KORN FERRY
Institute

When the founder steps down

Leadership transition in a founder-led organisation.

Contents

Introduction

In most organisations, getting the CEO transition right is a complex and often challenging experience for the board. A smooth transition promotes confidence in the new leadership and protects shareholder value. In founder-led organisations, the transition to a non-founder CEO is particularly challenging. Founders are usually deeply attached to the business and a transition to a new leader often signals a profound change in the direction and/or culture of the organisation.

Transitions are most successful when boards, key shareholders, and business founders understand and agree on the drivers for change while acknowledging and honouring the journey of those, including the founder, who has brought the organisation to its current stage. The second CEO in a founder led business will have more chance of succeeding when his or her predecessor, who often remains as a key shareholder or influencer, supports his or her vision for taking the business to the next stage. Conversely, the founder of the business must respect the boundaries of a non-executive position and allow the new leader to take full ownership of the role.

There isn't a manual for transitioning the top job at founder-led organisations. Each business is created differently with the journey to scale often starting with a great idea and entrepreneurs with vast energy and vision. Founders often learn as they grow, eschewing established business models of decision-making until their firms reach a size where more sophisticated business processes are required. A leadership transition from a founder to a non-founder involves complexity that doesn't occur in more traditionally structured businesses. It is an area that deserves more inquiry, particularly in the technology and digital space, where the speed and intensity of market pressures accentuate any faultlines in CEO or leadership succession and transition.

Korn Ferry conducted in depth interviews with 25 key players, including founders, chairpersons, directors, and investors in Australia-based founder-led businesses with employee numbers ranging from under 100 up to 1,000. Our interviewees came from businesses with private, public, private-equity and venture-capital backed ownership structures. We augmented these interviews with additional research and insights from our broader client activity and associated data.

This report, *When the founder steps down—leadership transition in a founder-led organisation*, provides insight into; how to maximise succession transitions within founder-led companies, and those aspects of founder-led organisations that make succession events within such environments a unique leadership challenge.

The organisation at the centre

Managing the founder transition

The underlying transition from founder to non-founder works best when the organisation is placed at the centre of the process, separate from and independent of the founder.

A founder is enmeshed with the fabric and purpose of his or her business, having created the organisation, shaped its culture, and influenced its people. For the founder, the transition of leadership is deeply personal, it also marks a significant change for those who have worked with or around the founder.

Any de-coupling of the founder from the organisation is influenced by the founder's profound impact on culture and the capability of management and staff to manage within a new operating rhythm that initially brings unclear decision rights, escalation points, and adjustments to levels of influence.

While retention through stock or other wealth-creation means remains in effect for identified critical talent, it appears to function as a relatively blunt instrument if used exclusively and without the benefit of a more comprehensive approach to founder transition.

Founder transitions tend to have low visibility and transparency to the organisation. Founder transitions usually centre upon management of the founder and the impact of the transition on them. The impact upon customers and critical staff members closely aligned to the founder must also be considered. In this situation, the transition process can be overly concerned with containment and reaction towards the immediate issues at hand without the necessary balance of the broader implications of the founder's transition from leadership.

A successful transition of the CEO of a founder-led environment requires the impact of the change upon the founder to be secondary (although extremely important) to the needs of the business. The needs of the business are not to be ignored, for they form part of the fabric of the organisation at the time of transition. The structure of the transition should place the organisation's needs at the centre and the legacy factors as peripheral but important considerations. Getting this balance right early, is an essential element of a successful CEO transition.

Founder leader transitions—success factors

CEO and leadership succession is an established point of focus for boards in more traditional corporate settings. The link between leadership succession and shareholder value is clearly understood by boards and therefore the critical importance of succession. Indeed, CEO succession is considered to be one of the most important responsibilities of the chairman and board.

Organisations that are transitioning to a non-founder as leader have similar themes, although the emphasis is noticeably different. Founder involvement creates a somewhat unique blend of circumstances that need to be carefully managed in order to maintain or build future business success.

When approaching leadership transition in founder-led organisations, the following key considerations should be at the forefront of the transition journey. (We note that, quite often, the response to these questions can be somewhat superficial and lacking appropriate due diligence.)

1. What are the key objectives of the business?
2. What type of leader does the business need?
3. What will be the succession approach?

What are the key objectives of the business?

All too often we note the succession discussions within founder-led organisations tend to begin with a few simple questions: Who do we know? Who is available? Who do we trust? While the forward-looking objectives of the organisation are certainly a consideration, they appear to take a back seat. Our interviews and additional research indicate the following approach may help to frame the business imperative that the succession exercise will need to support. The degree of effort required in this exercise should be appropriate to the complexity, maturity and business imperative facing the organisation. This exercise should also be complementary to the broader business and strategic planning activities of the organisation.

1. **Business plan:** Develop a clear, forward-looking view of the business as it relates to potential market opportunities and the key shifts and transitions the organisation will be required to take over the medium term. This could relate to approaches to growth, new markets, products or services, mergers and acquisitions, changes in ownership structure, funding demands, or approaches to market including alternative channels or partners.

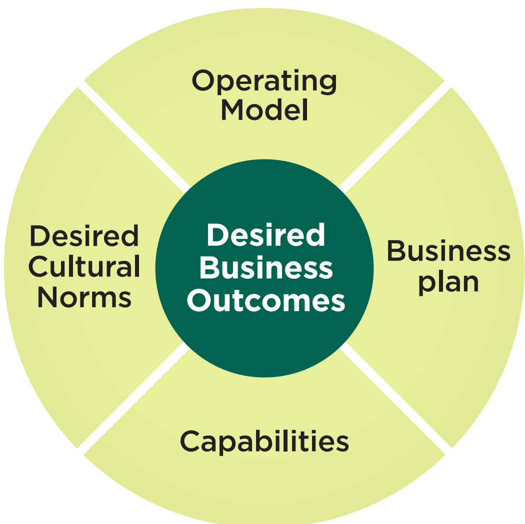
2. **Operating model:** Clearly understand how the business plan will be executed in terms of the operations of the business and how the business will operate in its ecosystem. This will help to inform how the organisation will need to interact across its component parts and with its external stakeholders. Often the changes to operating model can be undervalued when considering how the business will function when the unique environment of the founder as leader is no longer in effect.

3. **Cultural norms:** We noted that where founders had transitioned out of the business, the impact on culture is clearly recognised as inevitable. However, defining what culture would be in the best interest of the business appears less clearly defined. The focus tends to be on trying to remove the things that "we didn't like" rather than determining what is needed and building towards that position.

4. **Capabilities:** Once there is a clear view of the other dimensions, the business is then in a position to define the capabilities the organisation requires to meet the business objectives, allow the operating model to function effectively and within the desired culture of the business.

What type of leader does the business need?

By identifying the desired business outcomes and how they relate to the profile of a leader, those responsible for succession will better understand the drivers for the leader they are seeking. Korn Ferry's Four-Dimensional Executive Assessment (KF4D) has identified the differences in leadership attributes and how to align and measure their relevance to a desired leader profile. This includes exploring the implications for how a person may perform within a given cultural and operating environment. The following KF4D profile of CEOs of innovative technology companies is based on benchmarked data of best-in-class performers world-wide and explores four key dimensions of leadership: experience, competency, traits, and drivers.



What will be the succession approach?

The succession plan captures three key components of the succession journey, ensuring alignment between relevant stakeholders. It needs to answer the following questions:

1. What are the desired business objectives?
2. What leaders are needed to achieve the desired outcome?
3. What are the risks that must be managed (including critical talent, IP protection, and critical dependencies that require careful management)?

Our interview results indicate succession planning within founder-led organisations is largely “unstructured” and “discussed yet unplanned”, and tends to be a reactive activity rather than planned journey” and “overly influenced by the perspectives and implications for the founder”, regardless of the degree of full financial or leadership control the founder may have. The gaps in approach have often resulted in potentially avoidable situations that adversely impact morale, customer satisfaction, innovation, and the performance of the business. In order to reduce the potential negative fallout, our research indicates the succession journey should take the following into consideration.

1. **Remain future-focused while respecting the heritage.** The contributions of the founder, management, and staff should always be respected. Their energy has enabled the entity to lift from concept to substance, shaping the culture and influencing customers and the industry. The executives we interviewed that had followed founders into leadership roles spoke of investing time to unpack the “nuggets of real value” that will support the future development of the organisation. Planning effectively will ensure that the valuable ingredients, which allowed the business to flourish and which will be critical to success, can be articulated and refreshed in alignment with future strategy.

2. **Clearly define the future role of the founder.** A crucial element for all stakeholders involves defining the founder’s future role. All non-founders we interviewed recognise that the ongoing involvement of the founder can be extremely valuable as a source of continuity to the business. The value extends to customers who appreciate continued access to the founder. It also extends to staff who feel loyalty to the founder, and want the qualities and values of the company to continue. Shareholders value continued stewardship and the founder’s deep and insightful knowledge of the business and its ecosystem. The founder can continue to bring unique insight and value to the organisation and its stakeholders through possible involvement with R&D, marketing, brand initiatives, or other important activities. These positive effects can create a negative impact on the business if the rules of engagement and channeling of founder effort is poorly defined, or the founder lacks the personal discipline to adhere to agreed involvement.

3. **Objectivity and data to inform decisions.** A major consideration of many stakeholders we interviewed is the need for greater objectivity when dealing with founder transition and post-founder leadership appointments. The tendency towards more casual and “gut feel” –based appointments with a strong leaning towards what’s worked in the past will fit the culture tends to outweigh the importance of focusing ahead and looking to what will be needed. The succession time can be an important period of reenergizing and reinvigorating. The ability to objectively hold a mirror up to the business and its leadership and operational norms is seen widely by stakeholders as a valuable and insightful exercise if approached properly and not with strong political bias. Positioning the future while respecting the heritage in an objective manner is key.

4. **Recognise succession is a change/transformation–management exercise.** The impact of succession goes well beyond the founder and the successor CEO. The impact of change will likely reverberate across the culture, operations, people, and practices of the business, particularly when there is a significant shift from informal management style towards more visible, structured processes. We find succession reviews tend to underestimate the interoperability of the various activities and functions of the business and the impact of culture and interpersonal motivation (beyond a few key staff). The founder transition appears to focus too heavily upon the founder's perspective and those that have been staunch loyalists of the founder, such as key product and customer-facing executives. Others in the business may receive less attention as may often be the case for the relevant support functions. Often, it is in these areas that transitions become most difficult, given shifts in decision rights, authority, influence, and expectations may vary greatly from founder-led to non-founder situations.

5. **Clearly define the cultural and business norms to keep and those to develop.** Undertake a clear diagnostic of the culture of the organisation. Recognise and agree upon those norms that represent the strengths and values of the founder that will align and support the future strategy of the business. Remove or de-emphasise those cultural elements that do not support the strategy and seek to define those elements to be developed moving forward.

6. **Build a succession bench through the organisation and in support of critical roles.** Succession is a journey of alignment of the needs of the business with the organisation's capacity to meet those needs. All too often, transitions from founder to non-founder as leader become events that occur in unplanned fashion, in response to situations that are either unforeseen, unplanned, or have some degree of urgency. We note from our research the early indicators for succession are often visible for some time; however the motivation and recognised value of advance planning was lacking or simply not evident. Lip service and convenient compromises seemed to be all too often evident. This is avoidable.

7. **Put the organisation at the centre.** While respecting the needs and sensitivities of the founder, the business must be at the centre of the leadership transition approach and execution. Too often we find the business is in the centre at the outset of planning, but the vast majority of execution effort, and therefore attention, tends to be in response to the founder's behavior and activities, modifying the transition effort and focus. Create a situation where the transition becomes evolutionary rather than revolutionary. Leveraging the future focus of the exercise, enables communication and execution to align with the objectives that will shape the next phase of the business, allowing decisions to be anchored to that horizon and reducing the focus on "how we did it in the past."

The founder as leader—a unique transition environment

While many of the most successful founder-led technology companies have humble beginnings, their development was often overseen by visionary founders whose leadership has been or continues to be deep and lasting.

A founder's impact and influence is significant in all aspects of business operations and culture. As the business matures and evolves its products or offerings responding to or disrupting market forces—the evolution of the business is more closely aligned to how the founder modifies or adjusts his or her approach, attitudes, and beliefs. The founder sets the culture and remains its greatest influencer. The direct connection between the leader and the culture of the organisation is most profound in founder-led organisations as compared to more established corporate structures.

Korn Ferry examined the leadership impact of founders in three key areas: their motivation, their role, and their characteristics and traits. Our analysis reflects the views of our interviewees and additional analysis of the trends that surfaced from these discussions.

Motivation of the founder

Founders often have one of three motivations to start a business.

- **The product imperative:** Some founders feel intensely about a product or solution and its applicability in the market. He or she has a strong focus on quality and points of differentiation coupled with a desire to demonstrate and maintain innovative difference.

- **The domain expert:** Other founders are experts in the market space in which they operate, with deep knowledge of the products or services, the customers, and the competitors. These forward-looking people have identified the trends in the industry or aim to reinvigorate existing approaches to addressing needs.

- **The commercial driver:** These founders are motivated from a predominantly financial management perspective. They desire to lead an end-to-end operation while seeking to retain complete control or authority over decisions that link to business purpose and performance.

Interestingly, founders' motivation is rarely fame, fortune, or public recognition. While these aspects appear to surface in varying degrees as the founders' businesses matures and "succeeds", they do not appear to be material at the outset. The desire to do something new, better, interesting, and different, coupled with a desire to "give it a go" were core at the outset.

Role of the founder

One constant role for the founder is the "mission" drive, a steadfast focus on outcomes—with a reduced focus on the processes for getting to the result. There is a clarity of purpose and intent for the business, which allows all stakeholders to be clear about what they need to achieve, although often the question of how to achieve it remains more fluid. This can be an empowering period for staff and managers as they can shape their work habits to balance their interests and preferred approach with the desired outcomes required by the founder.

As the business evolves, however, we note that the founder's role varies along with the perceived value he or she provides the organisation. We explore themes across three broad transitory phases: start-up, early growth, and established presence.

- **Start-up:** At the start-up phase, the founder is often the principal evangelist—passionate and driven, bringing purpose and a sense of vision to the journey ahead. This important role appears to extend for the life of the founder's involvement, although with varying intensity depending upon the performance of the business and the stage of organisational maturity. Also in the start-up phase, the founder has maximum influence and control. He or she is directing all activities and quickly making many short-term decisions. The achievement of milestones serves as proof of success. Founders need tangible results and if something isn't working, they move quickly to alternative options, which tend to evolve from necessity rather a result of planning and analysis through management processes. To those around the founder, this phase brings excitement, optimism, and clarity of purpose, although the approach to achieving the mission may be less defined and/or more open to constant adjustment.

- **Early growth:** As the business develops, the need for management systems and processes increases. The management dynamic shifts and business managers have increased leadership responsibilities. Functions take shape and management and business processes become increasingly important, although often remain poorly defined or fluid. The customer base expands, and points of compromise, the balance of alternatives and the need for more considered decision making, also increase in importance. There are signs that frustration builds for both the founder and staff when informal, intuitive, fluid operating structures and decision–making activities come under pressure due to greater complexity and customer demand.

- **Established presence:** At this point, a business often requires management across cultures, geographies, and dispersed locations. Some businesses may be publicly listed or ownership is spread across multiple shareholders, with the founder not necessarily retaining a controlling interest. The business often has a stronger portfolio of products and services coupled with more diverse customer demands and more sophisticated partnering relationships. In this phase, the founder is perceived to be less accessible and involved, often focused upon key areas of personal and professional interest and generally anchored to his or her core motivations. Our interviews reveal a significant change in focus when the number of employees of the business approached 300 people. Around this time, organisations move from "agile entity to a corporatised organism" that begins to shift from the more "familial" hold of the founder.

While the operating and management systems differ in sophistication and complexity across the observed business phases, the adaptability of the founder to adapt to the changing organisational demands do surface as an important variable. As the business moves through maturity cycles, the founder's characteristics and traits appear to morph from strong assets that underpinned the business to, in many cases, areas requiring constant, active management attention (at all levels) by those around the founder.

Characteristics and traits

Our research reveals several characteristics and traits that dominate many founders. The term "entrepreneurial" appears to function as a catch-all descriptor of the positive and less positive aspects of founders' behaviours. An undertone to "entrepreneurial" in our research centers upon founders being more focused on building and creating and less restricted by the practicalities or limitations, such as the costs, resourcing, and competitive forces, of doing so. The primary characteristics and traits used to describe founders include:

- **Single-minded:** The "mission" drive, outlined previously, has been largely interpreted as single-mindedness. This provides resilience, focus, and courage through the various stages of building a business. Equally, it appears to bring decision-making clearly into focus, helping to avoid distractions that do not support obtaining the desired goals.

- **Decisive:** The "fast decision" is perceived by many to be more instinctive in nature. This factor appears to be due to the deep knowledge the founder develops regarding the product, solution, customer, market, and competitive landscape. Decisions are often made with analysis that may be high level in nature or deeply specific in a narrow area. When combining instinct with decision-making authority, the ability to move through decision processes quickly, and at times in asomewhat informal manner, is a clear distinction in the founder-led environment.

- **Adaptive:** The ability to shift, customise, and reposition in often unstructured or new situations is due to founders' adaptiveness. Their ability to move quickly in situations seen to support the mission or to address a customer–specific situation, is seen as important in taking advantage of opportunities in a manner that is more responsive. In such situations, the perception of the executive team is that the founder may be unpredictable in how he or she may proceed on a particular matter. In some cases, this is interpreted as the founder being opportunistic and creative in approach, with a willingness to adapt quickly.

Unique characteristics of founders

We noted two strong themes—intimacy and career agnostic—that are quite unique to the founder as leader environment that appear to materially impact the way a founder approaches their role and the implications for how they lead and influence within their organisations.

Intimacy: Founders have a strong sense of personal attachment to the business and, unlike more traditional executive leaders in mainstream corporate organisations, the personal and professional dimensions are intimately linked and are somewhat inseparable. This linkage may become more disentangled as the business matures and the interests of the founder adjust to the success of the business, although remain a stronger binding force than we would expect in non-founder-led businesses. This level of intimacy between the founder and their business can make it difficult to disassociate the individual from their mission, as the business is taken to be an extension of the founder (or their family), and therefore decision making comes with a unique and somewhat emotional bias, as does the evaluation of risk.

Career agnostic: Our interviews and broader analysis identified a clear lack of career perspective on the part of founders. Whereas senior executives operating in large corporate structures tend to think of their experiences and results as positioning them for future career advancement, the founder was focused on the mission and journey in the absence of career decisions. As a consequence, career development for management and staff becomes aligned to the mission of the founder and the areas in which the founder is prepared to relax their direct hands-on involvement. Additionally, we find less confining role definitions, more appetite for people to take action on matters beyond their job description. We also see a stronger alignment to informal influences across the organisation, allowing the most interested or motivated people to step up without restriction to their more formal position or role in the business.

- **Risk taking:** The perception of founders as risk takers is quite strong, although it doesn't appear to be overly anchored to financial risk. Combining the mission focus with a faster, more instinctive decision-making cycle can be an important asset to meeting the cycle times necessary for a start-up venture. Founders who rapidly make decisions with imperfect or often instinctive data points may be perceived to lack transparency or context by those they work with. In the absence of this context, there is a sense the founder is taking greater risk. The founders we interviewed were aware of the relevant risks although were more instinctive in making decisions given their deep knowledge of the subject matter or preparedness to support their mission. As the business becomes larger and more complex and sophisticated in its operations, founders' risk appetite tends to change as there is more at stake, and more to lose, personally, professionally, and in terms of responsibility to stakeholders. As a result, a more cautious founder posture begins to appear with the follow-through impact on business operations and culture.

- **Self-reliant:** The founder is consistently viewed as being reliant upon his or her own judgment and instincts when facing key decisions or critical business situations. While founders are often seekers of input and insights when forming their opinions, decisions tend to be based upon their own perspectives. As such, decisions are often viewed as "the founder's" with the burden of responsibility carried by him or her, rather than institutionalised as a learning experience for the organisation and management team.

- **Self-aware:** The majority of founders proved to be aware of their own limitations, although they do not see their limitations as constraints on what they could achieve. Indeed, their mission appears to be to direct purpose and intention, and where new skills and capabilities are required, they have an ability to draw those skills into their orbit.

  In discussions with those who work with founders, however, the issue of situational self-awareness proves to be a common concern. Founders' ability to modify their approach to meet the needs of the audience appears less evident. There is a perception that founders tend to be less situationally aware; rather, they are more driven by the mission and lacking self-discipline when adjusting to change. This is viewed as restrictive.

- **Opportunistic:** Our research reveals that executives within a business where founders have transitioned out (but maintain a strong level of involvement) consistently note the need to carefully manage the founder's involvement in activities. Often, founders are perceived to experience "interest spikes" that can be sharp and sudden, then dissipate abruptly. The founder's involvement can quickly become disruptive or be viewed as interfering with the broader business agenda. The value of founder interest and involvement is perceived to be extremely high where it is aligned with the business agenda, particularly where customer, market–development, or product development activities are in play. During misaligned interest spikes, founders are perceived to create a distraction, inadvertently undermining the operational business leaders by moving organisational resources away from other activities to focus on the spike. While executives note the value of innovation that interest spikes could achieve, often the transition from idea to action (and therefore resource distraction) could be rapid and without due consideration to the disruption this action could cause.

Impact of the founder

The founder's reach in their business is wide and deep. His or her impact and influence in culture, governance, and succession, is more imbedded and ingrained than business leaders in traditional corporate environments.

Culture

Due to the unique intensity of the personal and professional attachment the founder has to the business, the culture of the business becomes an extension of the founder. The core values, behaviours, attributes, and belief systems that develop in the organisation are a reflection of the founder's and there is rarely a planned approach to developing culture at the outset of the venture. It appears to evolve, often through informal means, to become the unstated, although closely adopted norms of the organisation. In some cases, founders approach the business with a sense of guiding principles to shape their own actions and those of others on the journey.

The sense of emotional and personal connectivity has also created a "familial" orientation to the culture. There is a strong sense of shared purpose and respect for the founders, or at least recognition of their status and ultimate decision–making authority. We noted a strong sense of loyalty to the founder, particularly by those that have been part of the early stages of the venture. Indeed, their loyalty seems far more strongly aligned to the founder than to the venture.

As custodian of the culture, the founder's ability to adjust and modify materially impacts the culture. We found many interviewees feel that on the whole, founders over time narrow the culture, and the ability to challenge and question the norms prove difficult as businesses grow and mature. The lack of articulation of the core values of the business makes the development of the culture harder to achieve and makes it difficult for new joiners to the business to understand the values and become integrated to the business. Too much emphasis may be placed on loyalty, which could prevent or disrupt the necessary evolution of the culture. This situation also creates an environment where often an individual's need to be aligned and "in favour" with the founder, is necessary to achieve their personal objectives. In turn, this creates a political layer of influence that may not be overtly visible yet very much in existence and impacting decision-making. Understanding the implications of culture in succession planning is essential.

Governance

Business control, either directly or indirectly, appears to rest with the founder. The decision-making authority on matters of importance tends to filter up to the founder as the single point of accountability. Even in more mature situations where business process, planning, and control systems are in place along with management layers, there appears to be an unwritten, although clear understanding that certain decisions will rely upon the founder.

The potential single point of failure that is inherent in founder-led organisations may not reduce proportionally as the organisation continues to mature. Founders retain authority (directly or through influence) over the business and therefore materially impact the governance structures, which we have found to be predominantly implied rather than clearly stated. Although founders seek input broadly, the level of accountability and responsibility carried by those around the founder is significantly less than would be evident in more traditional corporate structures. As a result, the founders carry a far greater burden; the development opportunity for those around the founders are lessened; and the extent to which the organisation's governance approaches maturity to support more experienced managers/leaders and more sophisticated business control systems/processes is reduced.

There is a perception that the founder is a bottleneck for decision-making, influenced strongly by a trusted few loyalists and, experiencing pressure from an ever-increasing number and breadth of decisions. Interestingly, decision escalations are not always formal or structured, and indeed “passing approval” via informal discussions or “implied agreement” becomes increasingly the norm, allowing for faster decision-making although leading to confusion or uncertainty for those left out of the decision process.

Whether the founder runs, controls, or influences the business, the transition from a single point of authority to shared ownership requires a personal and organisational shift in governance practices and processes.

Succession

Succession considerations appear to be absent in the vast majority of founder-led organisations. Founders are concerned with building and attracting capabilities to the organisation that are specific to the mission or product and service elements of the business. Access to the right talent with the right skills is a constant burden, with trial and error prevalent as a means of eventually getting to a workable outcome. The augmentation of skills is the primary focus. Succession becomes a consideration primarily in the event of retirement or a change in business ownership. In this regard, we note a predominantly reactive posture towards succession, being more of a response rather than a planned or managed event. In many circumstances, where some form of succession plan does exist, it is largely undisciplined in its execution and heavily influenced by the bias of the founder and generally considered to be anchored in the legacy of the organisation rather than possessing a clear lens to the future.

Even where succession is being considered, either for the founder or other critical roles in the organisation, it appears to be subjective and unstructured with poorly defined or ill-considered objectives. Organisational change components are either undervalued or completely missed. As succession–planning events are forward–looking, in situations where structured succession interventions are applied, deficiencies in other areas of the business become increasingly clear, including: organisation design, role clarity, business planning, investment management, product development, market development, governance, and risk management. In these key areas the impact of the founder will have a material impact on the performance of the “second” CEO, the executive team, and wider organisation. Recognising these implications when managing the transition from the founder can be a positive, value–creation initiative for the business and its stakeholders.

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