senior software engineers, who were still loyal to the founder, began working on projects not associated with the current direction of the company and neglected the ones requested by the CEO and other senior managers. In part, this was the problem the VCs and CEO had feared—the founder was using his personal relationship ties to re-establish authority in the company to the detriment of the organization. In retaliation, the CEO promoted one of the star software engineers, who had been hired by and was loyal to the founder, to manage the founder and the other developers. The founder quickly turned on his former friend and began to work against him as well, which led this individual to slowly reduce the founder's sphere of influence by reducing his responsibilities and ultimately removing his email access within the company. This treatment of the founder earned him the trust and respect of the other developers. Within a year of stepping down from the CEO post, the founder was let go from the company. While the VCs and new upper management had hoped to avoid many of the non-cooperative institutionalization actions that were taken, they felt it necessary in order to preserve their investment in the firm.

This last example shows how an organization (as directed by its leadership) was able to institutionalize an individual's social capital in order to retain the valuable social resources it needed to continue to perform and grow in the future. They did this initially through reorganizing the power/authority structure of the firm. As time progressed, the company also began to create some redundancies in order to completely transfer the important social capital resources before ending future interactions with the individual.

In order to aid the reader, I have included Figure 2.3 below which provides some examples of what an one can do to individualize or transfer important social capital held by the organization to him or herself. Figure 2.3 also provides examples of actions an organization can take to institutionalize an individual's social capital.

2.3

Cooperative Individualization Actions:
Article Example: Jobs, Pixar, Disney and Apple
Some Illustrative Actions:
- Develop interpersomal realtionship with the employee /client (recognize birthdays, family...etc)
- Create a sense of dynamic leadership
- Hire/promote friends/acquintances with existing loyalty

Cooperative Institutionalization Actions:
Article Example: FinSoft
Some Illustrative Actions:
- Retain individual in less powerful position
- Promote internal successors
- Long-term succesion planning
- Stock options grants to key internal members

Non-cooperative Individualization Actions:
Article Example: Frank Quattrone
Some Illustrative Actions:
- Demonstrate exceptional individual performance
- Position self as a mediator between organization and individual
- Develop interpersomal realtionship with the client representative

Non-cooperative Institutionalization Actions:
Article Example: WebSoft
Some Illustrative Actions:
- Establish formal boundary spanner positions to manage relationships
- Consolidate departments/divisions
- Formal contracts
- Equity investments
- Joint ventures and acquisitions

2.3: Examples and Illustrations of Individualization and Institutionalization

Having described and illustrated the four basic outcomes and processes of social capital transfer, I will now briefly describe co-development and destruction. It is important to keep in mind that what separates co-development and destruction from the four social capital transfer outcomes is a symmetrical and high mutual dependence versus an asymmetrical dependence with one side at an advantage over the other party. Co-development differs from destruction in that co-development occurs when the firm and the individual have a history of positive interactions as well as a foreseeable future. Under destruction, although the organization and the individual have high mutual dependence on another's social capital, they do not see the relationship continuing on, and therefore seek to extract as much as they can before leaving the relationship.

2.5.5 Co-development of Social Capital.

As mentioned before, co-development allows the originator to maintain access to valuable social resources while simultaneously developing additional access to these resources at a higher or lower level of analysis through either the individualization or institutionalization transfer processes. In other words, the social capital from one actor can be transferred in such a way that it allows the two parties going forward to derive benefit from it, independent of whether or not the two parties remain aligned. Co-development ultimately allows both parties independent access to the desired social resources. Often this outcome can become a precondition for one of the other types of transfer if the mutual dependence shifts to give either the organization or the individual an advantage as specified in Figure 2.2 above.

2.5.6 Destruction of Social Capital.

When two parties who have had a productive and mutually dependant relationship in the past reach a point where one or both want to get out of the relationship, more than just that one relationship can be at stake. For example, in the realm of human relations it can sometimes be seen as taboo for one to keep in touch with a friend’s ex-spouse. In these cases, the friend will likely see this endeavor as a betrayal. In exchange relationships, disputes and breakups among business partners can also lead to similar high emotion and high stress times. If the separation of an individual from an organization is typified by high mutual dependence and low temporal embeddedness, it is likely the case that the two parties will simultaniously try to capture the valuable social resources at stake. However, in this process, some of the firms or individuals after whom both parties are seeking may dislike the manner in which they are being pursued—especially if these efforts include some amount of slandering making the firm or individual feel as though a choice must be made between the two parties. This may lead the firm or individual to sever contact with both parties. In such circumstances, the two parties have effectively destroyed the valuable social capital in their overzealous efforts to transfer it.

2.6 Concluding Thoughts.

At its broadest level, this chapter seeks to enhance understanding of how social mechanisms influence economic organization. The concept of social capital has been explored at both the individual and organizational level in order to better understand how the two are related and the ways in which they influence the future health and survival of an organization. The models in this chapter provide not only a basis for understanding how individual social capital can be transferred from one level to another, but also provides some prescriptions regarding how to think about succession, compensation, and a wide range of corporate tools to help secure important resource relationships. Most importantly, this research promises to provide new insights into multi-level theorizing that can aid future research in proposing more dynamic and processual models.

Chapter 3

FROM FOUNDERS TO FIRM: EXAMINING THE INSTITUTIONALIZATION OF FOUNDER-CEO SOCIAL CAPITAL IN VENTURE-BACKED FIRMS

3.1 Introduction

Scholars have argued that the transition from a Founder-CEO to an outsider is potentially the most critical succession event in the history of the firm (Hofer and Charan, 1982; Haveman and Khaire, 2004). This is, in part, the case because the identities of the founders are more tightly linked to the organization's identity than are the identities of later-stage managers (Dobrev and Barnett, 2005). Founders also often control a sizeable portion of the venture's assets, so ownership and control are less separated in firms managed by founders than those run by non-founders (Berle and Means, 1932). Another reason why this first succession event is so critical is that a majority of the time the successor CEO is an outsider brought in to "professionalize" the organization (Dalton and Kesner, 1984; Wasserman, 2001), which often leads to a shift in the strategic organization of the firm (Wiersema, 1992).

While most scholars agree that this initial succession is extremely important in the life of the organization, these scholars have disagreed on how this event affects future organizational performance and survival. For example, one stream from the literature on executive succession has argued that such an event can improve performance (Guest, 1962; Virany, Tushman, and Romanelli, 1992) and increase survival chances (Pfeffer and Salancik, 1978; Singh, House, and Tucker, 1986) while a sister stream of research argues that the succession of a founder negatively affects not only a firm's future performance (Baron, Burton & Hannan, 1999; Fischer & Pollock, 2004) but also its chances for survival (Carroll, 1984; Fischer & Pollock, 2004).

The basic line of reasoning for this first perspective is that rapidly growing firms soon outgrow the founder's managerial capabilities and so a professional CEO must be brought in to manage the operations (Clifford and Cavenaugh, 1985; Hambrick and Crozier, 1985; McCarthy, Kreuger, and Schoenecker, 1990). This succession is seen as an adaptive process that is necessary for a successful organization (Dalton & Kesner, 1985) as it helps to reduce conflict and provide a conduit for external information, thereby enabling the organization to become better attuned to environmental demands (Helmich, 1974; Pfeffer and Salancik, 1977; Virany, Tushman, and Romanelli, 1992). One study within this stream even found that the effect of top management successions may be more apparent and positive on younger ventures (Greiner and Bhambri, 1989).

While this first stream of empirical research is convincing, another stream supports an alternative hypothesis—namely that replacing the founder with a "professional" CEO may be detrimental to the firm (e.g., Baron, Burton & Hannan, 1999; Certo, Covin, Daily & Dalton, 2001; Fischer & Pollock, 2004). As Hofer and Charan (1982) explained, "After the starting difficulties have been overcome, the most likely causes of business failure are the problems encountered in the transition from a one-person, entrepreneurial style of management to a functionally organized, professional management team" (p. 2). Furthermore, Carroll (1984) found that the departure of a founder had a disproportionately negative influence on the likelihood of organizational survival. Scholars from this perspective hold that such managerial succession leads to lower organizational performance and employee insecurity due to the uncertainty surrounding the change (Grusky, 1963, 1964). The loss of the founder to the organization has been shown to also signal the future demise of the organization (Haveman, 1993).

It is clear from the literature that the succession of a Founder-CEO saliently affects the new venture's ability to continue to grow and survive, but what is still unclear is just how the organization is affected. This chapter seeks to make an initial attempt at addressing the question of how the organization is likely to be affected and in the process to reconcile the inconsistent findings concerning founder succession and organizational performance and survival. In order to accomplish this reconciliation, I adopt an open system's perspective and will use a systematic contingency approach (Lawrence and Lorsch, 1967; Scott, 1987). Following the previous contributions of other scholars, I maintain that uncertainties, interdependencies, and contingencies in the organizational environment can influence not only the functioning of the organization but also the allocation of power and control within the organization (Pfeffer and Salancik, 1978). Examined in this manner, top management succession is no longer an isolated event but a dynamic and complex organizational decision process that can be subject to the influences not only of the external environment but also of the internal organizational characteristics (Lin and Li, 2004).

This chapter is organized as follows: First, I will review relevant portions of the executive succession literature and discuss the relationships those authors have found between succession, performance, and survival. I will also discuss the assertions these authors have made concerning the role of social capital in a new venture setting. Next, I will discuss how the succession of a founder may differ markedly from the succession of later-stage managers. Finally, I will draw from existing literature as well as the models discussed in Chapter 2 to present a number of testable hypotheses that will be empirically examined in the later chapters of this dissertation. Throughout this discourse, I will differentiate those hypotheses that examine the affect of key constructs on performance variables more generally (beyond founder transition events), and those hypotheses that are bounded specifically by the occurrence of a founder replacement event. All of this will be done to better understand the importance of a founder's social ties to a new venture's survival, and the extent to which Founder-CEO succession puts these valuable social resources at risk.

3.2 Theoretical Foundations: A Selected Review of the Executive Succession and New Ventures Literatures

Executive succession has been the subject of theoretical and empirical investigations for over three decades and has yielded many important insights for practitioners and academics alike. While a substantial amount of progress has been made, there are even more substantial gaps to be filled and overcome. Kesner and Sebora (1994) in their comprehensive review of the literature on this issue stated that "…there is little that we know conclusively, much that we do not know, and even more that we have not yet studied" (p. 327). Acknowledging that much has been contributed in the past decade since that review was written, I believe there is still much to be added to this growing area of research. In order to appropriately position the current piece, I wish to first provide a brief overview of some notable studies that have shaped the subject of executive succession to this point, and then to more narrowly focus on those works that are most directly relevant to the present research inquiry.

Scholars examining the subject of executive succession have taken three basic approaches to understanding the phenomenon. First, succession has been seen as the dependent variable where the goal was to identify the important antecedent conditions / predictors that were responsible for initiating the succession event. Next, some scholars have chosen to look in-depth at the event itself to understand more about the process of the succession event as it was carried out. Finally, a large number of scholars have sought to discover the short- and long-term consequences of the succession event for the organization. Since this dissertation focuses largely on the processes and outcomes and less on the antecedents, I will only review selected research from the latter two of these three perspectives. To begin however, it is important to examine the role social capital plays in a new-venture context as this factor can intimately affect both the process and the outcomes of a succession event in an early-stage firm.

3.2.1 The Role of Social Capital in a New-Venture Context

New ventures have a greater propensity to fail than do later-stage firms because they are not as well established within the broader organizational field and are less likely to have developed efficient, standardized routines (Stinchcombe, 1965). Thus, the relationships of the organizations' individual members are frequently used to carry out the firm's work and are critical to helping establish the firm and its routines. The absence of such relationships increases the firm's "liability of newness" (Freeman, Carroll, and

Hannan, 1983; Li and Guisinger, 1991), making it more vulnerable to failure. It is not unreasonable, then, to argue that a new venture's social capital could directly affect the firm's survival (Fischer & Pollock, 2004; Neergaard and Madsen, 2004).

The social capital of a new venture includes relationships both inside and outside the firm (Bolino, Turnley, and Bloodgood, 2002; Koka and Prescott, 2002). These relationships are brought into the firm by the organizational members. In some cases the relationships in question have been developed prior to joining the firm while in other cases they were initiated during the founding and growth of the company (Hansen, 1995). Regardless of how they are brought into the firm, the venture can extract considerable value from these relationships at a very formative time in its history. Social capital at the organizational level, as was noted in Chapter 2, differs from the individual level in that it includes a social structure that makes certain individuals' relationships more or less relevant, and therefore more or less accessible and valuable. As a result, it is important to understand the firm's social structure to properly examine which actors contribute more or less to an organization's overall social capital. It has been argued that a founder's relationships are extremely important for the survival of new ventures, as they contribute a great deal of the firm's initial social capital (Bamford, Bruton, and Hinson, 2006). By examining the succession of a founder in an early-stage context one can potentially track what actions a firm took pre- and post-succession in an effort to secure the most critical relationships. Examining such events necessitates looking at both the event itself and its consequences.

3.2.2 The Executive Succession Event

Understanding the factors that lead to CEO turnover is important in understanding the event itself. As we understand the antecedents of the event better, we can more fully examine why and how the event unfolds. In order to gain this understanding, however, scholars must use a variety of different methodologies in order to capture the processural nature of the phenomenon. As a result, this particular stream of inquiry has not been as well studied as the other two. Those few scholars who have endeavored to study the process of CEO succession have contributed greatly and provided a strong foundation on which future researchers can build.

One topic that has received attention within this area is the effect of CEO characteristics on the succession—in particular, whether the successor CEO is an insider or an outsider. A successor CEO's 'outsider' or 'insider' status matters to many stakeholders of the organization, as outsiders are often seen as less committed to the status quo (Hambrick and Mason, 1984) and are therefore generally sought after in times of poor performance by the firm. What constitutes an outsider has varied across the studies. For example, scholars have treated a successor as an outsider if he or she had less than two years of service with the company prior to becoming CEO (Cannella and Lubatkin, 1993), were not in the organization during predecessor's tenure (Dalton and Kesner, 1985), had fewer than five years of organizational tenure (Datta and Guthrie, 1994), or were designated as such (Friendman and Singh, 1989). Whether or not a successor came from the outside has been used to predict the infusion of new knowledge and competencies (Boeker, 1997) and also to predict improvements in firm performance

(Bantel and Jackson, 1989; O'Reilly and Flatt, 1989; Finkelstein and Hambrick, 1990). Despite the evidence provided by these studies, however, some scholars claim the meaningfulness of the insider/outsider distinction is still somewhat unclear (Zajac and Westphal, 1996).

Finkelstein and Hambrick (1996) have argued that viewing CEO successions in binary terms can be a very limiting approach since there are degrees of "insiderness" and "outsiderness." They also conjecture that the biggest breakthroughs in the study of insider versus outsider succession will come from this conception of outsiderness (p. 183). Since a large majority of successors in early-stage contexts come from the "outside" it would seem that this entire body of work would have little if any value in helping to understand the Founder-CEO succession event itself. However, in seeking to apply Finkelstein and Hambrick's (1996) concept of outsiderness, it may be the case that an outside successor in a venture-backed organization that comes from within the firm's industry will be less of an outsider than a new CEO who comes from an entirely different industry. This degree of outsiderness can then be a very useful and powerful concept in understanding the succession process in both early and late stage settings. It can also be helpful in understanding how this process affects the long-term performance or survival of the firm, which is the final area to be examined.

3.2.3 Consequences of Executive Succession

As suggested earlier, prior research has shown that succession can have a positive effect on performance (Helmich, 1974; Davidson, Worell, and Dutia, 1993), a negative effect on performance (Grusky, 1963; Carroll, 1984; Beatty and Zajac, 1987; Haveman, 1993) or appear to have no effect at all (Gamson and Scotch, 1964; Brown, 1982; Boeker, 1992). These inconsistencies in the empirical record have been attributed mainly to methodological differences and problems (Davidson, Worell, and Dutia, 1993). More recently, scholars have called for researchers to account for prior performance, the conditions surrounding the succession, and the choice of the eventual successor when seeking to examine the causal link between succession and performance outcomes (Finkelstein and Hambrick, 1996: p. 210). These scholars also advise researchers to use better ways of measuring performance.

Prior research has measured performance in a number of different ways. Beatty and Zajac (1987) use the stock price 300 days prior to and after the succession event, while Friedman and Singh (1989) use the stock price only two days before and after the transition. Similarly, firm survival has been measured as organizational death (Carroll, 1984) or as bankruptcy (Davidson, Worell, and Dutia, 1993). In an attempt to reconcile these inconsistencies, Pitcher, Chreim, and Kisfalvi (2000) used the field study methodology to overcome some of the measurement issues that have been discussed in the literature. They gathered field data from a global financial services firm over a 30 year period (1960–1990) using board and group membership, 50 semi-structured interviews, and archival records. From this intensive research they found that tracking both ROE and EPS for at least three to five years after the event is an adequate predictor of post-succession performance and failure.

Another consequence of CEO succession that has been researched is turnover in the firm's other employees. This research has been mostly concerned with turnover among the top management teams of an organization, and has been shown to have mixed outcomes in terms of a firm's financial performance (Boeker, 1992; Virany, Tushman, and Romanelli, 1992; Kesner and Dalton, 1994; Keck and Tushman, 1993; Zajac and Westphal, 1996). Turnover can be of great concern to an organization not only in terms of its financial impact, but also because of its cultural consequences for the organization. This problem is more profound in a startup environment wherein the organization and its culture are much more fragile than they might be in the later stages of the firm's development. Neither the performance impact nor turnover issues have been studied sufficiently in the context of venture-backed organizations, which can vary greatly from the large public firm context. This, along with the aforementioned opportunities, provides a number of possible ways to contribute to the burgeoning literature on executive succession and its affect on performance. I will therefore quickly revisit and elaborate on the important theoretical gaps and opportunities that this particular study seeks to address and will then present a number of testable hypotheses that, when tested, should provide empirical evidence for the questions being examined.

3.2.4 Theoretical Gaps and Research Opportunities

As this paper seeks to make contributions on multiple fronts in this field, it is important to explicitly outline a number of the relevant theoretical gaps and research opportunities that will be targeted. The most fundamental contribution will be the evidence provided of the contextual influence on executive succession. This line of reasoning follows an open system's perspective and argues that the current theoretical models and empirical evidence on executive succession may or may not be appropriate in an early stage context. For this reason, I will first discuss some of the differences between early and later stage settings then I will move on to discuss the gaps and opportunities for each of the three previously described branches of the succession literature. Many of the gaps and opportunities—and the subsequent hypotheses—that will be discussed in this project stem from the premise that key differences exist between the characteristics of the two contexts.

3.2.4.1 Succession in Later-stage versus Early-stage Settings

There are a number of important differences between later-stage and early-stage settings that give reason to question whether it is prudent to apply succession models developed in the later-stage settings to early-stage companies. At the heart of these differences is the theoretical paradigm provided by Berle and Means (1932) regarding the separation of ownership and control. Berle and Means argue that owners and managers are two distinct groups between whom there is a separation of ownership and control. In the case of such a separation, the managers (agents with control) could use the owner's assets (i.e., the company) for their own purposes rather than in ways that lead to wealth maximization for the owners (Jensen and Meckling, 1976). Such a problem is not as prominent in an early-stage company as the Founder-CEO, who has control over the firm's resources, is also a majority owner. Even as the company continues to grow, the founder will usually continue to own a large portion of the company (Wasserman, 2001). This critical difference between the two settings may call into question some of the results associated with executive succession in large firms because there is little separation (if any) between ownership and control in an early-stage environment.

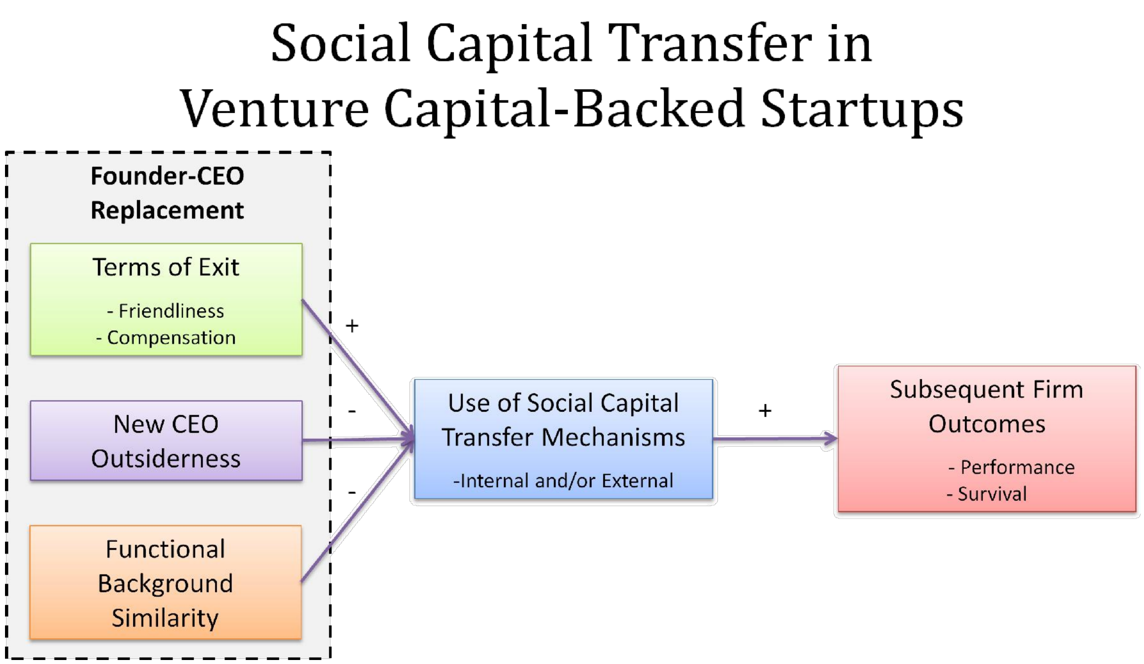
Wasserman (2003) argues that there are two other key differences between succession in early- and later- stage settings. First, Founder-CEOs wield a large amount of influence and loyalty inside their organizations not only due to their ownership, but also because the organizational identity is closely tied to that of the founder (Dobrev and Barnett, 2005). The second difference is that the successor CEO in venture-backed firms is almost always an outsider (Lauterback, Vu, and Weisberg, 1999). This difference nullifies a key variable that has been both an important predictor and a control variable in much of the succession studies to date.

As a result of these differences, there is a great need to conduct more research on succession within the early-stage context. More specifically, it is important to look at the process of, the conditions surrounding, and the outcomes of the first change in leadership from Founder-CEO to outside successor. The current project is inspired by such needs and seeks to contribute to the field on these multiple fronts. First, seeking to adhere to the recommendations provided by Finkelstein and Hambrick (1996), in my examination of the succession of Founder-CEOs and performance outcomes, I will bring into consideration the assumptions about the venture's prior performance, the conditions surrounding the succession, and the choice of the eventual successor. Second, I intend to extend current models of executive succession by examining the succession-performance link in the presence moderating mechanisms (or contingency factors), which may be partially responsible for the mixed results that we find in the literature. Finally, I expect to contribute to existing social capital literature by demonstrating how the loss or retention of a founder's individual social capital can be a determining factor in the performance outcomes for the firm. In seeking to accomplish the purposes of this project, I will briefly introduce a theoretical model of social capital transfer in a new venture context and then present hypotheses as they relate to the three branches of the executive succession literature.

3.3 Social Capital Transfer in Venture Capital-Backed Startups

Figure 3.1 presents a model describing the basic relationships among the key constructs involved in Founder-CEO succession.

3.1

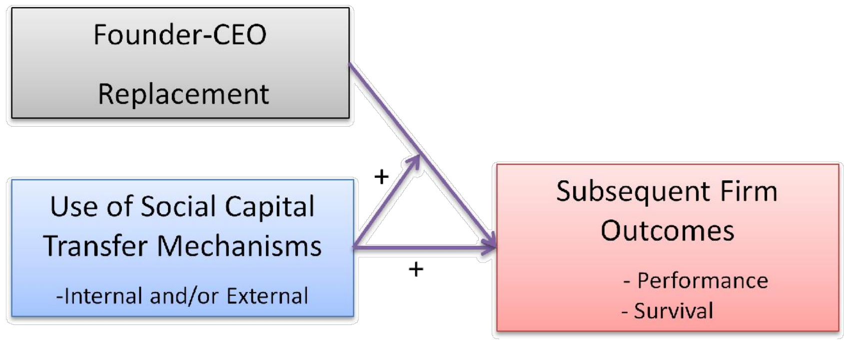


3.1: A Model Depicting the Factors Affecting and Affected by the Use of Social Capital Transfer Mechanisms in Venture Capital-Backed Startups.

The model presented in Figure 3.1 describes critical relationships between key constructs involved in the Founder-CEO succession event. The foundational relationship is between the use of social capital transfer mechanisms and the subsequent firm outcomes (this is hypothesized to be relevant beyond founder-CEO transition events and will be tested accordingly). Whether or not these mechanisms are put into use will depend on three driving factors: the outsiderness of the new CEO, the functional similarity, and the conditions that surround the succession event or terms of exit (these factors occur only when a founder-CEO transition is taking place). I will examine each of these relationships in more depth below in the context of the three sections discussed above (3.2.1, 3.2.2 & 3.2.3). Following the order above, I will first look at the research opportunities surrounding the role of social capital in new venture settings. Next, in a similar fashion, I will examine the context of the Founder-CEO succession while identifying some gaps in the succession event literature. After examining the CEO outsiderness construct and the functional similarity concept, I will present hypotheses which will address the aforementioned gaps in the succession event literature. Finally, I will look at the moderating effect of social capital transfer mechanisms as a probable contributing factor to some current holes in the work on the consequences of CEO succession. The relationship between social capital transfer and subsequent firm outcomes is captured in Figure 3.2 below:

3.2

Use of Social Capital Transfer Mechanisms as a Moderating Influence in the Succession-Performance Link



3.2: Moderating Influence of Social Capital Transfer on Founder-CEO Replacement and Subsequent Firm Outcomes.

3.3.1 The Role of Social Capital in a New-Venture Context.

As previously mentioned, a founder's relationships are extremely important for the performance and survival of new ventures as they contribute a great deal to the firm's overall social capital (Bamford, et al., 2006). These valuable relationships are found both within and outside of the firm's boundaries (Bolino, et al., 2002; Koka and Prescott, 2002). These relationships can occur in the form of bridging or bonding ties, both of which constitute an individual's social capital (Burt, 2000, 2005; Lin, 2001). The actions and underlying mechanisms an organization uses to transfer the founder's social capital will vary, but in general they are drawn from the theoretical logic in the models proposed in Chapter 2. For convenience, I have included the actions and mechanisms in Figure 3.3 below:

3.3

Social Capital Transfer: Internal and External Mechanisms for Appropriating Individual-Level Social Capital (ISC)

	External (Bridging)	Internal (Bonding)
Individual	– Firm obtains control over ISC by restructuring the power/authority structure on individual level – Internal Example: Retain individual in less powerful position – External Example: Retain individual in less powerful position	– Firm obtains control over ISC by establishing redundant ties on the individual level. – Internal Example: Promoting internal successor with ties to other members, long-term succession planning – External Example: Promoting internal successor with ties to the partnering organization, long-term succession planning
Organizational	– Firm obtains control over ISC by restructuring the power/authority structure on organizational level – Internal Example(s): Creating Internal Boundary Spanning Position, Consolidating Departments/Divisions, Formal Committees... – External Example(s): Establishing Formal Boundary Spanner Positions to Manage Relationships, Creating Select Partner Groups...etc	– Firm obtains control over ISC by establishing redundant ties on the organizational level. – Internal Example(s): Stock options grants to key internal members, promotions, increased responsibilities...etc – External Example(s): Formal Contracts, Equity Investments, Joint Ventures, Acquisitions...etc
	Operating Mechanism: Change current power/authority structure	Operating Mechanism: Increase dependence or redundancy

3.3: Model Depicting How and What an Organization Might Do to Appropriate a Founder's Social Capital

It is arguably safe to assume that a founder possesses both bridging and bonding forms of social capital simultaneously. This means that for an organization to appropriately and effectively transfer the critical social resources embedded in a founder's personal network, it must use a variety of mechanisms. This can be done either at the individual or the organizational level. At the individual level, the goal of the organization is to carry out the transfer either by changing the power/authority structure in such a way as to obtain possession of those critical social resources (through the founder or some other person) or by creating dependencies or redundancies using other key individuals (i.e. CEO successor, TMT member…etc). At the organizational level, the goal of the organization is to institutionalize the founder's personal social capital through the same two mechanisms mentioned at the individual level. This can be done through the creation of formal positions to manage things such as key relationships, equity investments, stock option grants, or department consolidation, depending on whether the desired social capital lies within or outside the firm.

Ultimately, the goal of an organization seeking to appropriate a Founder-CEO's social capital is to obtain some amount of control over the resources of interest (Coleman, 1990). Social capital flows to individuals through these bridging and/or bonding relationships (Adler and Kwon, 2002), and so an organization will need to select appropriate mechanisms to maintain the integrity of the relationship and to preserve the social capital at risk. Bridging relationships are exemplified in a power structure that allows a broker to bring together parties who might not otherwise interact. In order for an organization to transfer important relationships mediated by its founder, the firm needs to renegotiate the existing power structure in order to give itself more control over the individual and his or her relationships. In seeking to accomplish this transfer on an individual level, a firm may retain the founder in a non-CEO role, thereby retaining access to his or her mediated relationships by placing him or her in a position of lower formal authority. In seeking to transfer the founder's social capital at an organizational level, the firm might engage in actions such as consolidating departments or establishing a formal boundary role spanner position in an attempt to institutionalize the personal social relations of the founder. Whether the actions of the firm concentrate on the individual level, the organizational level, or both, renegotiating the power/authority structure of the firm can transfer valuable social resources from the founder to the firm.

Prior research has examined the institutionalization of actor-mediated personal social capital to the firm level. For example, Zaheer, McEvily, and Venkatraman (1998) examined the effects of both interpersonal and inter-organizational trust on exchange relationships. They demonstrated that interpersonal and inter-organizational trust are shown to be highly correlated in that they can influence each other either positively or negatively. As the firms interact repeatedly over time, the initial relationship develops into a deeper, more cooperative arrangement (Gulati, 1995). Though individual boundary spanners may come and go, role definitions are stable and enduring (Ring and Van de Ven, 1994). Institutionalizing processes codify informal commitments made by individual boundary spanners, and these commitments evolve into established organizational structures and routines over time (Zucker, 1977). Therefore, as new individual boundary spanners enter the inter-firm exchange relationship, they are socialized according to the established norms that define that relationship (Macneil, 1980). Norms from the inter-organizational relationship are then internalized, recreated, and enhanced in a new way by the boundary spanners during the process of the exchange (Zaheer et al. 1998). In sum, trust structures are created and recreated within and between the interpersonal and inter-organizational levels.

The use of boundary spanner roles was discussed in Chapter 2 as one set of actions a firm can take to transfer a founder's social capital. Another set proposed was the use of contracts and equity investments. Trust in business relationships can initially develop on a calculative basis (Shapiro, Sheppard, and Cheraskin, 1992), as parties try to determine the nature of their interdependence. Prior experience is likely to minimize uncertainty (and increase predictability), thus affecting the evolution of trust between organizations. Lacking prior experience with a particular partner however, the next logical step is to rely on the reputation of that firm, which is a direct consequence of prior relational behavior (Granovetter, 1985). However, when the trust between organizations is based on the social relations and reputation of the founder, such issues of uncertainty are minimized. When there is trust among the founder and other business leaders of the partnering organizations, the replacement of the founder may put these important social capital resources at risk. A company may then seek to institutionalize access to these resources through contracts or equity investments. Equity investments in a partnering organization by definition involve common ownership and are typically organized as joint ventures. In the market-hierarchy continuum of organizational forms, equity joint ventures most closely replicate the characteristics normally associated with hierarchies as they entail the creation of a separate administrative structure with formal coordination and control mechanisms. This sharing of resources and the separate administrative structure can formalize the relationships between the two firms, thus securing the desired resources independent of any individual member's personal social connection.

Contractual agreements, however, do not necessitate shared ownership or a dedicated administrative structure. They can be simple arrangements that specify or, rather, institutionalize the type and duration of the relationship that the two firms will have. Hence, equity arrangements are seen as governance forms fundamentally different from non-equity contracts, which are more akin to arm's length market exchanges (Contractor and Lorange, 1988). Research concerning the choice between equity investments and non-equity contracts has traditionally focused on the level of control typical of different governance forms (Das and Teng, 1998). Part of this literature assumes that equity investments provide more control over partner behavior than contracts do, but that both tactics still provide a means for a company to formalize or institutionalize the trust between the two entities.

Bonding relationships are marked by dense, embedded ties (Adler & Kwon, 2002). For an organization to transfer these important relationships to itself, it needs to establish redundant ties with the individuals or organizational partners it hopes to retain, or make these individuals more dependent on the firm. At an individual level, the transfer tactics may include a long succession process (allowing for the outsider to really integrate into the firm before taking over), or promoting internal candidates. At the organizational level, the firm can provide stock options for critical internal employees, make equity investments in important external partners, or draw up formal contracts. The tactics used by a firm to either create dependency or establish redundant contacts are aimed at gaining access to the founder's close network relations so as to obtain control over them.

Internal social capital is often characterized by strong cohesive relationships (bonding relationships). It has been argued that a founder's identity is closely linked to the organization's identity (Astone et al, 1999; Dobrev and Barnett, 2005). Many of the early employees have shared experiences with the founder through the early growth of the firm and believe in the founder's vision for the organization. As a result, these employees are extremely loyal to the founder. These strong personal loyalties can make it somewhat difficult for an organization to transfer the valuable resources that are embedded in these relationships. If a firm uses transfer mechanisms targeted at an individual level, it might be more likely to capture many of the social capital resources as it is seeking to maintain a personal connection with those individuals either through the founder or through some other trusted individual. I observed an example of this approach at a large software company. The successor-CEO stated that one of his biggest concerns in taking over for the founder was how to maintain the culture the founder had established. He knew that many of the employees were loyal to the founder and he did not want to disrupt the culture founder had created. In order to overcome this problem, the successor CEO worked with the founder before [his/her?] departure to execute a smooth and gradual transition. The founder and the successor CEO together chose a new senior management team and the successor CEO began running meetings even while the founder was still present. The transition itself occurred over a period of one year and allowed for the company to see the successor CEO alongside the founder in an equal leadership role. The successor CEO actively worked to connect with the employees and key leaders in the organization on a very personal level. This examples demonstrates how an organizational representative can seek to institutionalize valuable individual social capital of a departing organization member.

It is assumed that a company seeking to transfer a Founder-CEO’s social capital will engage in actions that specifically target either the individual or organizational level for the relevant types (bridging and bonding) of social capital desired. The express purpose for undertaking these actions is to secure control and or access to the important social capital in order to institutionalize it. As a result of carrying out these actions, the firm expects to improve its future performance and likelihood of survival. It is also important to note that at this point I am not differentiating between internal and external social capital as both can be argued to equally affect a new venture's survival and performance. This leads to the following hypotheses:

H1a: Taking greater action to institutionalize the Founder-CEO's social capital will be positively associated with firm performance.

H1b: Taking greater action to institutionalize the Founder-CEO's social capital will be positively associated with firm survival.

3.3.2 The Founder-CEO Succession Event

3.3.2.1 Terms of Exit

One of the important aspects of the succession event is the conditions surrounding the Founder-CEO succession or, as labeled more concisely in Figure 3-1, the terms of exit. This construct is shown to influence the firm's ability to take actions to institutionalize a Founder-CEO's important social capital. Past research in the executive succession literature has distinguished between forced and voluntary exits of CEOs (Fredrickson, Hambrick, and Baumrin, 1988). When the CEO is dismissed involuntarily it can be a politically contentious process (Vancil, 1987). The existing executive succession literature has generally pointed to poor performance on the part of either the firm or the CEO as the primary impetus for a CEO's forced exit (Finkelstein and Hambrick, 1996) while also acknowledging complex mediating factors, such as the power of the CEO relative to the board of directors (Boeker, 1992; Myatt, 1995; Ocasio, 1994). This distinction between forced versus voluntary exit is an important factor in determining whether or not an organization is able to transfer valuable social capital resources from a founder who has been ejected from his or her own company.

Forced turnover is generally viewed as signaling a much greater magnitude of change in an organization's operations, strategy, and power structure than a voluntary one (Helfat and Bailey, 2005). As mentioned above, having the successor CEO come from outside of the company (and/or industry) can also signal a strong break from the past, further crippling the organization's ability to transfer and make use of important social capital resources in a founder's network. From prior research, it would appear that a majority of the Founder-CEO replacements in new ventures are forced to some degree (e.g. Wasserman, 2003; Sapienza and Gupta, 1994) which can potentially affect the ability of the leadership of the firm to successfully capture important social capital held by the Founder-CEO.

In seeking to adequately capture the terms of exit, it will be essential to look beyond whether the founder voluntarily acceded to the transition, and instead look at whether it was done in a friendly or an unfriendly manner. From my study of the executive succession literature, it appears that the majority, if not all, of the research tends to treat these two dimensions as interchangeable (forced exit = unfriendly and voluntary = friendly). While this may be an appropriate assumption given a large firm context (although I am not entirely convinced of this either) it may be quite erroneous in a new venture context. It may be the case that although a founder does not choose (or want) to step down from being the CEO, he or she does so under friendly terms and is able and willing to help institutionalize key personal relationships.

A large number of studies examining the link between poor performance on the part of the firm or CEO and forced turnover have grounded their arguments within the realm of agency theory. This perspective argues that executives are responsible for organizational performance and should be dismissed when performance becomes poor (Walsh & Ellwood, 1991; Weisbach, 1988). They also propose that executive dismissal under poor performance will increase shareholder wealth (Denis and Denis, 1995; Worrell, Davidson, and Glascock, 1993). Much of this stems from the assumption that owners of the firm typically do not actually manage the company (Berle and Means, 1932), and therefore conflicts and a divergence of objectives arise (Fama and Jensen, 1983). As a result, friction will occur since each party will seek to serve his/her own self-interests (Eisenhardt, 1989). While many of these assumptions may be appropriate in a later-stage setting, they do not necessarily represent the characteristics in an early-stage environment.

Despite the unique differences between the early and later-stage settings (the most fundamental of which is the fact that managers tend to be majority owners), some scholars have attempted to invoke agency theory in entrepreneurial environments (Micheal, 1996; Norton, 1995; Glosten and Mueller, 1990). More recently, however, Cable and Shane (1997) criticize the underlying rationale used in prior investigations that invoke an agency theory perspective. They point out that the relationship between an entrepreneur and a venture capitalist is not always a hierarchical one as is assumed by agency theory. Furthermore, agency theory tends to ignore the important social relationship that is often present between a venture capitalist and an entrepreneur. As a result, Cable and Shane argue for a broader examination of the concept of agency when studying an early-stage setting. They go on to suggest the Prisoner's Dilemma framework approach, noting that "the agency perspective is actually a subset of the broader explanation" (1997, p. 146). In a similar vein, Nelson (2003) argued that a founder in an early-stage setting can have an "anti-agency cost" as a result of their immense psychological commitment. It would seem then that an agency perspective may not be adequate when examining the conditions surrounding the Founder-CEO succession event.

Walsh and Seward (1990) rightly point out that "the problem of agency initially was thought to disappear when a manager was made an owner. They note that "a management ownership stake was thought to align the potentially divergent interests of outside shareholders and management" (p. 434). While not downplaying the value of interest alignment, Walsh and Seward argue that the principal-agent problem can go beyond management opportunism. Sapienza and Gupta (1994) agree with Walsh and Seward (1990), but go further to argue that good faith disagreements may also create tension and friction between the VC and the entrepreneur. Specifically, they assert,

> [A]s long as both the VC and the CEO have major financial stakes in the venture and as long as there exists a possibility that neither side will always be right or always be wrong, disagreements over the direction of effort will create agency problems for the venture capitalist. (Sapienza & Gupta, 1994, p. 1620)

This uncertainty about the proper course of forward action leaves open the possibility that a CEO may be asked to step aside while still retaining a favorable disposition towards the

VC and other board members who initiated the change. In such circumstances, a firm could still retain the ability to transfer important social capital resources from the founder. What seems to be most salient in this sort of condition is not whether the founder was forced out or left voluntarily, but whether he/she left on friendly or unfriendly terms.

My field work with venture capitalists and founders suggests this particular characteristic makes a huge difference in the outcomes one can expect for the firm. Indeed, one Silicon Valley venture capitalist and board member of a number of startups noted

> …one thing that can really help or hurt the firm going forward is the terms under which the founder leaves. If he leaves under friendly terms then the overall transition has better chances of being smooth. If not, it can really be very destructive for the company. [needs parenthetical reference]

This comment reflects a general feeling about the importance of the personal relationships of those involved with or affected by this succession event. In fact, one founder has even gone so far as to say, "personal relationships are far more important than relationships with the corporation." [needs parenthetical] These arguments and examples lead to the following hypothesis:

H2a: If a Founder-CEO is replaced, greater friendliness of the succession event will be positively associated with the number of actions taken to institutionalize the Founder-CEO's social capital.

In my conversations with lead venture capitalists, who are often the ones charged with carrying out the Founder-CEO transitions, many attested to the role played by exit compensation in ensuring a smooth and friendly transition. One such venture capitalist remarked,

> There is always some compensation issue involved with these founder transitions…In order to make sure you have a smooth transition you need to have buy-in from the outgoing CEO and allow him to save face which almost always entails giving him a soft landing. [insert parenthetical ref]

In line with this logic, it can be argued that the inclusion of some form of monetary compensation as part of the Founder-CEO replacement will increase the likelihood the outgoing founder will cooperate and thereby enable the firm to take actions that help transfer the founder's social capital. This leads to the following hypothesis:

H2b: If a Founder-CEO is replaced, inclusion of exit compensation as part of the succession event will be positively associated with the number of actions taken to institutionalize the Founder-CEO's social capital.

3.3.2.2 CEO Outsiderness

It was noted earlier that the executive succession literature tends to focus on the executive's personal characteristics when examining a CEO succession event. Most notable among these characteristics is the insider/outsider distinction. For the purposes of the current project, the insider/outsider concern may be less of an issue as almost all of the successor CEOs in venture-backed start-ups are outsiders in some sense (Wasserman, 2003). As mentioned before, however, a more continuous measure of "outsiderness," rather than the binary inside/outside distinction, seems to have the most relevance in this particular setting. This is an important gap that has not been adequately studied in even the large firm context. There are major contributions that can be made in this particular area concerning the outsiderness of the successor CEO that may lead to new mechanisms which will alter or influence the success of the CEO transition and the future performance of the firm.

In order to address this important gap in the current literature, I will examine the relationship between new CEO outsiderness and a firm's use of social capital transfer mechanisms. Within the executive succession literature it has been argued that top executives (in this case founders) are only influential and effective during the early years of their tenures (Miller and Toulouse, 1986; Boeker, 1989) and must therefore be replaced as they quickly become impediments to change. In fact, Virany, Tushman, and Romanelli (1992) argue that executive succession is an important mechanism for organizational learning and adaption and is necessary in order to improve organizational performance in turbulent environments. Katz (1982) argued that prolonged tenure of top executives leads to restricted information processing, reliance on routines, and a reduced willingness to take risks. Finkelstein and Hambrick (1990) argue that prolonged firm experience leads to a restricted mindset which limits more novel strategic endeavors. This limitation on the part of managers can lead to negative performance implications for the firm. According to these arguments, the replacement of a founder (and his or her social capital) may serve to benefit rather than harm the firm given the dynamic environments of most startups (Henderson, Miller, and Hambrick, 2006).

Accordingly, this view suggests that the retention of a founder's social capital might serve to restrict or hinder a firm's ability to adapt to its environment and adopt new practices. In fact, many TMT or board members may be more focused on infusing the social network ties of the incoming CEO than on retaining the ties of the outgoing founder. The incoming CEO's outsiderness may accentuate the focus on the infusion of ties (Finkelstein and Hambrick, 1996), thus producing a lack of awareness or lack of perceived value of the predecessor's social capital. The new CEO's outsiderness can be conceptualized as a continuum ranging from extreme insiders (greater combination of firm and industry tenure) to extreme outsiders (no firm or industry tenure). Research suggests that long-tenured executives tend to maintain current firm conditions rather than introducing new strategic changes (Finkelstein and Hambrick, 1990; Wiersema and Bantel, 1993). As most incoming CEOs in founder transitions are from outside the organization (Wasserman, 2003; Lauterbach, Vu, and Weisberg, 1999), they will have very little, if any, organizational tenure. This limited experience within the company may restrict a successor's awareness of important social ties that are currently being mediated by the founder. Whether or not these delicate social capital resources are lost depends on the actions taken by the successor CEO in regard to the founder or the specific individuals within the founder's network. A new CEO that does not have any or has only very limited organizational experience may choose to alter the TMT (Brady and Helmich, 1991) or even bring a group of managers with him/herself in order to help implement changes (Puffer and Weintrop, 1991). It may also be the case that when a CEO with little or no organizational tenure takes the helm, senior executives within the firm will either leave or resist the changes initiated by the new CEO (Helmich and Brown, 1972; Shen and Cannella, 2002). This loss of internal talent, whether a deliberate choice on the part of the new CEO or not, could threaten the internal fabric of the company, putting it on a course of decreased performance and perhaps eventual failure (Hofer and Charan, 1982). Based on the preceding, I propose the following hypothesis:

H3: If a Founder-CEO is replaced, greater outsiderness of the successor CEO will be negatively associated with the number of actions taken to institutionalize the Founder-CEO's internal social capital.

3.3.2.3 Functional Background Similarity

In my field research I also discovered that many of these successor CEOs differ in their functional background. A venture capitalist involved in headhunting a new CEO may actually look for someone with a different functional background which they feel will help them in the next stage of the company's development. A CEO's background has been identified as an important factor affecting his/her cognitive representations (Prahald and Bettis, 1986) and choice of strategy (Gunz and Jalland, 1996). Therefore, an incoming CEO with a similar functional expertise may be more likely to carry out strategic actions similar to those pursued by the Founder-CEO and may be able to more easily replicate or create redundant ties to important others in his/her network. Such similarity may lead the Founder-CEO's successor to believe that there is little need to take actions that institutionalizes these relationships as s/he can merely personally retain and maintain many of the founder's key social ties.

Incoming CEOs that are functionally dissimilar however, are less likely to be committed to the status quo and are more cognitively open, but they are also less likely to be as socially connected (Finkelstein and Hambrick, 1996) and able to tap into the important social capital resources embedded in a founder's network without some additional help. Therefore, under such conditions it is extremely important for the Founder-CEO's successor to take actions to institutionalize the founder's social capital. It may be the case that under certain circumstances it is more important to focus on the incoming CEO's social capital, rather than seeking to also preserve the Founder-CEO's social capital. In an early-stage context, however, I argue that disregarding a founder's social capital may increase the firm's "liability of newness" (Freeman, Carroll, and Hannan, 1983; Li and Guisinger, 1991), making the firm as a whole more vulnerable to failure. While this dissimilarity may appear to affect both internal and external social capital equally, I believe it may have a greater impact on transfer of a Founder-CEO's external social capital.

In order to explain why the external relationships might be more affected by a functionally dissimilar successor CEO I cite Pennings and Lee (1999) who have stated:

> Entrepreneurs, new ventures, and small firms differ markedly from large corporations in terms of the links they maintain. The links that bind them might vary from those that are heavily endowed with trust to those that fit the arm's length relationships. The large corporation is prone to have arm's length relationships with external actors. [needs citation]

If it, is in fact, true that the external social relations of a new venture are different (in terms of value and/or strength) in an early stage setting than they would be in a later stage setting, it may be argued that the issue of social capital transfer will be more salient in a new venture setting. In particular, if a Founder-CEO possesses important external social capital resources and is being replaced by a successor that is functionally dissimilar, the incoming CEO will need to take a number of actions in order to institutionalize these relationships. Consequently, the following hypothesis is proposed.

H4: If a Founder-CEO is replaced, greater similarity in the functional backgrounds of the Founder-CEO and successor CEO will be negatively associated with the number of actions taken to institutionalize the Founder-CEO's external social capital.

3.3.3 Consequences of Founder-CEO Succession

The mixed results of the succession-performance link in the existing literature have already been sufficiently discussed. It has also been mentioned that in order to accomplish a reconciliation and a more accurate understanding of these past results, one must adopt an open system perspective using the systematic contingency approach (Lawrence and Lorsch, 1967; Scott, 1987). Building upon these prior contributions allows us to focus on specific contingencies in the organizational environment that can influence not only the functioning of the organization but also the allocation of power and control within the organization (Pfeffer and Salancik, 1978). By examining the succession-performance relationship in this manner, the top management transition is no longer viewed as an isolated event. Rather, it is seen as a dynamic and complex organizational decision process that can be subject to the influences not only of the external environment but also of internal organizational characteristics (Lin and Li, 2004). Adoption of this perspective provides a unique opportunity to contribute to the current body of literature in meaningful and novel ways.

Paradoxically, while we know an enormous amount about the succession-performance relationship, we also know very little. For example, we know much in that this relationship has been the focus of dozens of different studies using a host of varying methodologies. Yet, though these studies have provided us with a significant foundation of knowledge, they have really given us a very limited and uncertain understanding of the complex nature of the seemingly simple relationship. For instance, we are not entirely sure whether or not the relationship is positive or negative or if it is linear or curvilinear. For this reason, I have left the relationship depicted as neutral or without a positive or negative sign. The value of this model is in the contingent factor "Use of Social Capital Transfer Mechanisms," as this construct will influence the succession-performance (S-P) relationship in productive and positive ways. If the inherent nature of the S-P relationship is negative (succession leads to decreased performance/survival), then the use of social capital transfer mechanisms can mitigate the natural decrease in performance for the firm by transferring key resources embedded in the social relations of the founder to the firm. Similarly, if the inherent nature of the relationship is positive (succession leads to increased performance), then the use of social capital transfer mechanism can enrich the positive relationship or have no effect on it depending on the extent to which the firm sought to transfer important social capital resources. In either case, the outcomes for the firm are predicted to be positive as noted by the positive sign next to the moderating influence of the Use of Social Capital Transfer Mechanisms construct.

Prior research has argued that top management changes can only add disruption to the organization, thereby worsening performance (Grusky, 1963; Cannella and Lubatkin, 1993). More specifically, Friedman and Singh (1989) suggested that top management succession may result in two types of disruptions: destroying fit between the organization and its environment, and disrupting the internal authority structure. By transferring the internal social capital of a founder, the company is able to stabilize its internal environment from the shocks that could come from the founder's exit (Carroll, 1984). This stabilization of the internal environment lessens the risk of the loss of valuable employees through attrition or clashes between new and old managers over culture, norms, and processes. Similarly, a firm that is able to transfer a founder's external social capital is positioned to secure future growth and performance for itself. This leads to the following hypotheses:

H5a: Taking more actions to institutionalize the Founder-CEO's social capital reduces the likelihood Founder-CEO succession will have a negative effect on firm performance.

H5b: Taking greater action to institutionalize the Founder-CEO's social capital reduces the likelihood Founder-CEO succession will have a negative effect on firm survival.

Chapter 4

Methodology: Sample, Data Collection, Variables, and Analysis

4.1 Sample and Data Collection

The population for this study includes the Founder-CEO successors, their top management team (TMT), and venture capitalists. Each of these categories of individuals provides a different lens through which I can examine the phenomenon of interest. The Founder-CEO successor and his or her TMT will be useful in providing data regarding the actions taken to transfer critical relationships, their perception of the terms of exit, and the performance of the organization after the founder had left. The venture capitalists often sit on the boards of these young companies and are generally the ones who signal to the company that it is time for the founder to relinquish the top spot (Levensohn, 2006). Accordingly, it is important to capture the TMTs' perspectives on the transitioning of a founder in order to understand: (1) how they perceived the terms of the exit, (2) the impetus for the transition, (3) which relationships were critical to keep, (4) what actions were taken to retain those relationships, and (5) how a successor was ultimately chosen.

In order to effectively capture these perspectives through my survey, I first conducted over 50 personal interviews with individuals from the categories discussed previously. My purpose in conduting these interviews was two-fold. First, I wanted to develop an understanding of how Founder-CEO transitions were viewed from these different perspectives and what, if any, patterns would emerge in terms of specific actions taken to ensure a smooth transition. Second, collecting this qualitative data served to better inform the survey questions that I ultimately presented to the different groups. In constructing this survey, each group received a survey tailored to their particular category. Some of the individuals involved in this qualitative part of the process were asked to pretest and provide feedback on the survey questions and length. This was extremely useful in ensuring that the final set of questions for the different surveys were clear, concise, and accurate. It also helped to improve the response rate as many of the individuals who were surveyed indicated they were not willing to fill out lengthy survey instruments.

Once the survey instrument was refined, I used an online survey company to administer the survey via email. In order to ensure I had an adequate sample size, I decided to build a list of candidate companies whose primary line of business centered on software and information technology by using the VentureXpert database. I refined this database by considering only those companies who had received at least one round of financing within the 2000 to 2006 time period, had a definitive outcome (defunct, acquired, or go public), and had contact information for at least one of the categories mentioned above. I purposely excluded those firms who had received funding but had not had an outcome (still private) as these companies are either too young to obtain any reasonable performance measures or may have other incentives to remain private. Furthermore, in order to keep the criteria simple, I only included those companies in my initial sample that had one of the three outcomes mentioned above. I ended up with a list of 1559 companies of which 1103 had venture capital contacts. Of the 1559, 25% of them went defunct, 13% went public, and 62% were acquired. I mention this because the surveyed was administered through email and some of the email addresses were no longer used by the executives associated with the companies, which led me to anticipate a larger response from the venture capital category as they were more likely to receive the email and be able to respond to it.

The survey was carried out in two successive rounds. The first email introduced the project, stated that the survey would take between 5 to 7 minutes, and had a link that would take them to the online survey. On the first page of the survey, respondents were asked to identify which category they belonged to. The software then customized the survey based on that category. The essential questions were the same for all categories but the wording was customized to their specific involvement in the transition (if one occurred) and/or the professionalization (meaning that the firms employed some of these social capital transfer actions in order to institutionalize the founder's social capital despite the fact that he or she is still CEO) of the firm. I use the terms *transition* and *professionalization* here as they are terms often used and understood by practitioners. After the first wave of surveys were administered and responses were received, I sent out a reminder email requesting those who had not yet responded to please respond before the survey closed. This email was sent out approximately two weeks after the initial email. I then allowed those who received the second email two additional weeks to respond to the survey before I closed it and collected all the data.

The survey collected information on, among other things, executives' background, tenure, and demographics, as well as what firm he/she worked for, what VCs were involved, VC power on the board, whether or not the succession event was amicable, whether certain positions were developed in the company to manage the relationships established by the CEO, and who had put them in place. These questions also explored issues such as whether the Founder-CEO had personally interacted with the lead venture capitalist, how far back their relationship went, whether it was personal and/or professional, how close/strong was it, whether it was a long-term or short-term relationship, what happened to the relationship when the founder left, and what efforts (if any) were taken to maintain the relationship. It also sought to capture whether a transition took place and what prompted the transition if one did occur. The survey was sent to multiple representatives for each company when the contact information was available. For convenience to the reader I have included a copy of my survey and the form emails in Appendix A.

Of the original 1559 companies contacted, 185 representatives of these companies clicked on the link in one of the two emails and of those 185 companies, 126 of them actually filled out the survey and had usable data. I also had an additional 11 responses with usable data for companies that were already included in the 126. In other words, I had two respondents from 11 companies in the 126 firms in my final sample.

My initial response rate is just over 8 percent, which is on the lower end of the normal range of responses, but still reasonable considering the sensitive nature of the questions and the level of the executives targeted (Wasserman, 2003; Waldman, Ramirez, Gabriel, House, and Puranam, 2001; Finkelstein, 1992; MacMillan, Kulow, & Khoylian, 1988). Of the respondents, 73% were venture capitalists, 13% were the Founder-CEOs, 6% were TMT members, 5% were outside board members, and 3% were the CEO successors. Utilizing a methodology similar to McDougall and Robinson (1990), I examined the venture capitalist non-respondents to the survey. Surveying the venture capital non-respondent, I was able to contact 42 VCs. It was found that 16 (38%) of these VCs had a general policy of not responding or rarely responding to surveys. This percentage is similar to that found by Pearce and Zahra (1991) when examining corporate officers. In Pearce and Zahra's (1991) research, they automatically removed this percentage from the total number of potential respondents. As mentioned previously, only 1103 had venture capital contacts associated with them. If the percentage of venture capitalists who are not able to respond to surveys is eliminated, I obtained 18% of potential respondents. The revised response rate of 18% is consistent with the response rate of other research on venture capitalists (Vance, 2000; MacMillan, Kulow, & Khoylian, 1988) and is near the upper ranges of studies found in the literature as described previously.

More important than the specific response rate percentage is the possibility of a non-response bias. Utilizing common survey non-response bias techniques, two checks of non-response bias were made. Armstrong and Overton (1977) demonstrated that in a two-stage mailing the second-stage respondents are similar to non-respondents since they require an additional stimulus to respond. Thus, a comparison was made between the two waves of surveys. I found no significant differences on the key variables that are used to test the hypotheses, thus demonstrating that the respondents and non-respondents were similar.

Additionally, specific characteristics of respondents and non-respondents were compared. These non-responders were identified utilizing those VC who had clicked on the link but did not participate in the survey. I used this group because I knew they had received the survey but did not respond. Prior research has shown that VC behavior may vary based on the amount of time he/she spends with the portfolio company, the amount of capital invested, and the portfolio company's developmental stage (Elango, Fried, Hisrich, & Polonchek, 1995). Therefore, respondents were compared against a sample of non-respondents on these variables. No significant differences were observed.

4.2 Variables

4.2.1 Dependent Variables

Another potential problem with survey data is the possibility of a common method or same source bias. In order to ensure that this was not a problem for my analysis, I utilized data from VentureXpert to construct my performance and survival dependent variables. Unlike studies that use public companies as their population of interest, private companies are not required to disclose performance data. This presents a challenge to those researchers interested in this population (Wasserman, 2003). In order to overcome the challenge of the spotted nature of performance data found in third-party databases such as VentureXpert, I created two measures of performance and tested them independently.

Firm Performance. The first measure of performance uses a Tobin’s Q logic (market value over total assets) and is constructed using the last post-round evaluation of the market value of the company and the total amount of money invested in the company. In the IT and software industry, firms do not have a lot of capital wrapped up in physical assets. Most of the value of the company is in the intellectual assets and copyrights associated with the product offerings. As a result, the total amount of capital invested in the company can be a reasonable proxy for the amount of physical assets the firm has used to create an agreed upon market value. In accordance with this logic, I have constructed what I call a VBI (valuation by investment) index that captures the performance of these different firms relative to one another. In order to ensure this variable was consistent with other performance variables that have been used previously, I also collected the median net sales for the firms over the 7-year time period and used it as a second measure of performance. The use of sales gathered from archival resources has been established as a highly reliable measure of performance in new ventures (Brush and Vanderwerf, 1992). Since sales data is not reported consistently for each year (private companies can decided when and whether they will report) I have taken the median value over the 7-year window as mentioned to ensure I had net sales figures for the companies in my final sample. This measure will use a logarithmic transformation in order to ensure normal distribution of the dependent variable.

Firm Survival. Another dependent variable that was used to test a number of the hypotheses is the survival, or rather failure, of a venture-backed organization. Failure has taken many shapes in prior research, including bankruptcy and acquisition as equals in terms of firm failure. For the purposes of this study, I will differentiate between these two phenomena, as in reality the outcomes of these two different events can have disparate effects on shareholders.

In traditional organizational ecology research, acquisitions have been viewed as firm failure and death. There are many reasons why being acquired should be operationalized as a separate outcome. First, some firms' goals at the outset are to make the firm attractive to potential suitors for an acquisition. Even if acquisition was not the goal, acquisitions are generally profitable for the shareholders of acquired firms, as opposed to bankruptcy which has a decidedly negative effect. As the effects of these two outcomes are so disparate, they should be considered separately. (Chatterjee, 1986; Lubatkin, 1987; Singh and Montgomery, 1987; Datta, Pinches at al., 1992; Anand and Singh, 1997).

This survival dependent variable was also collected from the VentureXpert database. This particular variable describes the current status of the company and has three categories that are pertinent to my study: defunct, subsidiary, and public. As mentioned earlier, those companies who were still private were not included in my study so I organized each of the companies in my sample into one of these three categories. In my final sample, 11% had gone defunct, 18% went public, and 71% were acquired.

Social Capital Transfer Mechanisms. In order to capture what transfer mechanisms were used at a given organization,, I included a list of potential actions (mechanisms) which a firm might use to secure key relationships during the founder's transition or during the professionalization period. Respondents indicated which if any of the listed actions were taken. They were also given space to include others that were not on the list provided. The actions on the list and the other actions noted by the respondents were categorized as either internally or externally focused. This allowed me to count the number and types of mechanisms employed by an organization during their attempt to transfer important social capital from the founder. This construct is used as both a dependent and an independent variable. Since this variable is a count variable it will be squared when it is used in the 2SLS, 3SLS, OLS, binary and multinomial logit regression according to Cohen, Cohen, West, and Aiken (2003: 526) in order to ensure the variable is better behaved (closer to meeting the OLS assumptions of normality).

4.2.2 Independent Variables

Terms of Exit. The conditions surrounding a founder's exit are predicted to play an important role in directly affecting the ability of an organization to use social capital transfer mechanisms. The three dimensions I focused on are the friendliness and voluntariness of the exit as well as the involvement of the founder in the selection of the successor CEO. These three dimensions will be captured on the survey by using three items related to each dimension. For example, questions such as: "How amicable was the transition?", "How involved was the founder in selecting his/her replacement?", and "To what extent do you think that the founder voluntarily stepped down from the office of CEO?" were asked in order to capture the three dimensions about which I have hypothesized. The alpha coefficient for these three was .95, so I combined them into one variable.

A second variable that was used to assess the terms of exit was the use of exit compensation. This variable is a count variable that allowed the respondent to identify from a list of four forms of monetary compensation in order to ensure a smooth transition. Here, again, respondents were provided the opportunity to add responses not provided on the survey. These compensation options were derived from my field work and interviews.

CEO Outsiderness. In order to measure this particular construct I used two measures. The first measured was a scale made up of the degree of organizational tenure and new venture experience ranging from “little to none” to “a large amount.” The use of new venture experience is new to the literature on CEO outsiderness but holds particular relevance for this research context. Many employees drawn to work for new ventures can become concerned with a successor CEO who lacks new venture experience and might withhold important information and/or resources that can influence the optimal functioning of the firm. This lack of experience could also cause the executive to make decisions that subject a more fragile organization to risks from which it cannot recover if things go badly.

Functional Background Similarity. Similarly, employees of a high tech venture may respond more favorably to an incoming CEO with a similar functional background than one that is not similar. An individual’s functional background may also allow the executive to be attentive to certain important stimuli in the environment to which (s)he would not otherwise pay attention. This variable was constructed as a binary variable capturing whether or not the successor CEO had the same functional background as the Founder-CEO.

Control Variables. A number of control variables were used in order to rule out other alternative explanations in this study. Among these variables were prior organizational performance (survey item assessing prior performance of startup), prior startup experience of the founder and of the successor, VC experience (number of boards, number of years experience), firm maturity (number of rounds the firm has been through), firm size (number of employees), presence of founder-CEO, concentration of investors (number of firms invested in the startup), VC respondent dummy, and two period dummy variables (one for outcome events in 2000 when the market was hot and one for the period (2001-2002 when the market was cold)[1]. These variables are helpful in producing a conservative test that is in line with much of the succession research that focuses on the large, public firm context.

4.3 Statistical Analyses

4.3.1 Analysis for Hypotheses 2(a&b), 3, & 4

In order to test the relationship among exit terms, outsiderness, and use of social capital transfer mechanisms, I use negative binomial regression because the use of social capital transfer mechanisms is a count variable. I first ran these regressions using a Poisson regression as that is common practice and the preferred technique with count dependent variables. In order to assess whether or not this technique was suitable to the data, I estimated the *goodness of fit* for the models. This robustness check seeks signs of overdispersio—that is, greater variance than might be expected in a Poisson distribution. The chi-square statistic was large, indicating that the Poisson regression is not appropriate. I then ran the analysis using negative binomial regression. In this model, the count variable is believed to be generated by a Poisson-like process, except that the variation is greater than that of a true PoissonI also carried out robustness checks to ensure this model was appropriate given the data. Specifically, I examined the likelihood

[1] There variables were not included in the logistic regression models because they perfectly predicted the outcome.

ratio, which is another test of the overdispersion parameter alpha. When the overdispersion parameter is zero, the negative binomial distribution is equivalent to a Poisson distribution. If the coefficient is not statistically different from zero the negative binomial results are identical to the Poisson results we obtained earlier. In the case of the models I ran, the coefficient is statistically different confirming that I must use the negative binomial regression in order to test Hypotheses 2(a&b) through 4 from Chapter 3.

4.3.2 Analysis for Hypotheses 1a & 5a

A potential problem with testing some of the hypotheses presented in Chapter 3 is the problem of endogeneity. Endogeneity is a term arising from econometric analysis that describes a situation in which the value of one independent variable is dependent on the value of other predictor variables (Hamilton, Barton, and Nickerson, 2003). Because of this endogeneity, significant correlation can exist between the unobserved factors contributing to both the endogenous independent variable and the dependent variable, which results in biased estimators (incorrect regression coefficients). In order to overcome these issues of endogeneity, a researcher may employ either a simultaneous equations approach or a structural equation modeling approach in order to isolate the independent effects of the various predictor variables. For the purposes of this study, a structural equation modeling approach seems most appropriate and will therefore be used. structural equation modeling (SEM) is a statistical technique for building and testing statistical models, which are sometimes called causal models. It is a hybrid technique that encompasses aspects of confirmatory factor analysis, path analysis, and regression, which can all be seen as special cases of SEM. SEM encourages confirmatory, rather than exploratory, modeling. Thus, it is suited to theory testing rather than theory development (Anderson and Gerbing, 1988). SEM generally starts with a hypothesis, represents it as a model, operationalizes the constructs of interest with a measurement instrument, and finally tests the model. Two special cases of SEM that I use are the two-stage least squares model and the three-stage least squares model.

Since SEM is a confirmatory technique, the model must be specified correctly based on the type of analysis that the modeler is attempting to confirm. There are usually two main parts to SEM: the structural model showing dependencies between endogenous and exogenous variables, and the measurement model showing the relations between the latent variables and their indicators. For example, confirmatory factor analysis models contain only the measurement part, while linear regression can be viewed as an SEM that only has the structural part. Specifying the model delineates relationships between variables that are thought to be related (and therefore want to be 'free' to vary) and those relationships between variables that already have an estimated relationship, which can be gathered from previous studies (these relationships are 'fixed' in the model).

In order to test the relationships among the variables mentioned previously, I specify a firm performance equation for VBI, and then use instruments to solve for the endogeneity of the use of social capital transfer mechanisms. These equations are listed below:

)

Firm performance

$$VBI = \beta_0 + \beta_1 SCT + \beta_2 FT + \delta_1 + \mu_1 + \varepsilon_1$$

4.2)

Social Capital Transfer

$$SCT = \theta_0 + \theta_1 Z_1 + \theta_2 FT + \delta_2 + \mu_2 + \varepsilon_2$$

The dependent variable in Equation 4.1 is the performance measure for the firm (either VBI or median sales) and the dependent variable in Equation 4.2 is the use of social capital transfer actions. Firm performance is given by VBI; FT is a dummy variable denoting whether or not a founder transition occurred; β_1 and β_2 are the regression coefficients; δ_1 and δ_2 are the firm controls (firm size, firm maturity, presence of Founder-CEO); and μ1 and μ2 are the VC controls (concentration of investors, VC experience). ε_1 and ε_2 are the error terms, which are thought to be correlated with SCT because the use of social capital transfer mechanisms is endogenous and related to the occurrence of a founder transition. Therefore I used an instrumental variables technique to create new a new dependent variable that does not violate OLS regression's recursivity assumption.

In equation 4.2 SCT is endogenous and related to the occurrence of a founder transition and to the exogenous instrumental variables of Z_1 (outsiderness, functional background similarity, terms of exit). My two-stage least squares (2SLS) regression satisfies the rank and order conditions for model identification (see Greene 1997). To ensure that my error term ε_1 is uncorrelated with my instrumental variables I conducted a Hansen-Sargan test for the validity of instruments. The null hypothesis is that the instruments are valid instruments—that is, uncorrelated with the error (see Chapter 8 in Baum, 2006). Under the null, the test statistic is distributed as chi-squared in the number of over-identifying restrictions. Rejection of the null casts a doubt on the validity of the instruments. The Hansen-Sargan statistic was not significant (.90), providing evidence that the model has been identified correctly. Another potential problem in 2SLS regression is that if any of the exogenous variables can predict the squared residuals, the errors are conditionally heteroskedastic. In order to test for this, I ran the Pagan-Hall test statistic. While the Pagan-Hall is not yet widely used, it is seen as superior because it is robust to the presence of heteroskedasticity elsewhere in a system of simultaneous equations and to non-normal distributed disturbances (Baum, 2006). Similar to the Hansen-Sargan, rejection of the null would signal a problem with the model. The Pagan-Hall statistic for my model was not significant (.68) using fitted values, which indicates that my models did not have problems with heteroskedasticity.

For the purposes of this study, SEM (specifically 2SLS) appears to be the appropriate statistical technique as it allows for selected endogenous variables to be both independent and dependent simultaneously. This method also allows the researcher to control for a "method factor" that accounts for different methods in which data was collected (in my case survey vs. database, etc.). Additionally, I ran two separate OLS regressions manually, performing a two stage analysis, and found no differences among the results from the 2SLS regression. I also ran a three stage least squares (3SLS) with additional exogenous added to predict the occurrence of a founder transition. Unfortunately, these models failed the Hansen-Sargan test, indicating that the model was over-identified and was not appropriate.

4.3.3 Analysis for Hypotheses 1b & 5b

In order to test the effects of social capital transfer and the occurrence of a founder replacement on survival, I ran a simple binary logit model that defined failure as those companies that went defunct and survival as those companies that were either acquired or went public according to the logic presented in section 4.2.1. I subsequently ran multinomial logit regression to test the effects of the social capital transfer mechanisms on the organization's survival outcome as argued by hypotheses 1b and 5b. Defining SO as the variable indicating the survival outcome of the business, I let SO = 1 denote that the business went defunct, SO = 2 that the business went public, and SO = 3 that the business was acquired. I did this to get a more refined view of the variables of interest on the different categories of survival and failure. This produces the following two equations to be run in order to test for a firm's survival outcome:

(4.3)

$$log(P(\mathrm{SO}=2)/P(\mathrm{SO}=1) = \beta_0 + \beta_1\mathrm{SCT} + \beta_2\mathrm{FT} + \delta_1 + \mu_1 + \varepsilon_1$$

and

$$log(P(\mathrm{SO}=3)/P(\mathrm{SO}=1) = \beta_0 + \beta_1\mathrm{SCT} + \beta_2\mathrm{FT} + \delta_1 + \mu_1 + \varepsilon_1$$

In order to ensure that the model was robust I ran two additional tests. The first test, the Wald test, tests the null hypothesis that the coefficients of the variable equal zero across all equations. This results of this test showed that there was independence among variables. The second test, the Hausman test, tests the assumption of the independence of irrelevance alternatives (IIA) for each possible omitted category. This test confirmed that the odds (Outcome 2 [or 3] versus Outcome 1) are independent of other alternatives. It therefore appeared that these models were appropriate to test the hypothesized relationships among the variables for my data.

Chapter 5

Results: Empirical Examination of Social Capital Transfer in New Ventures

5.1 Descriptive Statistics

Before presenting the results of the models discussed in Chapter 4, I am including two tables. Table 5.1 below displays some descriptive statistics and Table 5.2 provides correlation coefficients among the key variables of interest.

Table 5.1

Variable	Obs.	Mean	Std. Dev.	Min	Max
Firm Performance (vbi index)	125	1.083	1.215	0.000	5.193
Outcome	126	2.587	0.684	1.000	3.000
Total SCT	126	4.500	3.971	0.000	14.000
Had Founder Transition	126	0.651	0.479	0.000	1.000
Ceo Outsiderness	126	-0.933	1.186	-4.500	0.000
Functional Similarity	126	0.579	0.496	0.000	1.000
Friendly Index	126	0.995	1.463	0.000	5.000
Exit Compensation	126	0.206	0.495	0.000	2.000
VC Experience (years)	126	9.052	9.296	0.000	38.000
No. of Rounds	125	4.096	2.431	1.000	11.000
No. of Firms Invested	125	5.872	3.759	1.000	19.000
VC Experience (# of brds)	126	11.714	15.003	0.000	100.000
VC Dummy	126	0.754	0.432	0.000	1.000
No. of Employees	126	60.222	42.088	2.000	400.000
Had Founder CEO	126	0.921	0.271	0.000	1.000
Net Sales (log)	126	4.478	4.671	0.000	12.766

5.1: Summary and Descriptive Statistics for Key Variables

Table 5.2

	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17
1. Firm Performance (vbi index)	1.00																
2. Outcome	0.08	1.00															
3. Median Net Sales (log)	0.23	0.40	1.00														
4. Total SCT	0.13	0.19	0.29	1.00													
5. Ceo Outsiderness	-0.09	0.04	-0.17	-0.22	1.00												
6. Functional Similarity	0.03	-0.11	-0.12	-0.22	0.45	1.00											
7. Friendly Index	0.18	-0.21	0.11	0.41	-0.63	-0.26	1.00										
8. Exit Compensation	0.13	-0.12	0.10	0.41	-0.25	-0.03	0.54	1.00									
9. Had Founder Transition	0.06	-0.11	0.01	-0.14	-0.59	-0.29	0.51	0.31	1.00								
10. VC Experience (years)	0.04	-0.09	0.21	0.21	-0.28	-0.12	0.30	0.15	0.15	1.00							
11. No. of Rounds	0.12	0.04	0.17	0.09	-0.08	-0.15	0.10	0.18	0.26	0.19	1.00						
12. No. of Firms Invested	0.19	0.03	0.20	0.02	-0.19	-0.15	0.15	0.16	0.31	0.19	0.72	1.00					
13. VC Experience (No. of brds)	-0.02	-0.08	0.15	0.20	-0.19	-0.07	0.19	0.06	0.04	0.80	0.14	0.18	1.00				
14. VC Dummy	0.10	-0.26	0.07	-0.11	-0.08	0.26	0.12	0.09	0.20	0.56	0.20	0.27	0.45	1.00			
15. Firm Size (# of employees)	-0.03	0.24	0.20	0.00	0.00	0.02	-0.10	-0.06	0.00	-0.09	0.06	0.16	-0.04	-0.04	1.00		
16. Outcome Event in 2000	-0.14	0.31	0.19	0.08	-0.14	-0.12	0.01	0.02	0.13	0.09	0.03	-0.01	0.04	0.00	0.04	1.00	
17. Outcome Event in 2001-2002	-0.06	-0.04	-0.09	0.00	0.05	0.11	-0.04	0.20	0.14	0.10	0.04	0.08	0.18	0.16	-0.01	-0.05	1.00

5.2: Correlation Matrix for Key Variables

5.2 Results for Hypotheses 1a & 5a

The results of Hypotheses 1a and 5a both required the use of a 2SLS regression method as was described previously in Chapter 4. Hypothesis 1a stated that the transfer of Founder-CEO social capital will lead to better performance. Hypothesis 5a argued that the transfer of Founder-CEO social capital will moderate any negative effects wrought on performance by the transitioning of the founder..

Table 5.3

	(1)	(2)	(3)	(4)	(5)	(6)
	Firm Performance	Firm Performance	Net Sales (log)	Net Sales (log)	Firm Performance	Net Sales (log)
Total SCT(sqr)	0.235*	-0.056	0.921*	5.380	0.220+	0.867*
	(1.98)	(0.06)	(2.14)	(1.40)	(1.89)	(1.98)
Had Founder Transition	0.066	-0.421	-0.221	8.702		
	(0.27)	(0.23)	(0.25)	(1.17)		
No. of Rounds Company Rcvd	-0.029	-0.018	0.067	-0.101	0.001	0.048
	(0.48)	(0.25)	(0.30)	(0.35)	(0.02)	(0.19)
No. of Firms Invested in Company	0.080+	0.074	0.172	0.270	0.043	0.150
	(1.92)	(1.60)	(1.13)	(1.45)	(0.99)	(0.91)
Number of Employees	-0.002	-0.002	0.019*	0.018+	-0.001	0.021*
	(0.73)	(0.71)	(2.10)	(1.82)	(0.62)	(2.38)
Had Founder CEO	0.460	0.559	0.129	-1.633	0.290	5.501*
	(1.16)	(1.04)	(0.09)	(0.76)	(0.46)	(2.30)
VC Total Boards	-0.015+	-0.011	0.017	-0.013	-0.008	0.041
	(1.70)	(0.99)	(0.55)	(0.29)	(0.62)	(0.85)
VC Dummy	0.464	0.301	0.667	2.903	0.232	0.589
	(1.60)	(0.53)	(0.64)	(1.27)	(0.67)	(0.45)

Outcome Event in 2000	-1.081+	-1.076+	4.285*	4.782*	-1.131*	3.895+
	(1.82)	(1.80)	(1.99)	(2.00)	(2.07)	(1.90)
Outcome Event in 2001 - 2002	-0.407	-0.393	-1.798	-2.204	-0.350	-2.800+
	(1.00)	(0.94)	(1.22)	(1.32)	(0.88)	(1.88)
Total SCT(sqr) X FT		0.241		-4.666		
		(0.25)		(1.23)		
Constant	-0.133	0.408	-0.136	-8.333	0.309	-5.414+
	(0.26)	(0.22)	(0.07)	(1.14)	(0.41)	(1.92)
Observations	125	125	125	125	81	81
Absolute value of z statistics in parentheses						
+ significant at 10%; * significant at 5%; ** significant at 1%						

5.3: Two-stage Least Squares Regression Models with Firm Performance (vbi index) and Net Sales as Dependent Variables.

Table 5.3 displays the results from four different 2SLS models that were run. Models 1 and 2 use the vbi performance measure as their dependent variable and Models 3 and 4 use log net sales as their dependent variable. Models 1 and 3 empirically test Hypothesis 1a while Models 2 and 4 test Hypothesis 5a. Models 5 and 6 are equivalent to Models 1 and 3 except that they are run on only those observations that had a founder transition event.

The results from Models 1 and 3 support Hypothesis 1a's assertion that the use of social capital transfer mechanisms improves performance outcomes for a firm. I was encouraged by the fact that I found a significant (at the .05 level) and positive result for this variable for both dependent variables. This also provides some legitimization for the VBI variable (for use with new ventures) although more work needs to be done with it. In Model 1, the number of firms invested was also significant and positive. Interestingly, another control, total boards sat on by lead VC, was marginally significant and negative suggesting that the more boards a lead VC has sat on the worse the firm's performance.

This may be explained by the notion that VCs who sit on a number of boards simultaneously might not be able to give adequate attention to any one company and therefore the company is not able to draw from the experience and wisdom of the VC. Alternatively, it could also reflect a greater willingness by richer, more seasoned investors to cut loose from a venture instead of digging in with more youthful vigor and doing more to make the venture a success. In Model 3, the number of employees is also significant and positive. Given that the dependent variable in this model is net sales, it suggests that larger organizations tend to have more sales. While this is not surprising, it provides assurance that the controls are making the tests conservative. It is also important to note that the use of social capital transfer mechanisms is still significant in Models 5 and 6 which are run on the reduced set of observations. This suggests that engaging in actions that are targeted at transferring the founder-CEO's social capital in companies where a transition is taking place will lead to better overall performance for the firm moving forward.

The results from Models 2 and 4 do not provide any support for Hypothesis 5a. Neither the interaction term nor the first order terms are significant. The two control variables discussed above from Models 1 and 3 that were significant are only marginally significant in Models 2 and 4. These results suggest then that the use of social capital transfer mechanisms does not appear to moderate the relationship between a founder's succession and the performance of a firm.

5.3 Results for Hypotheses 1b & 5b

The next set of results was obtained by using a binary logit and multinomial logit technique to test Hypotheses 3b and 4b. Hypothesis 1b argued that the more a company takes actions to institutionalize a Founder-CEO's social capital, the more likely the company will be to have a favorable survival outcome. Hypothesis 5b stated that the more a company takes actions to institutionalize a Founder-CEO's social capital, the more that social capital will moderate any negative effects of the transitioning of the founder on a favorable survival outcome.

Table 5.4

	(1)	(2)	(3)
	Firm Survival	Firm Survival	Firm Survival
Had Founder Transition	2.702	4.367+	8.311*
	(1.32)	(1.85)	(2.24)
VC Experience - Years	0.954	0.941	0.945
	(0.96)	(1.19)	(1.06)
No. of Rounds Company Rcvd	1.128	1.079	1.084
	(0.65)	(0.40)	(0.42)
No. of Firms Invested in Company	0.927	0.943	0.964
	(0.63)	(0.48)	(0.29)
Number of Employees	1.035+	1.052*	1.037
	(1.80)	(2.36)	(1.63)
VC Total Boards	1.016	1.015	1.015
	(0.51)	(0.42)	(0.40)
Total SCT(sqr)		1.779*	2.413*
		(2.01)	(2.29)
Total SCT(sqr) X FT			0.485
			(1.32)
Observations	125	125	125
Absolute value of z-statistics in parentheses			
+ significant at 10%; * significant at 5%; ** significant at 1%			

5.4: Binary Logit Regression Using Firm Survival as the Dependent Variable

Table 5.4 displays the results of the binary logit regressions using the survival dependent variable that differentiated those ventures that went defunct from those that were either acquired or went public. Model 1 uses only the control variables. Model 2 tests Hypothesis 1b and provides evidence supporting the claim that the use of actions to transfer social capital increases the likelihood of firm survival. Interestingly enough, the occurrence of a founder transition was significant and positive suggesting that founder transitions increase the likelihood of firm survival. The firm size variable (number of employees) was also significant and positive in this model. Model 3 tests for Hypothesis 5b and finds no empirical evidence to support it, a finding similar to the models presented in the last section.

In order to examine these relationships in more detail however, I test these hypothesized relationships using a multinomial logit model which differentiates between acquisition and going public as survival outcomes. The dependent variable for these two models is a categorical variable that listed three potential outcomes for the company: defunct, public, or acquired. A multinomial logit model assesses the probability that one outcome will be selected over another based on the influence of the independent variables. For this study I have chosen 'defunct' as the base category and therefore assess the likelihood of a company going public versus defunct as well as the probability of a company being acquired versus going defunct. The results for these models are captured in the Table 5.5 below:

Table 5.5

	(1)	(2)	(3)	(4)	(5)	(6)	(7)
	Acq/Def	IPO/Def	Acq/Def	IPO/Def	IPO/Acq	Acq/Def	IPO/Def
Total SCT	1.196+	1.298*	1.278+	2.050**	1.085	1.166	0.773
	(1.72)	(2.21)	(1.65)	(3.17)	(1.11)	(1.01)	(1.01)
Had Founder Transition	4.931*	0.853	6.692+	42.881*	0.173**		
	(1.96)	(0.17)	(1.90)	(2.19)	(2.69)		
VC Experience - Years	0.936	0.952	0.937	0.950	1.017	1.008	1.052
	(1.22)	(0.65)	(1.11)	(0.66)	(0.26)	(0.09)	(0.36)
No. of Rounds Company Rcvd	1.061	1.019	1.070	0.950	0.960	1.153	1.174
	(0.31)	(0.08)	(0.36)	(0.19)	(0.23)	(0.62)	(0.44)
No. of Firms Invested in Company	0.931	1.030	0.946	1.129	1.107	0.887	1.123
	(0.60)	(0.20)	(0.45)	(0.73)	(0.91)	(0.84)	(0.59)
Number of Employees	1.041*	1.053*	1.025	1.045+	1.011+	1.041+	1.060*
	(1.97)	(2.44)	(1.14)	(1.89)	(1.94)	(1.76)	(2.37)
VC Total Boards	1.015	0.987	1.016	1.000	0.972	0.925	0.932
	(0.43)	(0.26)	(0.39)	(0.01)	(0.68)	(1.04)	(0.61)
Outcome Event in 2000	0.070	1.436e+17	0.941	3.606e+18	1.021e+17	0.001	4.243e+17
	(0.00)	(.)	(0.00)	(.)	(0.00)	(0.00)	(.)
Outcome Event in 2001 - 2002	4.400e+15	0.569	4.487e+15	1.383	0.000	5.714e+15	0.525
	(.)	(0.00)	(.)	(0.00)	(0.00)	(.)	(0.00)
Total SCT(sqr) X FT			0.569	0.055**			
			(0.92)	(3.06)			
Observations	125	125	125	125	125	81	81

5.5: Multinomial Logit Regression Models with Outcome as the Dependent Variable

Model 2 in Table 5.5 displays the results for Hypothesis 1b which is an empirical examination of the direct effect of the use of social capital transfer mechanisms on the firm's survival outcomes. From the results, it appears there is strong empirical evidence that engaging in actions to transfer a founder's social capital increases the likelihood that a company will go public versus going defunct (significant at the .05 level) and marginally significant support that engaging in social capital transfer actions will increase the probability that the firm will be acquired versus going defunct. In the comparisons of the acquisition category to the base category (defunct), the occurrence of a founder transition was significant and positive, suggesting that undertaking a founder transition will increase the likelihood that the firm will experience a more favorable survival outcome.

Similar to the results from the 2SLS models above, the interaction term testing the effect of social capital transfer mechanisms on the relationship between founder's transition and survival was not significant for the acquisition vs. defunct category. In contrast to those findings however, the interaction term for the effect of social capital transfer mechanisms on the relationship between founder's transition and survival—for the IPO vs. defunct category—was significant as were the two second order terms in Model 4. These results provide partial support for Hypothesis 5b, suggesting that the use of social capital transfer actions might act as a moderator in the succession-survival relationship when comparing the likelihood the firm will IPO vs. go defunct. This mixed result might be attributed to the exclusion of some additional variable that is important to unpacking the succession-survival link. Whether this is the case or not, for the purposes of this study it appears that the use of social capital transfer mechanisms is not a clear contingent factor in helping us to understand whether or not a firm that undergoes a Founder-CEO transition will experience a more favorable survival outcome. Models 6 and 7 are equivalent to Models 1 and 2 although they are run on the reduced set of observations that include only those firms that experienced a founder transition. The use of social capital transfer mechanisms was not significant in either model but this may be partially the result of the fact that only eight firms made up the base category, which increases the chance for random error to muddy the statistical analysis.

5.4 Results for Hypotheses 2 through 4

As described in Chapter 4, I used negative binomial regression to empirically test the hypothesized relationship from Chapter 3. Specifically, Hypotheses 2a & 2b argued that the more friendly the exit terms in a Founder-CEO transition, the more likely a firm would be able to engage in actions targeted to transfer important social capital. Hypothesis 3 argued that the degree of outsiderness of the incoming CEO (as a result of limited organizational tenure and/or new venture experience), correlates negatively to the ability of the firm to retain the Founder-CEO's internal social capital. Finally, Hypothesis 4 argued that the greater the functional background dissimilarity of the incoming CEO, the less likely the firm will be to take actions to retain the Founder-CEO's external social capital. The first two hypotheses incorporate both internal and external social capital, so the dependent variable is the total count of actions used (both internal and external). Hypothesis 3 looks only at the internal social capital and

Hypothesis 4 examines only the external social capital. I will display the results for each of the three models below and discuss the results for the corresponding hypothesis after each table. The results for Hypotheses 2 through 4 are shown below in Table 5.6:

Table 5.6

	(1)	(2)	(3)	(4)
	Total SCT	Total SCT	Internal SCT	External SCT
VC Experience - Years	0.013	-0.001	-0.016	0.011
	(0.34)	(0.03)	(0.86)	(0.70)
No. of Rounds Company Rcvd	0.013	0.056	0.036	0.080
	(0.14)	(0.97)	(0.63)	(1.39)
Number of Employees	-0.000	0.002	0.002	0.003
	(0.02)	(1.02)	(0.92)	(1.58)
No. of Firms Invested in Company	0.010	0.001	0.011	-0.044
	(0.15)	(0.04)	(0.33)	(1.22)
VC Total Boards	0.017	0.003	0.010	0.006
	(0.61)	(0.21)	(0.68)	(0.45)
Outcome Event in 2000	0.610	1.127**	1.026**	0.753*
	(0.83)	(2.78)	(2.76)	(2.04)
Outcome Event in 2001 - 2002	-0.043	0.720+	0.780*	0.166
	(0.08)	(1.85)	(2.18)	(0.45)
CEO Outsiderness		-0.348**	-0.309**	-0.264*
		(3.11)	(2.98)	(2.40)
Functional Similarity		-0.399+	-0.393+	-0.453*
		(1.71)	(1.76)	(1.96)
Friendly Index		0.470**	0.447**	0.281**
		(5.06)	(5.15)	(3.40)
Exit Compensation		0.498**	0.365*	0.650**
		(2.79)	(2.23)	(4.07)
Constant	0.864*	-0.884*	-1.057*	-1.333**
	(2.11)	(1.97)	(2.36)	(2.91)
Observations	81	81	81	81

Absolute value of z statistics in parentheses
+ significant at 10%; * significant at 5%; ** significant at 1%

5.6: Negative Binomial Regression Models with Total SCT, Internal SCT, and External SCT as the Dependent Variables.

From the results in Table 5.6 above it appears that there is evidence to support Hypothesis 2a. In model 2, the variable friendly (as described previously in Chapter 4) is significant at the .001 level and the coefficient is positive suggesting that the friendlier the transition, the more likely the firm was to engage in multiple actions in order to transfer important social capital resources. Model 2 also displays similar findings for Hypothesis 2b that indicated whether or not the founder was offered any monetary compensation as part of the exit agreement in order to ensure a smooth transition. This variable is also positive and significant confirming that the friendlier the exit terms, the more likely a firm will be to engage in more social capital transfer actions. I also included the outsiderness and functional dissimilarity variables and, as can be seen, outsiderness was negative and significant (at the .01 level) and functional dissimilarity was positive and marginally significant (at the .10 level). Since the dependent variable combined both the actions directed at capturing both internal and external social capital, this is not a direct test of Hypotheses 3 and 4 but it foreshadows what I expect to see.

From the results of Model 3 shown in Table 5.6, there is sufficient evidence to support the argument that the greater the degree of outsiderness, the less likely the firm will be to engage in actions to transfer a Founder-CEO's internal social capital. The outsiderness variable was both significant (.01 level) and negative. Thus, Hypothesis 2a is supported. As might be expected, the two friendliness variables were positive and significant, suggesting they are important factors in the transfer of internal social capital. Functional similarity was not significant.

Hypothesis 4 argued that the greater the functional background similarity of the incoming CEO, the less likely the firm will be to take actions to retain the Founder-CEO's external social capital. The results in Table 5.6 provide evidence to show just that. Namely, that if the incoming CEO's functional background is dissimilar to the Founder-CEO's functional background, then the company is more likely to engage in actions that seek to transfer the Founder-CEO's external social capital. This result is statistically significant at the .05 level whereas this variable was not significant in the internal social capital analysis. This suggests that functional dissimilarity matters more for external social capital than for internal social capital. Outsiderness is highly significant and negative and the two friendliness variables were highly significant and positive in line with the results of the first two models. Overall, Hypotheses 2a & 2b, 3, and 4 all appear to be fully supported.

5.5 Post Hoc Analysis

For the reader's convenience, I am including a portion of my post hoc analysis. I do this to demonstrate the robustness of the results presented above. The first set to be displayed is the set of results from the three-stage least squares regression mentioned in Chapter 4. While this model failed the Sargan-Hansen over-identification tests, I provide the results to demonstrate how the basic relationships among variables do not change even when I include a number of predictor variables for the occurrence of founder transitions. These results can be seen in Table 5.7 below:

Table 5.7

	(1)	(2)	(3)
	Had Founder Transition	Total SCT(sqr)	Firm Performanc
VC Total Transitions	-0.005		
	(1.52)		
No. of Rounds	0.039		
	(0.83)		
Seeking Funding	0.166+		
	(1.65)		
Looking to Exit	0.192+		
	(1.83)		
VC-Founder Prior History	-0.031		
	(0.34)		
Assessment of Past Firm Performance	0.130**		
	(3.83)		
Had Founder Transition		-4.054**	0.347
		(11.12)	(1.18)
Functional Similarity		-0.553**	
		(2.65)	
Friendly Index		0.574**	
		(5.87)	
CEO Outsiderness		-0.435**	
		(3.44)	
Exit Compensation		0.876**	
		(3.89)	
VC Experience - Years		0.012	
		(1.09)	
Total SCT			0.063*
			(2.25)
VC Total Boards			-0.013
			(1.62)
No. of Firms Invested in Company			0.055+
			(1.80)
VC Dummy			0.381
			(1.33)
Constant	0.291**	3.347**	0.118
	(3.87)	(12.40)	(0.39)
Observations	125	125	125
Absolute value of z statistics in parentheses			
+ significant at 10%; * significant at 5%; ** significant at 1%			

5.7: Three-stage Least Squares Regression Results with Founder Transition, Total SCT and Firm Performance as Dependent Variables

Model 1 has founder transition as its dependent variable. Of the predictors included in this stage of the regression model, three have some significance. Two of them, Seeking Funding and Looking to Exit, are marginally significant and positive. These results are in line with the accepted logic in the VC world that, when seeking for a new round of funding or looking to sell, it is often necessary to "dress up" the company and one aspect of that may include bringing in new management. The fact that these two variables are significant provides some assurance that the results match other real-world observations and studies. The third variable, Assessment of Past Firm Performance, is significant and positive. This suggests that the firms whose Founder-CEOs are performing well are more likely to replace the Founder-CEOs than those that are performing poorly. This is at odds with a large portion of the succession literature discussed previously that argued that poor performance leads to executive succession (e.g Huson, Malatesta, and Parrino, 2004; Cannella and Lubatkin, 1993; Boeker, 1992) but is in line with the "paradox of success" idea put forward by Wasserman (2003). Given that Wasserman's study examined a similar population to the one I am studying, it is again reassuring to find results similar to those of previous studies.

Model 2 in Table 5.7 is similar to the first stage of the two-stage least squares regression run previously as well as the negative binomial regressions. In fact, the results from Table 5.6 Model 2 are very similar to the results in Table 5.7. The four predictor variables for SCT are all significant and in the appropriate directions. Again, this serves to provide additional assurances of the results obtained previously. Finally, in Model 3 we have similar results to those displayed in Model 1 of Table 5.3 above, which reports on the results of the second-stage of the two-stage least squares testing Hypothesis 1a.

The results are once again in line with the previous findings, providing additional evidence of their robustness.

The next table contains the results of a number of regressions that separate the social capital transfer variable into more refined categories to ensure that the results I am seeing are not the result of any one particular action. These results can be seen in Table 5.8 below:

Table 5.8

	(1)	(2)	(3)
	Firm Performance - Internal	Firm Performance - External	Firm Performance - Internal and Extern
Had Founder Transition	0.092	-0.070	0.103
	(0.31)	(0.25)	(0.32)
No. of Rounds Company Rcvd	-0.030	-0.046	-0.052
	(0.47)	(0.67)	(0.75)
No. of Firms Invested in Company	0.080+	0.087+	0.089+
	(1.81)	(1.95)	(1.97)
Number of Employees	-0.002	-0.002	-0.002
	(0.74)	(0.79)	(0.76)
Had Founder CEO	0.395	0.490	0.405
	(0.93)	(1.15)	(0.94)
VC Total Boards	-0.014	-0.013	-0.014
	(1.65)	(1.52)	(1.61)
VC Dummy	0.452	0.359	0.428
	(1.51)	(1.21)	(1.40)
IndBrgSCTM	-0.125	0.096	-0.311
	(0.89)	(0.63)	(1.14)
IndBondSCTM	0.335*	0.196	0.264
	(2.01)	(0.75)	(0.46)
OrgBrgSCTM	0.042	0.090	0.035
	(0.23)	(0.41)	(0.62)
OrgBondSCTM	-0.001	0.130	-0.034
	(0.01)	(0.31)	(0.11)
Constant	0.065	0.171	0.073
	(0.13)	(0.34)	(0.14)
Observations	125	125	125
R-squared	0.11	0.09	0.13
Absolute value of t statistics in parentheses			
+ significant at 10%; * significant at 5%; ** significant at 1%			

5.8: Regressions with Refined SCT Action Categories as Predictors of Firm Performance.

Each of these models contain regressions similar to the second stage of the 2SLS models discussed previously, except that Model 1 only includes the refined categories for internal SCT actions, Model 2 only includes those for external SCT actions, and Model 3 incorporates both. Overall, it does not appear that any one category is more important than another across the three models. This helps to illustrate that my previous findings are not the result of one particular action taken by firms who end up performing better. Rather, it suggests that it is the combination of these actions that have a positive effect on the firms going forward.

The last results that I will display in this section are the inter-rater reliability results. These results were obtained by using the 10% of respondents that had answered a survey for the same company as someone who had already answered for that company. The results can be seen in Table 5.9 below.

Table 5.9

Model Construct	Observed Agreement	Expected Agreement	Kappa Coefficient	Z Statistic
Founder Transition (Y/N)	100%	68%	1.00	3.16*
Internal SC Transfer	60%	18%	.51	3.54*
External SC Transfer	60%	26%	.46	2.69*
Monetary Compensation	70%	60%	.25	.98
Voluntariness of Trans	70%	23%	.61	4.24*
Involvement in Hiring	70%	21%	.62	4.03*
Friendliness Assessment	80%	25%	.73	4.26*
New Venture Experience	80%	34%	.69	3.36*
SCEO Tenure	100%	42%	1.00	4.83*
SCEO Functional Back	80%	27%	.72	4.10*

5.9: Results from the Inter-rater Reliability Tests

From the Table above, the variables appear to have great to excellent agreement which adds some additional support that the results should be reliable, regardless of whether a venture capitalist, Founder-CEO, successor CEO, or some other respondent answered the survey.

Chapter 6

From Founders to Firms: Discussion and Conclusion

6.1 Discussion

This project set out to test the idea that social capital can be transferred from one level of analysis to another—or more specifically, from an individual to an organization. Chapters 1 and 2 theoretically introduce and develop this idea. Chapters 3 and 4 argue for how I expected to see this idea manifested in a real-world context and introduce the methods of gathering data to test this idea. Chapter 5 provides the actual results of the analysis which offers evidence that confirms the basic idea is sound and empirically valid. In concluding this research, it is important to revisit some of the key findings and discuss their relevance and implications. It is also important to discuss some of the limitations and opportunities for future research.

The most prominent result that brings the most learning in this study is the discovery that actions taken by the firm to institutionalize a founder's social capital have organizational level performance implications. This relationship was alluded to many times in my conversations with practitioners in the early stages of this research. Phrases such as, "replacing founders creates a lot of instability within the company" or "two important issues in any transition are economics and the internal cult," or "there were concerns internally because he would continue to hang out with his buddies that he had hired" were common place and plentiful. All of these comments speak to the often deep and personal relationships that founders have with those inside and outside the organization who have helped make the firm successful up to that point in its history. All of the venture capitalists I spoke with also conveyed a sense of caution that they carried with them into each transition scenario as a result of these delicate and important relationships. While a transition event is never guaranteed to be completely smooth, firms and their investors can take explicit actions that will help to streamline the process. The conversations I held with VCs and the empirical results from this study both clearly show that by taking actions targeted to capture and manage a founder's social capital, a firm increases its likelihood of better performance and survival.

While this finding was expected, it also provided an additional degree of insight that I had not considered. Since I was not able to know which organizations had experienced a founder transition before I sent out the surveys, I included both firms with and firms without transitions in my final sample. While I had expected to find a strong relationship between taking SCT actions and firm performance in firms with transition events, I was not clear how it would matter in the firms that did not experience such an event. My findings suggest that SCT actions affect performance regardless of whether or not a transition event occurs. After reflecting on these results together with the interviews I carried out, I realized that even when a founder maintains his/her prominent position at the top, the need to institutionalize the founder's personal social capital persists for the firm. One venture capitalist commented that in order for a founder to continue to sit at the top, (s)he "needs to be humble and adaptable in order to grow and change with the needs of a maturing organization." [needs citation] While personal social relationships are instrumental in getting the young venture started and in moving it forward, as the venture grows these relationships need to mature and evolve into institutional ties rather than just personal linkages. The fact that an organization does not experience a change in its top management does not mean that its top management doesn't need to change. In fact, my results indicate that the social capital of the TMT must be institutionalized to some degree in order to ensure that the organization is able to continue on through the next developmental stages of its lifecycle (i.e. acquisition, IPO, additional funding/growth, etc.).

Having discovered the critical role that SCT plays in new ventures, the other findings (in terms of what allows a firm to undertake SCT) become increasingly important as well. The three major constructs of interest—CEO outsiderness, functional similarity, and exit terms—were all shown to be important predictors of a firm's ability to undertake the SCT actions. All three of the variables assume a transition event , which is reflected in my. The negative binomial regression models included only those observations where a transition event occurred, as it didn't make sense to include the others. When I ran the models on the entire sample with the inclusion of the founder transition variable as a control, the basic results did not change (from those displayed in Model 2 of Table 5.6) but the founder transition was negative and highly significant (.001). This suggests that the occurrence of a transition could serve to harm a firm's ability to engage in SCT actions as argued in Chapter 3. Specifically, CEO outsiderness and functional similarity negatively impact the likelihood that the firm can take SCT actions beyond just the disruptive occurrence of the event itself. However, the exit terms—friendliness and offering monetary compensation to step down—appear to offset the negative effects of the transition event and those of the other two variables. All of this provides us with new knowledge of how succession events might affect young organizations. These results also provide some prescriptions for what actions organizational leaders can take to overcome the potentially adverse effects of [transition events?].

The results presented in Chapter 5 produced a surprising finding, however. The occurrence of a founder transition did not interact with the use of SCT mechanisms to affect performance or survival. I had previously argued that there is some inconsistency in the succession literature in regards to the succession-performance link. This inconsistency was identified as a potential gap. I had anticipated filling part of this gap if the results were able to show that the use of SCT mechanisms acted as a contingent factor explaining some of the inconsistency of this relationship. Unfortunately, this was not borne out by the results. In spite of this, I think a more important result emerged. Since my sample included firms that had experienced a transition (about 60%) and those that had not, I was able to assess the effect of using SCT actions for those firms that did and for those that did not have a transition. The results illustrated that, regardless of whether a transition occurred, use of SCT actions affect a firm's performance and survival. Therefore, while I did not find an effect for the interaction of SCT mechanisms and founder transitions, I did find that SCT tactics do matter. Ergo, the conclusion can be made that engaging SCT tactics will lead to higher performance in new firms regardless of whether a succession follows. In one sense, therefore, the original notion that the use of SCT actions will reduce any negative effects from a Founder-CEO transition are verified since the use of SCT mechanisms leads in [every?] case to improved performance. The bonus here is that using SCT tactics also helps in firms where no

Founder-CEO transition occurs, which reveals that the use of SCT actions is a more important determinant of ongoing performance or survival than is the transitioning of a Founder-CEO as I have discussed previously. Succession events also were shown to matter in terms of a firm's ability to undertake SCT actions. Succession therefore might affect organizational performance differently than I had originally anticipated. This is an important variable and the exact nature of its relationship needs to be understood in much more depth. Future studies could provide additional insight into the relationships that have been discussed already in terms of these succession events and thereby help to clarify the role of transitions and the use of SCT in influencing an organization's performance and survival.

6.1.1 Future Research and Limitations

Social capital has been argued to be a great theoretical construct, but it has been difficult to measure (Woolcock and Narayan, 2000). Some of the difficulty that has arisen may stem from the diverse definitions that have been posited for the concept. My approach to capturing this variable breaks a bit from the traditional models as I sought to capture not social capital itself, but rather its transfer from an individual to an organization. While I believe the method and construction of this new variable are justified for my study, I do think future work could capitalize on using more traditional ways of measuring social capital in addition to my method of capturing its transfer. For example, a commonly used measure is membership in formal and informal associations or networks (Kraatz, 1998). Actors who belong to certain associations and/or networks can often leverage those memberships to discover and mobilize resources that could be useful to themselves personally as well as to the organizations to which they belong. Scholars could gather association and membership data for top managers across a number of firms within an industry and track those relationships across time. This approach would allow researchers to explore a number of different questions. For example, does access to certain networks and associations privilege some firms over others who lack this access? If yes, is the organization at risk of losing that access if it loses a key employee who mediates those ties? If so, what has (or hasn't) the organization done to transfer those ties away from the individual so that they can be maintained independently of the individual member? All of these questions can be tested by tracking TMT network and association memberships over time as well as by gathering data about TMT movement, compensation, and equity investments.

A second approach would be for scholars to use a survey instrument to capture network measures and to calculate the number of bridging and bonding relationships an actor possesses. This data would allow scholars to investigate not only how actors maintain a portfolio of both types of relationships, but it would also be extremely beneficial in monitoring how these relationships are (or are not) transferred when the actor exits the organization. Looking at how these transition events unfold over time would allow researchers to empirically test the proposed mechanisms above in light of the organizational and industry context.

The models presented in this dissertation, while useful, are limited in that they seek to explain mechanisms that relate to the specific phenomenon of social capital transfer. Future research needs to develop additional theories and models that help to address the micro-macro problems in the current literature. Ideally, these theories and models would provide more integrative frameworks for the wide range of subjects that have been examined previously but without integration by social capital theorists.

6.1.2 Implications for Academics

Beyond the broad implications for academics outlined previously, this study provides management scholars with a new approach to constructing multi-level theories. Prior research has tended to use aggregation or other tactics that make problematic assumptions. The current approach recognizes the role of human agents in organizational phenomena and seeks to explain collective behavior as stemming from the actions of the individual members. In this manner, a number of our current notions about organizational behavior could benefit from revisiting old anthropomorphized models. The old models would likewise benefit as the current research would breathe new life into them by factoring in individual agents (Felin & Foss, 2005).

One such area that should be explored further is the "individualization" of organizational social capital. This project has argued that an organization should seek to institutionalize important social capital from an individual member it risks losing. Conversely, it is often the case that individuals are able to transfer organizational social capital in such a way as to individualize or make it their own so that if they were to leave their firm, they would still retain access to these important social resources. Such an idea needs to be further developed and tested. I seek to develop this idea theoretically in Chapter 2 of this project, but I did not set up or conduct and an empirical examination of the concept. Individualization is similar in some sense to institutionalization but is also quite different in the means and tactics used to transfer the social capital from the organization. An empirical examination would be an important extension of this research and would doubtless provide further clarification and insight into the notion of social capital transfer.

6.1.3 Implications for Practitioners

The implications for practitioners appear to be both notable and timely. Increasingly, organizations are relying on partnerships and other inter-organizational relationships to remain competitive. Many of these organizational-level ties were or are mediated by members within the boundaries of the firm. The results of this study suggest not only that these mediated ties *can* be institutionalized independent of a succession event, but that they *should* be in order to ensure positive operating performance. This dissertation also identifies a few important factors that can enhance or detract from a firm's ability to institutionalize important social capital. If the successor CEO is seen as being more of an "outsider" (no new venture or organizational experience) the firm is less likely to be able to take necessary actions to ensure positive performance. This can be easily remedied by either bringing the new CEO into the organization before he or she takes the helm and/or by seeking a successor with new venture experience. Similarly, I found that bringing in a functionally similar successor CEO also made it less likely that a firm would be able to engage in SCT, thereby squelching opportunities to positively affect the firm's future performance. VCs should seek successor CEOs who are functionally dissimilar and who are more likely to engage in SCT tactics.

The terms of exit of the Founder-CEO are another finding from this study that can easily be incorporated into practice. First, it is important to ensure that the founder is able to save face in this process. Involving the founder in the decision to step down and in finding his or her replacement are two practical ways to enable the founder to leave with dignity. From my conversations, it seems as though many veteran venture capitalists meaningfully employed such practices, but this was not necessarily the case among the younger VCs. Ensuring that the founder perceives a friendly exit is one practice that can serve to help the organization in its continued struggle to perform and survive. Offering appropriate monetary compensation packages can also help to ease the founder's transition from his/her post. Obviously, being too generous can lead to financial concerns for the organization going forward, but striking the right balance appears to greatly improve the firm's ability to institutionalize important social capital and thereby promise better future performance and survival.

By examining the models in this study further, practitioners can improve their ability to facilitate social capital transfers when an exit is imminent. This project also will help practitioners to facilitate social capital transfer even when an exit is <u>not</u> imminent The mechanisms proposed, however, may be more or less useful given different environmental or industry conditions. More research needs to be done to identify how certain characteristics of an environment or situation affect the utility of a particular mechanism being employed to facilitate a social capital transfer. Such work promises to provide substantial practical benefit to the large body of practitioners who would are involved in these transitions.

6.2 Conclusion

This project develops a conceptual and theoretical approach to understanding how an individual's social capital might be transferred across levels of analysis (specifically from the individual to an organization) and then empirically tests for it. In doing so, this study makes a number of theoretical and empirical contributions. First, it provides new insights that contribute to the social capital and embeddedness literatures by providing a process-oriented framework for a phenomenon that has received scant attention in either the content-based or process-based literatures. Recently, Oh and colleagues (2006) recognized the role that past relationships (or lack thereof) and former members can play in adding to or diminishing a group's social capital resources. What was not present in this discussion of past relationships was how or if these social resources can be held or controlled at the organizational level. The model presented in this study attempts to provide such answers and, in the process, introduces the concept of social capital transfer to the literature.

Second, this project contributes to the network literature by illustrating how a focus on key mechanisms can help us understand the interaction between individual and organizational levels of analysis. This micro-macro problem is much debated and not easily resolved. Through this study, I seek to demonstrate one approach to a specific phenomenon that accounts for both individual and organizational level constructs and also for the interaction between them. I also empirically test for the effects of this interaction, namely, the institutionalization of a founder's social capital. The theoretical motivations and empirical tests of these mechanisms provide fertile ground for further research in this domain in order to more clearly specify the relationships among these important factors.

This research also contributes to the upper echelons literature. First, it explores the effects of succession in early-stage firms. Most of the research in the upper echelons—and more specifically, succession—has focused on later-stage firms. Examining succession in a new venture setting promises to yield additional insights that have not been discovered through past empirical examinations in later-stage contexts. As noted earlier, a founder's relationships are extremely important for the survival of new ventures, as they contribute a great deal of the firm's initial social capital (Bamford, Bruton, and Hinson, 2006). This alone serves to differentiate succession in early- versus late-stage companies. While some research has started to examine this topic in new ventures (e.g. Hofer and Charan, 1982; Wassermann, 2003; Haveman and Khaire, 2004) there is much to be discovered. This study examines the ability of a firm to transfer a founder's social capital as well as how that ability influences the firm's ongoing performance and likelihood of survival. One important insight that this analysis reveals is the direct effect taking actions to transfer social capital has on the firm's performance. This alone increases our understanding of how a successful succession ought to be carried out in a new venture.

Finally, this study also contributes to the succession literature by looking at "outsiderness" versus just making the inside-outside distinction. I find that outsiderness does inhibit a successor CEO in his ability to use SCT mechanisms. To my knowledge, this is the first empirical test of outsiderness in a new ventures context. While this project has contributed in many ways, there are still some limitations that provide opportunities for future research.

At its broadest level, this dissertation seeks to enhance our understanding of how social mechanisms influence economic organization. The concept of social capital has been explored at both the individual and organizational levels in order to better understand how the two are related and how they each influence the future health and survival of an organization. The models in this study provide not only a basis for understanding how individual social capital can be transferred from one level to another, but also they also provide some prescriptions regarding how to think about succession and compensation. This study's models further offer a wide range of corporate tools to help secure important resource relationships. Most importantly, this research promises to provide new insights into multi-level theorizing that can aid future research in proposing more dynamic and process-oriented models.

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Appendix A

Survey Instrument and Emails

A.1 Survey

Opening Page:

You have been identified as being a/the past or present of (Role in Company). Please answer the following questions in regards to your experience with (company name) . This survey should take no longer than 3 to 5 minutes.

Please select one of the following positions that best describes your role/involvement at (company name).

Venture Capitalist/Board member
Other Board Member
Founder/Founder-CEO
CEO (Non-founder)
TMT Member

Venture Capitalist Background

Please answer the following questions concerning your background:

How many years experience do you have in venture capital?

How many boards have you sat on as a venture capitalist?

How many boards do you typically sit on concurrently?

How many founder transitions have you been involved with?

What is your gender?

Male
Female

What is your approximate age?

20 to 24
25 to 34

35 to 44
45 to 54
55 to 64
65 years and over

What are your educational attainments? Please check all that apply:
High School / GED
Some College
4-year College Degree
MBA
Master's Degree - Other than Business
Doctoral Degree
Professional Degree (JD, MD)
CFA

Transition

Was a founder of also the CEO of the company at some point in time?
Yes No

Did ever experience a transition in management from its Founder-CEO to another CEO?
Yes No

If so, what was the approximate year of the transition?

Professionalization

Which of the following actions were taken with respect to key employee relationships in order to professionalize the firm? Check all that apply

- Face-to-face formal (work-related) meetings with key employee(s) by the CEO
- Face-to-face informal (non work-related) meetings with key employee(s) by the CEO
- Creation of new positions to manage employee relationships
- Increased compensations for key employees in the organization
- Offering of retention bonuses for key employees in the organization
- Promotion of key employees within the company
- Formalization of HR practices and policies
- Other actions which you consider important for the professionalization of a young start up.

Which of the following actions were taken with respect to key external (i.e. customer, supplier...etc) relationships in order to professionalize the firm? Check all that apply

- Face-to-face formal (work-related) meetings with supplier/customer(s) by the CEO
- Face-to-face informal (non-work related, such as breakfasts, dinners, golf outings, etc.) meetings with supplier/customer(s) by the CEO

- Creation of formal position to manage supplier/customer relationships
- Promotion of current organization member to act as a liaison to the supplier/customer
- Equity investments in partner/supplier
- Allowing partner/supplier to have an equity position in the firm
- Other actions which you consider important for the professionalization of a young startup

Please describe the 3 most important considerations when seeking to professionalize and how you have gone about accomplishing/overcoming them.

Successor-CEO Background

Please answer the following questions in regards to the CEO who succeeded the Founder-CEO as part of the management transition.

How long was the successor with the new venture before the transition occurred?
Took Over Immediately 3-11 months 1 - 2 years 3 - 4 years 5 + years

What is the primary functional background of the successor?
IT SALES/MKT MGMT LOGISTICS LEGAL R&D/TECHNOLOGY FINANCE /ACCT

Did the incoming CEO have prior experience as a CEO?
Yes No If yes, was any of this prior CEO experience at a start-up? YES or NO

How many years experience did the successor have in running a new venture?
0 1 – 2 yrs 3 – 4 yrs 5 – 6 yrs 7 – 8 yrs 9 – 10 yrs 11 + yrs

Did the company use an interim CEO before hiring the Founder-CEO’s successor?
Yes
No

What is the Successor-CEO's gender?
Male
Female

What was Successor-CEO's approximate age at the time of the transition?
20 to 24
25 to 34
35 to 44
45 to 54
55 to 64
65 years and over

Other Board Member

Please answer the following questions concerning your background:
How many years experience do you have as a Board Member?

How many boards have you sat on?

How many boards do you typically sit on concurrently?

How many founder transitions have you been involved with?

What is your gender?
Male
Female

What is your approximate age?
20 to 24
25 to 34
35 to 44
45 to 54
55 to 64
65 years and over

What are your educational attainments? Please check all that apply:
High School / GED
Some College
4-year College Degree
MBA
Master's Degree - Other than Business
Doctoral Degree
Professional Degree (JD, MD)
CFA

Successor-CEO Background II

How long were you with the new venture before the transition occurred?
Took Over Immediately 3-11 months 1 - 2 years 3 - 4 years 5 + years

What is your functional background?
IT SALES/MKT MGMT LOGISTICS LEGAL R&D/TECHNOLOGY FINANCE /ACCT

Did you have prior experience as a CEO?
Yes No If yes, was any of this prior CEO experience at a start-up? YES or NO

How many years experience did you have in running a new venture?
0 1 – 2 yrs 3 – 4 yrs 5 – 6 yrs 7 – 8 yrs 9 – 10 yrs 11 + yrs

Did the company use an interim CEO before you were hired?
Yes
No

What is your gender?
Male
Female

What is your approximate age?
20 to 24
25 to 34
35 to 44
45 to 54
55 to 64
65 years and over

What are your educational attainments? Please check all that apply:
High School / GED
Some College
4-year College Degree
MBA
Master's Degree - Other than Business
Doctoral Degree
Professional Degree (JD, MD)
CFA

Founder-CEO Background II

Which of the following best describes your functional background?
IT SALES/MKT MGMT LOGISTICS LEGAL R&D/TECHNOLOGY FINANCE /ACCT

Had you previously started other companies?
Yes No If YES, how many?

Did you work with any of the VCs/Board Members in a previous company?
Yes No

How long had you known the VCs/Board Members?
<1 year 1 – 3 yrs 4 – 6 yrs 7 – 8 yrs 9 + yrs

Had the possibility of hiring another CEO at some point been discussed with you when first seeking venture funding?
Yes No

What is your gender?
Male
Female

What is your approximate age?
20 to 24
25 to 34
35 to 44
45 to 54
55 to 64
65 years and over

What are your educational attainments? Please check all that apply:
High School / GED
Some College
4-year College Degree
MBA
Master's Degree - Other than Business
Doctoral Degree
Professional Degree (JD, MD)
CFA

Transition Event Characteristics Founder

How involved were you in the decision to step down from being CEO?
Extremely involved Very involved Involved Somewhat involved Not involved

How involved were you in selecting your replacement?
Extremely involved Very involved involved Somewhat involved Not involved

Which of the following actions were taken with respect to key employee relationships around the time of your succession? Check all that apply

- Retention of the founder in a different organizational capacity
- Face-to-face formal (work-related) meetings with key employee(s) by the incoming CEO
- Face-to-face informal (non work-related) meetings with key employee(s) by the incoming CEO
- Face-to-face formal (work-related) meetings with key employee(s) by the incoming CEO and founder together
- Face-to-face informal (non work-related) meetings with key employee(s) by the incoming CEO and founder together

- Creation of new positions to manage different employee groups (i.e. VP of Technology, VP of Sales...etc) formerly managed by the Founder-CEO.
- Increased compensations for key employees in the organization
- Offering of retention bonuses for key employees in the organization
- Promotion of key employees within the company
- Formalization of HR practices and policies
- Other actions which you consider important for success

Which of the following actions were taken with respect to key external (i.e. customer, supplier...etc) relationships around the time of your transition? Check all that apply

- Retention of the founder in a different organizational capacity
- Face-to-face formal (work-related) meetings with supplier/customer(s) by the incoming CEO
- Face-to-face informal (non-work related, such as breakfasts, dinners, golf outings, etc.) meetings with supplier/customer(s) by the incoming CEO
- Face-to-face formal (work-related) meetings with supplier/customer(s) by the incoming CEO and founder together
- Face-to-face informal (non-work related) meetings with supplier/customer(s) by the incoming CEO and founder together
- Creation of formal position to manage supplier/customer relationships
- Promotion of current organization member to act as a liaison to the supplier/customer
- Equity investments in partner/supplier
- Allowing partner/supplier to have an equity position in the firm
- Other actions which you consider important for success

Were you offered any compensation incentives for stepping down? Please check all that apply:

- no monetary incentives were offered
- partial liquidity of stock ownership
- full liquidity of stock ownership
- continued employment contract
- continued income without employment obligations
- other

Were you offered any non-monetary incentives for stepping down? Please check all that apply:

- no non-monetary incentives were offered
- senior executive position within the company
- assignment/retention of chairman of the board seat
- public figure/consultant job for the company going forward
- vacation/time off
- other

How amicable was the transition?
Well Above Average Above Average Average Below Average Not very Amicable

New Venture Background

Please answer the following questions in regards to (company name) :
Approximately how many rounds of financing had the company received at the time of transition?

At the time of the transition, how many individuals constituted the company's top management team (i.e. C-level)?

Approximately how many employees worked at the company at the time of the transition?

What were the firm's approximate annual revenues at the time of the transition?

How many total board members were there at the time of the transition?

How many of the board members were venture capitalists?

Was the company seeking another round of financing at the time of transition?
Yes No

Was the company anticipating an exit within one year at the time of transition?
Yes No

Given your expectations for the company, how was it performing at the time of the transition?
Well Above Average Above Average Average Below Average Less than Expected

Transition Event Characteristics

How involved was the founder in the decision to step down from being CEO?
Extremely involved Very involved Involved Somewhat involved Not involved

How involved was the founder in selecting his/her replacement?
Extremely involved Very involved involved Somewhat involved Not involved

Which of the following actions were taken with respect to key employee relationships around the time of the Founder-CEO succession? Check all that apply
- Retention of the founder in a different organizational capacity
- Face-to-face formal (work-related) meetings with key employee(s) by the incoming CEO
- Face-to-face informal (non work-related) meetings with key employee(s) by the incoming CEO

- Face-to-face formal (work-related) meetings with key employee(s) by the incoming CEO and founder together
- Face-to-face informal (non work-related) meetings with key employee(s) by the incoming CEO and founder together
- Creation of new positions to manage different employee groups (i.e. VP of Technology, VP of Sales...etc) formerly managed by the Founder-CEO.
- Increased compensations for key employees in the organization
- Offering of retention bonuses for key employees in the organization
- Promotion of key employees within the company
- Formalization of HR practices and policies
- Other actions which you consider important for success

Which of the following actions were taken with respect to key external (i.e. customer, supplier...etc) relationships around the time of the Founder-CEO transition? Check all that apply

- Retention of the founder in a different organizational capacity
- Face-to-face formal (work-related) meetings with supplier/customer(s) by the incoming CEO
- Face-to-face informal (non-work related, such as breakfasts, dinners, golf outings, etc.) meetings with supplier/customer(s) by the incoming CEO
- Face-to-face formal (work-related) meetings with supplier/customer(s) by the incoming CEO and founder together
- Face-to-face informal (non-work related) meetings with supplier/customer(s) by the incoming CEO and founder together
- Creation of formal position to manage supplier/customer relationships
- Promotion of current organization member to act as a liaison to the supplier/customer
- Equity investments in partner/supplier
- Allowing partner/supplier to have an equity position in the firm
- Other actions which you consider important for success

Was the Founder-CEO offered any compensation incentives for stepping down? Please check all that apply:

- no monetary incentives were offered
- partial liquidity of stock ownership
- full liquidity of stock ownership
- continued employment contract
- continued income without employment obligations
- other

Was the Founder-CEO offered any non-monetary incentives for stepping down? Please check all that apply:

- no non-monetary incentives were offered
- senior executive position within the company
- assignment/retention of chairman of the board seat

- public figure/consultant job for the company going forward
- vacation/time off
- other

In comparison with other transition events you have been involved with, how amicable was the transition?
Well Above Average Above Average Average Below Average Not very Amicable

Founder-CEO Background

Please answer the following questions in regards to the Founder-CEO.

Which of the following best describes the primary functional background of the founder CEO?
IT SALES/MKT MGMT LOGISTICS LEGAL R&D/TECHNOLOGY FINANCE /ACCT

Had the founder previously started other companies?
Yes No If YES, how many?

Did you work with the Founder-CEO in a previous company?
Yes No

Did the founder stay with the company after the transition?
Yes No If so for how long?

How long had you known the founder at the time of transition?
<1 year 1 – 3 yrs 4 – 6 yrs 7 – 8 yrs 9 + yrs

Had the possibility of a transition been discussed with the founder at the time of your firm's first involvement?
Yes No

What is the Founder-CEO's gender?
Male
Female

What was the Founder-CEO's approximate age at the time of the transition?
20 to 24
25 to 34
35 to 44
45 to 54
55 to 64
65 years and over

A.2 Invite Letter (Initial letter sent)

Dear (Name here),

I am writing to **request your participation in a study** that I believe will be of interest to you and others at **(company name here).** It is a study designed to learn more about the specific conditions and processes that contribute to the successful professionalization of a young startup, in particular, the processes involved in the transition of leadership from Founder-CEOs to their successors.

I have already conducted a large number of interviews with founders, professional CEOs, Venture Capitalists, and other senior executives to gather insight into this topic. However, your participation is necessary to confirm my initial findings. Thus, I am asking you to complete the following survey, which **will not take more than 5-7 minutes**:

Follow this link to the Survey:
http://smeal.qualtrics.com/SE?SSID=SS_eDx2PEk13z8axs8&SVID=Prod

All responses will be treated as **strictly confidential**. I am the only person who will have access to any identifying information.

What's in it for you:

Once my data collection is complete I will summarize my findings and distill the best practices used in managing the transition process. I will share these results with all those who completed a survey. I am also happy to speak with anyone individually about the aggregate results and their implications for a young startup and its leadership. Thank you for your help and participation.

Warm Regards,

Bret

About the Researcher:

Bret R. Fund is a PhD Candidate at the Smeal College of Business at Penn State University. He is the author of multiple academic articles examining such topics as how new organizations become central in industry networks and how venture capitalists effectively govern startups. Before pursuing a PhD, Bret worked as a business analyst for a large software company and prior to that he worked as a marketing manager for an internet startup.

~~~~~~~~~~~~~~~~~~~~~~~~~~~~~
Bret R. Fund
PhD. Candidate

Smeal College of Business
Penn State University
418A Business Bldg.
Univeristy Park, PA 16802

Office: (814) 865-6651
Fax: (814) 863-7261
~~~~~~~~~~~~~~~~~~~~~~~~~~~~~~

A.3 Reminder Email

Dear (Name here),

I wanted to send out a final reminder to request your participation in the **Penn State Effective Governance Research Project**. I anticipate closing this survey in about two weeks and would really appreciate your participation. Please keep in mind that although you may or may not *currently* be involved with , **you were involved at a critical time in its development** and therefore your perspective is valuable and needed for this study. Please, if you have just a few minutes (3 to 5), your participation would help to provide the insights necessary to understand more about professionalization and leadership changes in young startups.

Please note if you have already started the survey you will not have to redo the portions you have already completed, but instead will start off where you left off.

I have included the link below and hope that you will lend your valuable insights and perspective.
Follow this link to the Survey:
Follow the link to opt out of future emails:

Warm Regards,

Bret

A.4 Thank you email.

Dear (name here),

I wanted to send a short email to thank you for taking a few moments to answer some questions in regards to your experience with (company name). I believe the time you provided was well spent and I look forward to learning from your experience as well as identifying some best practices that will potentially help you and others going forward in future endeavors similar to the one you reported on.

Once again, your participation was greatly appreciated as I recognize that your time is precious.

Warmest regards,

Bret

BRET R. FUND

EDUCATION AND ACADEMIC EXPERIENCE

Pennsylvania State University, University Park, PA ■ 2008 *(Expected)*
Ph.D. in Management and Organization
Dissertation: "From Founders to Firms: An Examination of the Institutionalization of Founder-CEO Social Capital" (Dissertation Committee Members: Tim Pollock (chair), Don Hambrick, Wenpin Tsai, Forrest Briscoe, and Michelle Lowry (Finance Professor and Outside Member).

Northwestern University, Evanston, IL ■ 2003
Research Fellow at the Kellogg School of Management in the Center for Research on Technology, Innovation, and E-Commerce
Research: "Make, Buy, or Ally? The Social and Economic Basis of Governance Structure in Procurement Relationships"

Brigham Young University, Provo, UT ■ 2002
M.S. in Organizational Behavior
Research: "Towards a Conceptualization of Person-Organization Relationships as Flowing Dialogical Identity Narratives"

Brigham Young University, Provo, UT ■ 2000
B.S. Honors in Business Management: Finance
Areas of Concentration: Finance, Strategy
Honors Thesis: "Value Creation through Corporate Acquisition: Studying the Influences of Transaction Size and Frequency."

PUBLICATIONS & WORKING PAPERS

Fund, B.R., Pollock, T.G., Baker, T. & Wowak, A. 2008. "Who's the New Kid? The Process of Developing Network Centrality and Embeddedness in Venture Capitalist Deal Networks" Advances in Strategic Management, *Forthcoming*.

Pollock, T.G., Baker, T. & Fund, B.R. "Learning to Govern: Venture Capitalists and the Replacement of Founder-CEOs in IPO Firms"

Fund, B.R., Pollock, T.G., Tsai, W. "When Hierarchy is Not Enough: A Multilevel Examination of Social Capital Transfer between Individuals and Organizations" *In preparation for submission to Academy of Management Review*

Fund, B.R. & Gulati, R. "Flocking Together: Examining the Role of Homophily in Economic Exchange Relationships" *In preparation for submission to Academy of Management Journal*

Fund, B.R. & Pollock, T.G. "Hero or Goat? Examining the Interpretation and Consequences of CEOs' Extreme Actions"