

6-9-2007

CONFIDENCE IN COOPERATIVE RELATIONS BETWEEN ENTREPRENEURS AND VCS: THE ROLE OF SOCIAL AND FORMAL CONTROL MECHANISMS

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Recommended Citation

Yitshaki, Ronit (2007) "CONFIDENCE IN COOPERATIVE RELATIONS BETWEEN ENTREPRENEURS AND VCS: THE ROLE OF SOCIAL AND FORMAL CONTROL MECHANISMS," *Frontiers of Entrepreneurship Research*: Vol. 27: Iss. 3, Article 3. Available at: <http://digitalknowledge.babson.edu/fer/vol27/iss3/3>

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CONFIDENCE IN COOPERATIVE RELATIONS BETWEEN ENTREPRENEURS AND VCs: THE ROLE OF SOCIAL AND FORMAL CONTROL MECHANISMS

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ABSTRACT

This study examines how VCs' strategic and managerial involvement mediates the relationships between social control mechanisms and entrepreneurs' confidence in VCs' cooperation. Based on data collected from 120 Israeli entrepreneurs, the findings indicate that VCs' strategic involvement is found to be positively associated with entrepreneurs' confidence in VCs' cooperation whereas, VCs' managerial involvement is found to be negatively associated with entrepreneurs' confidence in VCs' cooperation. Specifically, it was found that VCs' *strategic involvement* mediates the positive relationships between shared beliefs and similarities, fairness and justice, entrepreneurs' influence on decision-making and their confidence in VCs' cooperation. VCs' *managerial involvement* mediates the negative relationships between shared beliefs and similarities and entrepreneurs' confidence in VCs' cooperation. However, contrary to the expectations, VCs' managerial involvement does not mediate the relationships between fairness and justice and entrepreneurs' confidence in VCs' cooperation. Furthermore, entrepreneurs' influence on decision-making is found to be positively associated VCs' managerial involvement although this involvement was found to be negatively associated with entrepreneurs' confidence in VCs' cooperation. The contributions and limitations of the study findings are further discussed, providing additional directions for research.

INTRODUCTION

Prior studies examine venture capital investments through two different streams of research. The first stream of research refers to venture capital investments as an economic activity that can be governed hierarchically and best managed by employing cost-effective considerations. Agency theory (Jensen and Meckling, 1976) focuses on explaining agency risk as stemming from the management of internal relations in economic activities and from the agent's adverse selection or inappropriate behavior. In the context of venture capital investments, agency theory emphasizes how VCs should screen and select new investments, as well as how they can best formally govern their relations with entrepreneurs. In contrast, transaction cost economic theory (Williamson, 1991) explains that economic relations between actors in the market are driven by cost-effective considerations. As such, both VCs and entrepreneurs seek to minimize their transaction costs. However, as both hold idiosyncratic knowledge (assets specificity) their ability to minimize transactions costs is limited due to bilateral dependency. Both agency and transaction cost economic perspectives fail to explain VC-entrepreneur relations as cooperative and non-hierarchical. In addition, these perspectives also fail to explain how process and outcome uncertainties impact the ability of each party to preassess transaction costs, as well as how these relations can be best managed based on 'relational self-enforced mechanisms' (Williamson, 1991).

The second stream of research refers to venture capital investments as interorganizational relationships that are based on cooperative relations. Accordingly, the relations between VCs and entrepreneurs are examined by their motivation to cooperate rather than act opportunistically (Cable and Shane, 1997). Recent studies suggest that VCs' and entrepreneurs' relations rely on reciprocal relations rather than formal control mechanisms (Sapienza and Korsgaard, 1996; De Clercq and Sapienza, 2001, Busenitz, Fiet and Moesel, 2004; Weber and Göbel, 2005; De Clercq and Sapienza, 2006). It was further argued that the relational rents of VCs' and entrepreneurs' relations are managed through social control mechanisms such as trust (De Clercq and Sapienza, 2001; De Clercq and Sapienza, 2005). Although highlighting VCs' and entrepreneurs' social exchange and mutual interdependence, these studies provide limited explanation

about how trust relations between the parties are created and how VCs' formal control mechanisms influence their informal relations.

The aim of this study is to examine how entrepreneurs construct their confidence in VCs' cooperation and how entrepreneurs' and VCs' control mechanisms impact entrepreneurs' confidence in these cooperative relations. Following the argument presented by Shepherd and Zacharakis (2001), I argue that VCs and entrepreneurs are managed through formal and informal control mechanisms in order to ensure their cooperative relations. Thus, although trust between VCs and entrepreneurs may increase confidence in cooperative behavior (Shepherd and Zacharakis, 2001; McEvily, Perrone and Zaheer, 2003), social control mechanisms are mediated by VCs' control that is expressed by the scope of their involvement.

This paper contributes to the current literature in two ways. In contrast to other studies, this study focuses on how entrepreneurs construct their confidence in VCs' cooperation and how entrepreneurs' and VCs' control mechanisms impact entrepreneurs' confidence in these cooperative relations. In addition, the study findings have theoretical implications as they suggest that formal and informal control mechanisms jointly affects entrepreneurs' confidence in their VCs' cooperation.

THEORETICAL BACKGROUND

Formal Control Mechanisms

Although venture capitalists (VCs) and entrepreneurs can most benefit from cooperation, they may also consider behaving in an opportunistic way (Cable and Shane, 1997). To maintain their cooperative relations, the relationships between VCs and entrepreneurs are formally established through contractual arrangements that include stipulations and governance mechanisms to control opportunistic behavior (Amit, Glosten and Muller, 1990; Ruhnka and Young, 1991; Amit, Brander and Christoph, 1998). These contracts serve as control mechanisms to ensure consistency between the goals of the two parties and to oversee the agent's actions.

VCs use the board of directors as a governance mechanism (Daily et al, 2002; Amani, Wallace and Fayez, 2002; Williams, Duncan and Ginter, 2006). The portfolio firm's board composition reflects the contractual covenants and provisions (Busenitz, Moesel and Barney, 1997; Smith, 2005). Usually VCs receive extensive control rights that enable them to obtain board control. As such, they "frequently have substantial power over other participants in the startup" (Fried and Ganor 2006, p. 971). Thus, VCs seek to secure a higher proportion of seats on the board to increase their control over strategic decision-making (Sapienza et al, 1996; Smith, 2005; Williams, Duncan and Ginter, 2006). The number of board seats under a VC's control also enables the VC to enforce changes in its portfolio management structure (i.e. the entrepreneur's dismissal) (Rosenstein et al, 1993; Gompers and Lerner, 1996; Busenitz, Moesel and Barney, 1997). For example, it was found that in VC-backed biotechnology and healthcare firms, founders occupied fewer leadership positions than in non-VC-backed firms. These findings suggest that VCs have a clear preference to reduce "the concentration of executive power in the hands of owners and entrepreneurs as a condition for their participation" (Williams, Duncan and Ginter, 2006, p. 310).

From the perspective of agency theory, the involvement of VCs in their portfolio firms serves as an active control mechanism to ensure that entrepreneurs' behavior is aligned with their interests. Studies have shown that VCs add value to their portfolio firms by assisting in financing, formulating business strategy, building managerial teams, serving as sounding boards, managing crises and developing networks (Macmillan, Kulow and Khoylian 1988; Gorman and Sahlman 1989; Gomez-Mejia et al. 1990; Sapienza, Manigart and Vermeir 1996; Morris, Watling and Schindehutte 2000). In fact, most VCs require involvement in strategic decision-making in order to ensure that entrepreneurs act according to their expectations (Floyd and Lane 2000). Thus, VCs use the board as a mechanism for aligning managers' and shareholders' interests "through the monitoring and ratifying of management decisions"

(Hillman, Cannella and Paetzold 2000, p. 237). Moreover, VCs may also use their formal control to ensure cooperation based on coercion (Shepherd and Zacharakis, 2001). In such cases, VCs may consider dismissing entrepreneurs that they perceive as underperforming (Fiet et al. 1997; Bruton, Fried and Hisrich 1997, 2000). When agency risks cannot be resolved by entrepreneur replacement, VCs may choose an exit strategy and defect (Amit, Brander and Christoph 1998; Parhankangas and Landstrom 2003).

VCs' governance on the board means that entrepreneurs usually control a smaller proportion of representation and subsequently have less ability to influence strategic decision-making (Williams, Duncan and Ginter, 2006). In addition, VCs' scope of involvement might also impact on entrepreneurs' ability to influence decision-making. Employing extensive formal control mechanisms by VCs might lead to less motivation among entrepreneurs to cooperate (Chua and Woodward, 1993; Cable and Shane, 1997). It is therefore suggested that VCs' scope of involvement, whether strategic or managerial, mediate the relationship between entrepreneurs' perceptions of social control mechanisms and their confidence in VCs' cooperation.

Social Control Mechanisms

Previous studies have shown that interorganizational relations are embedded in social contexts (Larson, 1992; Uzzi, 1997). The social exchange theory indicates that social relations rely on voluntary behavior that leads to obligatory and reciprocal behavior between the parties. These social relations are based on trust, frequent communication, and perceived procedural justice that embody perceptions, beliefs and attributions of the other party's goodwill, benevolence and integrity (Whitener, et al., 1998). Similarly, it was also argued that interorganizational cooperative relationships are based on trust underlying contractual arrangements. That is "personal relationships can serve to shape and modify the evolving structure of a cooperative interorganizational relationship" (Ring and Van de Ven, 1994, p. 93).

Trust is defined by McEvily, Perrone and Zaheer (2003) as "the willingness to accept vulnerability based on positive expectations about another's intentions and behaviors" (p.92). According to this definition, trust serves as a cognitive heuristic that affects the interaction and coordination patterns between economic actors, as well as their willingness to cooperate and share resources to achieve common goals. As venture capital investments are associated with high levels of process and outcome uncertainties, formal control mechanisms might be difficult to use because both VCs and entrepreneurs possess idiosyncratic knowledge. Accordingly, trust between VCs and entrepreneurs sets up expectations and intentions for cooperative relations (Cable and Shane, 1997). In addition, trust between VCs and entrepreneurs contributes to confidence in cooperation (Shepherd and Zacharakis, 2001), as "trust gives actors the confidence that they will be able to work things out with their counterparts in an equitable and reasonable manner" (McEvily, Perrone and Zaheer, 2003 p.98).

This paper focus on examining three social control aspects that might influence entrepreneurs' confidence in VCs' cooperation: shared beliefs and perceived similarities, perceived fairness and justice and entrepreneurs' influence on decision-making.

Shared Beliefs, Perceived Similarities and Entrepreneurs' Confidence in VCs Cooperation

Social capital theory suggests that knowledge exchange depends on relational factors. Nahapiet and Ghoshal (1998) argue that "an essential part of the social exchange and combination processes [that] require at least some sharing of context between the parties to such exchange" (p.293). Beyond network ties, Nahapiet and Ghoshal suggest two other factors that influence social exchange. The first refers to cognitive dimensions such as shared language, vocabulary and collective narratives; the second refers to relational dimensions such as trust, shared norms and obligations, in addition to commitment, factors that enable the parties to construct expectations and identify with reference groups (Levin, Whitener and

Cross, 2006; Tsai and Ghoshal, 1998). The association between shared perspectives and trust is found to be higher in relations that are managed over time (old relations) (Levin, Whitener and Cross, 2006).

When considering new investments, VCs pay much attention to interpersonal chemistry between themselves and entrepreneurs (DiMaggion, 1992; Nohria, 1992). In addition, VC decision-making is also influenced by assessing similarities with entrepreneurs as a criterion for making new investments (Shepherd and Zacharakis, 2001; Franke et al, 2006). Perceived similarities thus contribute to the creation of trust and cooperative relations (Das and Teng, 1998) because they set up expectations about behaviors and intentions (McEvily, Perrone and Zaheer, 2003).

Consistent with the above literature, shared beliefs and perceived similarities between entrepreneurs and VCs contribute to the creation of trust relations and to entrepreneurs' confidence in VCs' cooperative behavior. However, VCs' scope of involvement mediates between shared beliefs and perceived similarities and entrepreneurs' confidence in VCs' cooperation. When VCs' involvement is perceived as strategically focused, entrepreneurs might consider such involvement positively as it is aligned with a common understanding about the cooperative relations. However, VCs' managerial involvement might be perceived as opposing entrepreneurs' expectations about cooperative relations and therefore might be negatively associated with their confidence in VCs' cooperation. I therefore hypothesize that:

H1: VCs' strategic involvement will mediate the positive relationships between shared beliefs and perceived similarities and entrepreneurs' confidence in VCs' cooperative behavior.

H1a: VCs' managerial involvement will mediate the negative relationships between shared beliefs and perceived similarities and entrepreneurs' confidence in VCs' cooperative behavior.

Fairness and Justice and Entrepreneurs' Confidence in VCs' Cooperative Behavior

Social exchange theory indicates that perceive fairness and justice increase trust between social actors (Shepherd and Zacharakis, 2001), as well as mutual obligations (Whitener, et al, 1998). Following the procedural justice argument, perceived fairness and justice can be enhanced by behavioral consistency, behavioral integrity and sharing and delegation of control (Whitener, et al, 1998). These behavioral aspects serve to reduce trust risks, as well as increasing predictability about economic actors' behavior. Thus, perception of fairness and justice may increase both VCs' and entrepreneurs' confidence in cooperative relations (Shepherd and Zacharakis, 2001).

Pervious studies have shown that timely feedback from entrepreneurs impacts on VCs' perception of fairness and trust (Sapienza and Korsgaard, 1996). In addition, it was also found that relational capital and commitment contribute to VCs' perceptions of their portfolio firms' performance (De Clercq and Sapienza 2006). Although these studies highlight the importance of perceived procedural justice to VCs' and entrepreneurs' relations, little is known about how entrepreneurs construct their perceptions of fairness and justice with VCs. Especially, how entrepreneurs' perceptions of VCs' control mechanisms impact on their confidence in their VCs' behavior. When VCs are managerially involved, entrepreneurs might perceive such involvement as unfair, as VCs might employ formal control mechanisms that restrict entrepreneurs' managerial autonomy, as well as the risk they bear when VCs take coercive actions, such as entrepreneurs' dismissal. I therefore hypothesize that:

H2: VCs' strategic involvement will mediate the positive relationships between perceived fairness and justice and entrepreneurs' confidence in VCs' cooperative behavior.

H2a: VCs' managerial involvement will mediate the negative relationships between entrepreneurs perceived fairness and justice and their confidence in VCs' cooperative behavior.

Entrepreneurs' Influence On Decision-Making and Confidence in VCs' Cooperative Behavior

Sharing control, participation in decision-making and delegation of control are considered to be key components of trustworthy behavior between employees and managers (Whitener, et al, 1998). According to Whitener, et al (1998) "Managerial sharing and delegation of control may promote trust because of the interplay between economic and social factors. When managers involve employees in decision making, employees have greater control over decisions that affect them and, therefore, can protect their own interests. In agency terms this control by employees reduces the risk of opportunism on the part of the manager and increases the likelihood of favorable outcomes for the employee" (Whitener et al, 1998, p. 517). From the agency theory point of view, entrepreneurs' participation in decision-making indicates that VCs trust their ability to make decisions that are consistent with their interests (Jensen and Meckling 1976).

The abovementioned literature suggests that entrepreneurs' ability to influence decision-making influences their confidence in VC cooperation. In cases in which VCs are extensively involved in the actual management of their portfolio firms, entrepreneurs have less ability to influence decision-making. Moreover, some of VCs' actions may be considered by entrepreneurs' as opportunistic, especially if they take coercive actions and replace the entrepreneur (Fiet et al. 1997; Bruton, Fried and Hisrich 1997, 2000). Thus, VCs' managerial involvement is expected to be negatively associated with entrepreneurs' influence on decision-making and with their confidence in VCs' cooperative behavior. On the contrary, VCs strategic involvement might be considered by entrepreneurs as providing valuable complimentary assets in a way that adds value to the portfolio firms (Macmillan et al, 1988). Further more, previous study findings indicated that VCs' perception of fairness and trust increases the support given to entrepreneurs' strategic decisions, while decreasing the frequency of monitoring (Sapienza and Korsgaard, 1996). Similarly, VCs' strategic involvement is expected to be positively associated with entrepreneurs' influence on decision-making and with their confidence in VCs' cooperative behavior. I therefore hypothesize that:

H3: VCs' strategic involvement will mediate the positive relationships between entrepreneurs' influence on decision-making and their confidence in VCs' cooperative behavior.

H3a: VCs' managerial involvement will mediate the negative relationships between entrepreneurs' influence on decision-making and their confidence in VCs' cooperative behavior.

METHODOLOGY

Data Collection

Data were collected from 120 Israeli entrepreneurs using a survey instrument developed by Shepherd and Zacharakis, (2001) to examine those entrepreneurs' confidence in VCs' cooperation. In addition, data were also collected about VCs' scope of involvement using a questionnaire developed by Macmillan, et al, 1988. These surveys were used in their original (English) format, as Israeli entrepreneurs are used to corresponding in English. Additional data about entrepreneurs' perceptions of their influence on decision-making were developed by the author of this paper. In addition to this questionnaire, semi-structured interviews were conducted with six entrepreneurs.

The survey instrument was sent out in winter 2004, by emails to entrepreneurs' who were randomly selected from 500 VC-backed entrepreneurial firms, using the Israeli Venture Capital Research Center (IVC) database. 120 entrepreneurs completed the survey instrument, representing a response rate of 24%. Most of the entrepreneurs (82%) referred in their answers to the lead investor. Most of the entrepreneurs (92%) indicated that the entrepreneurial team holds 50% or less of the equity shares, meaning that VCs had formal governance over most of the firms examined.

Measures

Shared beliefs and perceived similarities between entrepreneurs and VCs were measured with questions developed by Shepherd and Zacharakis, (2001). Entrepreneurs were asked to rank their perceived similarity and shared beliefs, using a seven-point Likert scale (e.g., “the VC shares your beliefs about doing business”). This measure contain 6 items ($\alpha=.915$).

Perceived fairness and justice between entrepreneurs and VCs was measured with questions developed by Shepherd and Zacharakis, (2001). Entrepreneurs were asked to describe to what extent they perceive their relations with their VCs as being honest, fair and trustworthy, as well as being equitable with regard to rewards, using a seven-point Likert scale (e.g., “the VC keeps his/her promises”). This measure contain 5 items ($\alpha=.895$).

Entrepreneurs’ perceived influence on decision-making was measured by questions developed by the author of this paper. Entrepreneurs were asked to describe to what extent they have influence on decision-making related to the R&D, marketing and organizational strategies, using a seven-point Likert scale (e.g., “you have influence over most of the decisions relating to the R&D process”). This measure contain 3 items ($\alpha=.800$).

VCs’ Scope of Involvement

VCs’ strategic involvement was measured by the questionnaire developed by Macmillan et al, 1988. Entrepreneurs were asked to describe to what extent VCs are involved strategically in setting up marketing and R&D strategies, serving as sounding boards and by developing network ties. Strategic involvement was measured by a seven-point Likert scale. This measure contain 7 items ($\alpha=.86$).

VCs’ managerial involvement was measured by the questionnaire developed by Macmillan et al, 1988. Entrepreneurs were asked to describe to what extent VCs are involved in hiring key managers, management replacement, management crises and problems, as well as in setting priorities and providing managerial assistance. Managerial involvement was measured by a seven-point Likert scale. This measure contain 5 items ($\alpha=.81$).

Confidence in VCs’ cooperation was measured with questions developed by Shepherd and Zacharakis, (2001). Entrepreneurs were asked to what extent VCs act according to mutual interest rather than opportunistically, using a seven-point Likert scale (e.g., “the VC has not invested sufficient funds into your venture”). This measure contains 2 items, indicating that entrepreneurs perceive confidence in VCs’ cooperation via two aspects that related to VCs’ commitment over time: the degree to which VCs are willing to provide subsequent investments and the pressure of VCs toward long-term profitability. These items were averaged to produce a scale score ($\alpha=.726$).

RESULTS

Table 1 shows the correlations between the independent variables and entrepreneurs’ confidence in VCs’ cooperation. As shown in Table 1, shared beliefs and perceived similarities ($r=.585$ [$p<.01$]) and perceived fairness and justice ($r=.529$ [$p<.01$]) are positively associated with entrepreneurs’ confidence in VCs’ cooperation, whereas entrepreneurs’ influence on decision-making is found to be negatively associated with entrepreneurs’ confidence in VCs’ cooperation ($r=-.238$ [$p<.01$]).

Figure 1 shows the results for the structural equation modeling. The findings show that VCs’ strategic involvement mediate the positive relationship between shared beliefs and perceived similarities ($\beta=.55^{***}$), perceived fairness and justice ($\beta=.25^{**}$) and entrepreneurs’ influence on decision-making

($\beta=.37^{***}$) and entrepreneurs' confidence in VCs' cooperation. As expected, the findings indicate that entrepreneurs' confidence in VCs' cooperation is mediated by VCs' strategic and managerial involvement. VCs' strategic involvement is found to be positively associated with entrepreneurs' confidence in VCs' cooperation ($\beta=.61^{***}$) whereas VCs' managerial involvement is found to be negatively associated with entrepreneurs' confidence in VCs' cooperation ($\beta=-.45^{***}$).

The findings also show that VCs' managerial involvement mediate the negative relations between shared beliefs and perceived similarities ($\beta=-.17^*$) and entrepreneurs' confidence in VCs' cooperation, thereby providing support for Hypothesis 1a. Contrary to expectations, VCs' managerial involvement does not mediate between perceived fairness and justice and entrepreneurs' confidence in VCs' cooperation ($\beta=.04$, *ns*), thus not supporting Hypothesis 2a. Surprisingly, entrepreneurs' influence on decision-making is found to be positively associated with VCs' managerial involvement ($\beta=.50^{***}$), thus not supporting Hypothesis 3a.

The chi-square value for the model was non-significant ($\chi^2=6.36$). The fit indexes closely match the data (CFI=.98, TLI=.92, RMSEA=.097).

DISCUSSION

Venture capital investments rely on formal and informal control mechanisms. While the aspects associated with VCs' formal control mechanisms are well discussed in the literature, less is known about how VCs and entrepreneurs construct trust relations in general, and how entrepreneurs perceive the connection between social control mechanisms and confidence in VCs' cooperation in particular. As entrepreneurs have less formal control mechanisms, their confidence in VCs' cooperation become an important aspect for their decision to consider cooperation rather than defection (Cable and Shane, 1997).

The findings of this study indicated that VCs' strategic and managerial involvement mediate the relationships between entrepreneurs' perceptions of shared beliefs and similarities, fairness and justice as well as their ability to influence decision-making and their confidence in VCs' cooperation. The results suggest that although social control mechanisms contribute to trust-building and confidence in cooperative relations between VCs and entrepreneurs, the context in which their relations take place should be taken into consideration. That is, the degree to which VCs employ formal control mechanisms by intervening strategically or managerially.

VCs' Strategic Involvement and Entrepreneurs' Confidence in VCs' Cooperation

The findings indicate that VCs' strategic involvement mediates the positive relations between social control mechanisms and entrepreneurs' confidence in VCs' cooperation. Consistent with previous studies' suggestions, shared beliefs and similarities as well as fairness and justice do contribute to entrepreneurs' confidence and VCs' cooperation (Shepherd and Zacharakis, 2001; McEvily, Perrone and Zaheer, 2003). In addition, the findings indicate that, similar to VCs, entrepreneurs' perception of fairness and trust is associated with strategic involvement and confidence in cooperation (Sapienza and Korsgaard, 1996). However, although consistent with other studies findings (De Clercq and Sapienza, 2006), the findings of this study indicate that entrepreneurs consider their ability to influence decision making as a signal for their VCs' trust. Therefore, as long as VCs' involvement is perceived as strategically oriented, social control mechanisms contribute to entrepreneurs' confidence in VCs' cooperation.

VCs' Managerial Involvement and Entrepreneurs' Confidence in VCs' Cooperation

The findings indicate that VCs' managerial involvement is negatively associated with entrepreneurs' confidence in VCs' cooperation. This finding is supported by one of the interviewee words:

I don't want any governance - we are too mature for that; I ask for involvement. Governance leads to suspicions and prevents practical management. From my point of view, they [the VCs] should omit the perception of governance and adopt an attitude of mutual cooperation and real involvement, but not managerial involvement. I ask for another type of involvement: of guiding, mentoring, networking and professional assistance. I ask for the autonomy that is associated with mentoring. Autonomy indicates that the VCs trust me. Trust is the central premise in each relation between VCs and entrepreneurs. If the VCs don't trust me, they should discontinue our relationship.

Consistent with the above citation, the findings indicate that VCs' managerial involvement mediates the negative relationships between shared beliefs and perceived similarities and entrepreneurs' confidence in VCs' cooperation. These findings suggest that VCs' managerial involvement is negatively associated with entrepreneurs' expectations and intentions and therefore their confidence in VCs' cooperative relations.

Surprisingly, the findings indicate that VCs' managerial involvement does not mediate the negative relationships between fairness and justice and entrepreneurs' confidence in VCs' cooperation. Although fairness and justice negatively correlates with VCs' managerial involvement (see Table 1), this correlation becomes non-significant when mediated by VCs' managerial involvement. Entrepreneurs' perceived fairness and justice relate to the extent to which the equity allocation is fair and to the extent to which VCs are honest and fulfill their promises. Therefore the non-significant relations between fairness and justice and VCs' managerial involvement can be explained by the fact that fairness and justice relate more to contracting term issues rather than to ongoing managerial activities. Thus, entrepreneurs' perceived fairness and justice is more associated with strategic involvement that focuses on financing strategies, such as raising subsequent financing, going public (IPO) and creating strategic alliances. Consistent with previous studies' suggestions (Whitener, et al, 1998; Shepherd and Zacharakis, 2001), these findings indicate that entrepreneurs' perceived fairness and justice have a direct effect on their confidence in VCs' cooperation.

Contrary to expectations, the findings also indicate that entrepreneurs' influence on decision-making is found to be positively associated with VCs' managerial involvement. It is possible that entrepreneurs perceive their influence on decision making as positively related to VCs' involvement in management because their joint cooperative relations is interrelated. That is, entrepreneurs ability to influence decision-making is interrelated to VC' managerial involvement suggesting some sharing of managerial responsibilities between entrepreneurs and VCs. However, VCs' managerial involvement is negatively associated with entrepreneurs' confidence in VCs cooperation indicating that although entrepreneurs might cooperate with their VCs managerially, they still perceived it as contradicting their expectations for cooperation.

Implications, Limitations and Future Research Directions

As VCs' and entrepreneurs' relationships consist of bilateral interdependencies, trust between VCs and entrepreneurs are crucial for their ability to cooperate. This is especially true due to the fact that entrepreneurs hold idiosyncratic knowledge and practices that cannot be fully controlled by formal control mechanisms. So far, the current literature under examined entrepreneurs perception of their confidence in VC' cooperation although their willingness to cooperate is clearly depend on their social control mechanisms, as they usually lack formal control mechanisms.

Theoretically, the findings of this study suggest that entrepreneurs may perceive the interplay between their social and formal control mechanisms different from their VCs. From entrepreneurs' point of view, building trust and confidence in VCs' cooperation depends not only on their perception of shared beliefs, similarities and fairness and justice but also by the degree they can influence on decision-making. From VCs' point of view, the need to employ formal control mechanisms may be associated with

entrepreneurs' perceived competence. Thus, it is suggested to examine perceptions of trust between VCs' and entrepreneurs', while taking into consideration contextual aspects that may contribute to trustworthiness as perceived by VC' and entrepreneurs'.

Practically, the findings of this study call for VCs' and entrepreneurs' attention to the role of social control mechanisms in venture capital investments. Thus, although having superior attitude, VCs should be aware of the negative implication that their managerial involvement can have on entrepreneurs' confidence in their cooperation. From the entrepreneurs' point of view, this study's finding joins the suggestion made in previous studies for the construction of informal relations with their investors, as this could influence VCs' perceived fairness and justice, lower their need to use formal control mechanisms and contribute to their perceived performance.

The limitation of this study relates to the subjective assessment of using entrepreneurs as a single source for the data analysis. Further research should therefore focus on a dyadic examination of VCs' and entrepreneurs' perceptions. Additionally, it is also recommended to further examine the variation that might exist in trust relations between entrepreneurs and VCs in different contexts.

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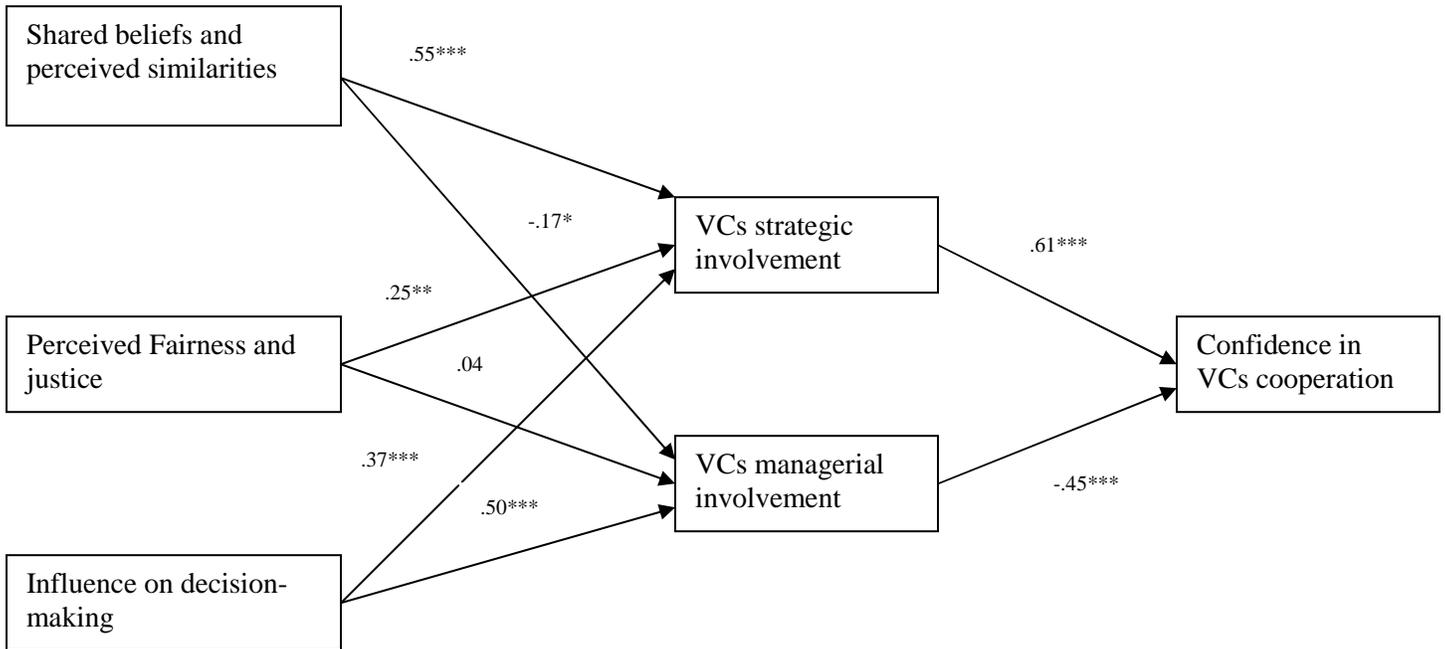
Table 1: Means, Standard Deviations, and Correlations for Study Variables (n=120)

	Mean	S.D.	1	2	3	4	5
Shared beliefs and perceived similarities	4.40	1.34					
Fairness and justice	4.80	1.30	.673**				
Influence on decision making	2.16	.83	-.368**	-.348**			
VCs strategic involvement	3.87	1.11	.570**	.492**	.067		
VCs managerial involvement	3.35	1.14	-.342**	-.249**	.548**	.214*	
Confidence in VCs cooperation	4.62	1.54	.585**	.529**	-.238**	.513**	-.319**

*p<.05 (2-tailed)

**p<.01 (2-tailed)

Figure 1: Entrepreneurs' Confidence in VCs Cooperation – Structural Equation Model Results



Chi-square = 6.36 ($df=3$)
 CFI=.98, TLI=.92, RMSEA=.097
 * $P < .05$, ** $P < .01$, *** $P < .001$