

How can Venture Capitalist-Owner Manager conflicts be managed?

If you want peace, agree to keep the peace.

Claire Champenois, Michel Devigne, and François-Régis Puyou¹

This article identifies four mechanisms (talking continuously; showing commitment to a community; strengthening operational focus; and accepting difficult decisions) in Venture Capitalist (VC) – Owner Manager (OM) relationships that serve to manage tensions and thus avert detrimental situations, namely conflicts. The results enrich the literature on VC-OM conflict by mobilizing a tension intensity variable and by providing evidence on how tense critical events can be managed. We offer recommendations and insight into managing tension intensity, which can help VCs and OMs derive the potential benefits of opposing viewpoints while avoiding major disruptions in their relationships.

¹ Claire Champenois is an Associate Professor in the Department of Management, Organization and Law at Audencia – Nantes Business School, France.

Michel Devigne is an Associate Professor in the Department of Social Sciences and Management at Ecole des Mines de Nantes, Nantes Engineering School, France.

François-Régis Puyou is an Associate Professor in the Department of Management Control and Accounting at Audencia – Nantes Business School, France.

Address correspondence to: F-R. Puyou, Audencia Nantes, 8 route de la Jonelière, BP 31222, 44312 Nantes Cedex 3, France. E-mail: frpuyou@audencia.com

“Today they say: ‘*Si vis pacem para bellum!*’ If you want peace, prepare for war. This Congress says in behalf of the people: ‘*Si vis pacem, para pactum!*’ If you want Peace, agree to keep the Peace.”

Bartholdt, R. (1907) in Proceedings of the National Arbitration and Peace Congress, New York, April 14 to 17, p.233.

Introduction

Cooperation between Venture Capitalists (VCs) and Owner-Managers (OMs) is highly desirable (Cable, and Shane 1997), yet a growing body of the VC-OM relationship literature highlights the ‘dark side’ of such relationships, particularly conflicts (Brettel, Mauer, and Appelhoff 2013; Collewaert 2009; Collewaert, and Fassin 2013; Erikson, and George 2010; Higashide, and Birley 2002; Khanin, and Turel 2015; Parhankangas, and Landström 2006; Yitshaki 2008; Zacharakis). It is well known that whenever two parties cooperate, there is potential for conflict over both the means used and the ends they hope to accomplish (Jehn 1997; Jehn and Mannix 2001). Despite mechanisms to align interests (for example, stock options) and contractual agreements formalizing pre-approved solutions to sensitive topics (for example, investors’ agreements), the VC-OM relationship is also subject to conflict (Jog, Riding, and Lawson 1991). Conflict emergence and conflict management offer relevant and valuable avenues of research inquiry into the ways actors deal with friction. There is a long tradition in conflict theory studies of focusing on the links between different conflict types and their outcomes (Amason 1996; De Dreu, and Weingart 2003; Deutsch 1990; 1994; 2006; Jehn 1995; Pondy 1967; Rahim 2002; Thomas 1992; Tjosvold 1998a; 1998b). Accordingly, various conflict types (for example relationship conflict, task conflict, and process conflict) can have negative or positive outcomes (Jehn, and Bendersky 2003; Pelled, Eisenhardt, and Xin 1999; Wit, and Greer 2012). This literature has been applied extensively to the specific context of VC-OM relationships to study the link between conflict styles and confidence (Zacharakis, Erikson, and George 2010), performance (Higashide, and Birley 2002), exit intentions (Collewaert 2012), contractual covenants (Parhankangas, Landström, and Smith 2005) and

regrets related to action or inaction (Khanin, and Turel 2015). As advocated by conflict theory, these studies collectively demonstrate that affective conflict is detrimental to performance whereas task and process conflicts, if moderate and occurring under specific circumstances, can benefit performance. In addition, there is evidence that disagreements can have positive impacts at low conflict levels, whereas escalation in opposition triggers strong negative emotional outcomes (Eisenhardt, Kahwajy, and Bourgeois III 1997). However, existing research remains unclear when it comes to distinguishing between “mild conflict,” which may prove beneficial, and “intense conflict,” which has detrimental consequences (Todorova, Bear, and Weigart 2014). Conflict intensity is therefore a key issue that warrants further investigation.

In this paper, conflict is defined as perceived discrepant views of a problem that has remained unresolved despite dedicated efforts to do so. Conflict situations between VC and OM are therefore characterized by decisions that are made (or not) against the will of the other party. In contrast, most of the issues jointly addressed by VC and OM lead to mutually held positions that are reached either rapidly or after longer debates. This article therefore considers situations of conflict as occupying the high end of a continuum of tension intensity ranging from high tension level (conflict) to low tension level (rapid agreement), with a moderate tension level in-between (agreement after long discussions). This continuum is helpful to clarify that, if all tensions between VCs and OMs originate in problems to be addressed collectively, not all of them are of a conflictive nature. This conceptualization of conflict increases the distinctiveness between critical events that are compatible with collaboration and those leading to the failure of the VC-OM relationship.

The article contributes to research on VC-OM conflicts by clarifying practices and processes implemented by interdependent partners to control tension intensity. The paper identifies four mechanisms (*talking continuously; showing commitment to a community; strengthening operational focus; and accepting difficult decisions*) within VC-OM

relationships that enable both parties to manage tensions and thus avert detrimental situations. Our approach is inspired by Simmel's sociology of conflict (Simmel 1904a; 1904b; 1904c), which argues that conflict and cooperation should not be considered opposites. Instead, one should consider intermediate levels of tension within relationships as opportunities for socialization. Simmel's work encourages observers to see potential future conflicts as incentives to make efforts immediately to preserve peaceful relations.

The results are based on a case study of a French Private Equity Firm named ALPHA (a pseudonym), which offers development capital to growing medium-sized regional companies, and of eleven of its ventures. The entrepreneur-investor relationship is analyzed after the investor's decision to invest. We consider both investors' and entrepreneurs' points of view, and reconstruct the temporal emergence and development of these VC-OM relationships.

The paper proceeds as follows. First, we present the literature on conflict management in VC-OM relationships and our theoretical approach to conflict management, inspired by Simmel's framework. Next we describe the research method and the empirical data collected for the study. The third section is dedicated to the detailed analysis of the four mechanisms that have been identified as contributing to tension management. The empirical results are discussed in the fourth section. Theoretical and practical implications of the study are highlighted in the conclusion.

Conflicts in VC-OM relationships and Simmel's contribution

Inspired by Simmel's (1904a; 1904b; 1904c) work, the "what is a conflict" sub-section provides a definition of conflict grounded in the actors' experience. We then challenge the existing conflict typology by arguing that tension *intensity* is a characteristic dimension of such relations that has been largely overlooked. Consideration of tension as a relational experience is further explored in the "tension management" subsection. Lastly, the social embeddedness

of VC-OM relationships is examined carefully in the “conflict and socially embedded interdependencies” section.

What is a conflict?

The definition of conflict used in most articles dealing with VC-OM relationships (Collewaert 2012; Brettel, Mauer, and Appelhoff 2013; Higashide and Birley 2002; Zacharakis, Erikson, and George 2010) draws on Boulding (1963) and Jehn (1995). These authors define conflict as perceived incompatibilities or the perception that the parties involved hold discrepant views. Consequently, these articles do not take into account critics that have invited scholars to distinguish between conflict itself and its antecedent conditions (Schmidt, and Kochan 1972; Pondy 1967).

To complement this definition of conflict, we consider Simmel’s sociology of conflict (1904a; 1904b; 1904c). The famous German sociologist defined conflict as a social form: unlike Weberian “ideal types,” Simmelian “social forms” are not concepts invented by the researcher in the process of sociological analysis; rather, they exist in the actors’ minds. Viewing conflict as a “social form” means that human actors have a clear understanding of what conflict is even when their relations with other individuals are harmonious. They are able to give examples of a conflict even if none is ongoing, and there is no need for a well identified conflict to exist in practice for it to influence behaviors, especially when interdependence is high:

That in very intimate relationships, which control, or at least affect, the whole content of life – such, for example, as marriage – no occasions for conflicts emerge, is unthinkable. Never to yield to them, but to anticipate them from a distance, to insure against them in advance by reciprocal concession, is by no means always an affair of the most genuine and profound affinity, [...] The perceived insecurity in the basis of such relationships frequently influences us, because of our wish to preserve the relationships at all costs, to exercise quite exaggerated

unselfishness, and even to use mechanical guarantees of the situation, through avoidance on principle of every threatening conflict. Simmel (1904a: 517-518).

One consequence of Simmel's view of conflict as social form is that social actors are quite capable of identifying what a conflict is. Conflict can therefore be defined through empirical study. This article shows that venture-capitalists (VCs) and owner-managers (OMs) use the word "conflict" only in reference to situations that have gone out of control. Considering conflict as a threat present in their minds, VCs and OMs carefully manage situations to prevent them from degenerating into uncontrolled opposition.

Informed by Simmel's definition of conflict as social form, we introduce a more precise definition of conflict. Specifically, conflict consists of perceived discrepant views on a problem *that failed to be fixed in spite of dedicated efforts to do so*. If conflict is viewed as a result of a process through which discrepant views have failed to be fixed, there are, in contrast, situations when discrepant views can be resolved and agreements settled. We propose to call "tensions" *situations in which actors acknowledge their discrepant views and make efforts to overcome them*. Our definitions of conflict and tension imply that the social mechanisms inherent in processes, which could lead to conflict if not properly managed, should be considered relevant to the conflict literature.

Tension intensity

Tension level is defined by the time necessary to overcome discrepant views (short or long) and by its result (agreement or disagreement). *Low tension* prevails when a discrepant view of a problem is easily fixed by a rapid exchange of views between partners, and *moderate tension* occurs when the discrepant view is fixed through a longer and more demanding process of discussion between parties. In both cases, an agreement is reached. In contrast, *high tension*

– *i.e. conflict* - occurs when actors abandon hope of finding an agreement in spite of dedicated efforts to do so.

This continuum from low to high tension contributes to the literature on conflict in VC-OM relationships by introducing tension intensity beyond traditional conflict types (Amason 1996; Bourgeois III 1980; Jehn 1995; Jehn, and Mannix 2001; Rahim 1983a; 1983b). The conflict theory approach applied to VC-OM relationships neglects intensity. Other research (such as Eisenhardt, Kahwajy, and Bourgeois III 1997) argues that a ‘moderate’ level of task conflict within management teams can be productive, but without specifying what this ‘moderate level’ may be. Our goal is to complement existing research regarding tension intensity and to extend it to the VC-OM relationship.

Our research invites scholars and commentators to construe conflict as the extreme point of a continuum of tension situations: from low and moderate tension between potentially reconcilable viewpoints – which can be beneficial to the relationship – to high tension, that is conflicts, which are destructive. Conceptualizing conflicts as one end of a continuum of tension intensity increases the distinctiveness between critical events that are compatible with collaboration and those leading to the failure of the relationship. Whereas all tension events between VC and OM originate in disagreements, not all disagreements are conflictual. In this view of the tension continuum, a tension level score can be developed. The present study thus complements that of Zacharakis and Erikson (2010) by exploring tension management mechanisms not only in situations of declared conflict (high tension), but also across tensions of varying intensity. It addresses the issue of ‘how’ tension is managed and invites observers to carefully consider the intensity level of tension between partners, and not merely situations of conflict.

Tension management

We contribute to the conflict management literature by developing a more precise view of how VCs and OMs develop a cooperative style of tension management. Drawing on Simmel's work (Simmel 1904a; 1904b; 1904c), we construe conflict as a force that brings social actors together in a relationship. From a Simmelian point of view, conflict anticipation prompts mutual attention to the preservation of good relations when tension emerges. Inspired by the socializing effect of both declared and anticipated conflicts, this paper contributes to a better understanding of the relational processes to handle tensions so that they do not spiral out of control with damaging consequences on performance, reputation and partnerships. We argue that VCs and OMs develop specific mechanisms to manage tensions, notably to prevent them from reaching a high level.

Conflict management theory (Deutsch 1990; 1994; 2006; Rahim 2002; Thomas 1992; Tjosvold, and Weicker 1993; Tjosvold 1998a; 1998b) has developed as a branch of conflict theory. It aims at understanding the way in which people deal with conflict when it occurs. It suggests that conflict can be a positive force in organizations only if it is managed properly (Jameson 1999; Pelled, Eisenhardt, and Xin 1999; Rahim 2002). Several methods or strategies for handling conflict have been considered. Based on Blake and Mouton's work (1964), a taxonomy of conflict-handling modes has been elaborated that distinguishes five different modes (Rubin, Pruitt, and Kim 1994; Thomas 1992; Rahim 2002): competing, collaborating, compromising, avoiding and accommodating. These conflict-handling modes are classified according to the underlying dimensions of assertiveness (attempts to satisfy one's own concerns) and cooperativeness (attempts to satisfy others' concerns). Even if the conflict management approach stresses that there is no single best way for managing conflict, and advocates for a contingency approach (also called situational approach), some studies (Rahim, Magner, and Shapiro 2000; Tjosvold and Sun 2002; Zhang, Cao, and Tjosvold 2011)

nonetheless point out that cooperative styles of handling conflict, such as accommodating, collaborating or compromising, are correlated with positive outcomes, and non-cooperative styles, such as competing or avoiding, are correlated with negative outcomes. Deutsch and Tjosvold (Deutsch 1990; 2006; Tjosvold 1998b; 2008) explored the cooperative and competitive theory of handling conflict. They clearly show that the cooperative handling mode of conflict contributes more positively to organizational effectiveness than a competitive mode does. Nevertheless, Tjosvold (1998b; 2008) states that little is known about *how* cooperative goals, rather than competitive ones, can be set before a conflict occurs. One major contribution of our article is that it investigates how cooperative relations emerge, and considers how actors (OMs and VCs) deal with tensions in their relationships to prevent them from becoming too high. We adopt a Simmelian perspective by arguing that actors (VCs and OMs) mainly anticipate the possibility of conflict when handling tensions. VCs and OMs dedicate their efforts mainly to managing tensions before they develop into conflict. We thus redirect attention from conflict management to tension management.

Our work deepens insights offered by previous conflict studies in the specific context of VC-OM relationships (Parhankangas and Landström 2004, 2005, 2006; and Yitshaki 2007; Zacharakis, Erikson, and George 2010) by defining tension management mechanisms adopted by the two partners. Informed by the conflict management approach, we depart from a conflict resolution perspective advocated by Parhankangas (2004, 2005), among others, and propose a tension management approach. Parhankangas and Landström (2004) studied how VCs react when entrepreneurs fail to live up to their expectations. Mobilizing the theoretical frameworks of psychological contract violation (Levinson, Price, Munden, Mandl, and Solley 1962; Morrison, and Robinson 1997; Rousseau 1995) and of responses to unmet expectations (Farrell 1983; Hirschman 1970), they underline that VCs are not passive but rather are active problem solvers, and that their behavioral attitude is dependent on the type of psychological contract

violation. Although they do not use the conflict management literature, they confirm one of its important contributions: conflicts can be beneficial for the venture's performance if it is actively handled (by the VCs). Our research adds to this work by precisely documenting the 'active handling' approach used by both VCs and OMs. To better understand tension management and the creation of relational rents (De Clercq, and Sapienza 2001; 2006), we develop a relational view of tensions including both VC and OM perspectives (as advocated by Zackarakis et al. (2010, p. 123) but rarely done in the literature.

Conflict and socially embedded interdependencies

Relations between VCs and OMs are often considered only through a single actor's point of view (for an exception see notably Collewaert (2012) on Business Angels and entrepreneurs). Interdependencies between VCs and OMs are therefore likely to be underestimated. The present study addresses a call to further investigate the investor-investee dyad (Lockett, Ucbasaran, and Butler 2006) by examining tensions between VCs and entrepreneurs in the course of their post-investment relationship. The interdependency of VC and OM has long been documented from financial (Admati, and Pfleiderer 1994; Casamatta 2003; Gompers 1995; Kaplan, and Stromberg 2004; Lerner 1995) and non-financial perspectives (Busenitz, Fiet, and Moesel 2004; Croce, Marti, and Murtinu 2013; Fried, and Hisrich 1995; Politis 2008; Sapienza 1992; Sapienza, Manigart, and Vermeir 1996; St-Pierre, Nomo, and Pilaeva 2011; Timmons, and Bygrave 1986). It has also been shown that VC-OM exchanges are socially "embedded" (Ferrary, and Granovetter 2009; Ferrary 2003; Granovetter 1983; Sorenson, and Stuart 2001; Uzzi 1996): their behaviors cannot be understood without taking into account their social relations with actors in the environment. In contrast, the impact of social embeddedness and interdependency on conflict in VC-OM relationships has largely been overlooked. An exception is Parhankangas and Landström (2006), who investigated the

role of social environment in venture capitalists' response to entrepreneurs' unmet expectations. They demonstrate that VCs with strong ties to their peers tend to solve problems with their portfolio companies in a more active and constructive manner than their isolated colleagues do.

Considering social embeddedness and interdependencies between parties in conflict is one of the main insights of Simmel's theorization of conflict (Simmel 1904a; 1904b; 1904c). Accordingly, conflict can be seen as functional: as a socialization device or a tool to create bonds between parties sharing similar interests for common stakes. Consequently, conflict can also be seen as a reciprocal relationship in which interdependency between the involved parties is a fundamental dimension. In line with Simmel's view on conflict, the conflict management approach (Coser 1956; Jehn, and Bendersky 2003) expresses a concern for the cooperative and socializing dimensions of tense or difficult relations. The present article complements the literature on conflicts in VC-OM relationships by introducing this Simmelian perspective, which explains why socialization may thrive when interdependent actors deal with common concerns in tense situations.

Method

Research design and data collection

Case studies are particularly relevant when the objective is to analyze processual and interdependent mechanisms and to answer a 'how' question (Eisenhardt, and Graebner 2007). The present case study investigates *how* entrepreneurs and investors mitigate tensions between them. We examine the relationships between one capital investment firm ("ALPHA") and eleven of its ventures. Our research strategy was to use a case study to inductively create theoretical propositions (Corbin, and Strauss 1998; Eisenhardt 1989; Eisenhardt, and Graebner 2007). The repeated mentioning of peace-keeping mechanisms, first by ALPHA investors and then by OMs, signaled that it was an important subject of analysis.

ALPHA is a French venture capital firm investing in well-established, profitable and growing SMEs of all sectors situated within a limited, although historically increasingly large, geographical area: western France. Contrary to most large national or international venture capital firms, the firm takes only minority shares in ventures and does not set a specific exit date in advance. This investment policy (summarized in Table 1) is a result of the VC firm's specific statutory regime that, in the French legal context, allowed it to reduce taxes on value added profits and dividends.

[INSERT TABLE 1 ABOUT HERE]

Unlike many VCs, ALPHA investors lacked formal power over entrepreneurs, who generally owned a majority of their company shares. ALPHA was thus strongly encouraged to get along well with the entrepreneurs because they could not easily replace them. Deprived of the usual means, described extensively by agency theory scholars, to impose its will on the entrepreneur, the VC was in a situation where disagreements had to be solved peacefully and harmoniously. Therefore, ALPHA is a case where tension management mechanisms were expected to be particularly numerous and refined. This is consistent with the fact that all but one interviewee asserted that they had *good*, or harmonious, relations with their business partner (VC or OM). The only notable exception was POLYSTYRENE (a portfolio company pseudonym) that, according to both its CEO and ALPHA's investment managers, constituted a case of overt conflict.

Another reason to study ALPHA was the unusual length of the VC-OM relationships. In a Simmelian perspective, in situations where both parties anticipate that the relationship will be long, the need for both actors to regulate tensions is particularly strong.

Finally, access to a wide range of interlocutors also played a role in the choice of ALPHA as an adequate field of study. The research team was given the rare opportunity to interview all investment managers within ALPHA, allowing for solid data triangulation. In

addition, researchers could also contact a sample of eleven entrepreneurs, illustrating ALPHA's portfolio diversity not only in terms of tension levels, but also regarding dates of creation and sector.

Data collection started in January 2010 with structured interviews of all ALPHA general and investment managers. This initial investigation contributed to the construction of a trustful relationship between ALPHA members and the team of researchers. During the interviews with VCs we explicitly asked our interlocutors to suggest a few company names that they considered representative of the spectrum of tensions they faced in their relationships with OMs. Out of this list of names, we produced, together with the two ALPHA directors, a short list of twelve companies with the explicit aim of including a wide variety of tension levels and diverse company size, seniority in the portfolio and sectors. A second series of contacts was then made and eleven interviews were conducted between October and December 2010 (see a brief description of the companies in Table 2).

[INSERT TABLE 2 ABOUT HERE]

The CEOs in our sample were all owner-managers, who could be considered "entrepreneurs" in that they made their businesses grow by identifying and exploiting "entrepreneurial opportunities" (Kirzner 1973). Consequently, we will use the terms "entrepreneurs" and "owner-managers" ("OMs") as synonymous for our purposes. During interviews, our questions were designed to clarify how the relationship between the VC and the entrepreneur developed in a longitudinal perspective. They concentrated on facts using standard courtroom interrogation (for example, "What subject had been under scrutiny?" "When did this become an issue?") and on processes. Interviewees were encouraged to narrate in detail events of importance that had occurred over the course of their collaborations with ALPHA. We also asked each OM to characterize his or her relation with ALPHA in terms of tension level. OMs could answer with some direct knowledge of the situation in other companies because all of

them knew other OMs working with ALPHA either through “meeting days” organized by ALPHA, or through connections via business unions or via membership in entrepreneur clubs. For example, the OM at POLYSTYRENE confirmed that he was undoubtedly the most difficult case in the ALPHA portfolio and was unique. In total, semi-structured interviews were conducted with 20 people (nine investors and eleven owner-managers). More than thirty hours of interviews were carried out, recorded and fully transcribed.

Data analysis

Our question was ‘How do entrepreneurs and VC prevent tensions from developing into detrimental opposition’? Consistent with a Simmelian approach that considers conflict as an inherent element of any intimate relationship, we focused on the mechanisms implemented to manage situations of tension.

We started by analyzing the data collected respectively from the VC and entrepreneur groups, and we wrote two monographs in the first quarter of 2011. Based on a thematic coding of each interview and on cross-analysis between informants and between firm cases, we looked for similar constructs and relationships among cases. This analytical work allowed us to identify preliminary patterns of tension mitigation and the existence of critical events.

In the second step, a list of critical events was established individually by each author, then cross-checked and compared, resulting in a final list of 40 critical events (See Table 3). This was done in line with the critical incident technique methodology (Chell and Pittaway 1998; Flanagan 1954; Turcan 2008). However, unlike the critical incident technique, our intent was not to study the impact of events on the success or failure of the venture. Therefore, the more neutral term ‘event’ was preferred to ‘incident.’ In interviews, such events correspond to particular moments in a venture’s life when a phenomenon occurs that is perceived by actors as having high tension potential (for example, shareholder exit, disappointing economic results,

and investment/divestment from a subsidiary). These are situations where decisions and actions are required that might create disagreements. Indeed, tensions cannot be measured independently of the persons involved, and our informants were best positioned to identify the moments that were most critical in the business partnership.

For each event, the mechanisms implemented by VCs and entrepreneurs were studied in depth. All interviews were coded a second time by each of the authors independently, before being cross-checked, to precisely identify the nature and intensity of the tension management mechanisms implemented. The entrepreneurs' and the VC's viewpoints on their handling of each critical event identified were considered. We used tables to facilitate the analysis (Miles and Huberman 1994). For example, relevant interview sections were copied and compared in tables presenting, by column, the tension management mechanisms and, by row, the firm names and the event numbers.

Lastly, we developed a score to measure conflict intensity for each event and a set of metrics measuring the frequency and relative importance of each mechanism to quantify their intensity in the eleven firms under study. A detailed description of the metrics methodology is given in the following section.

The data analysis was an iterative process. We constantly returned to the data, literature and theory to refine our emerging concepts. This allowed us to come up with a model of four mechanisms implemented to manage tensions and prevent conflicts, with variable levels of intensity.

Results

Tension management as a breeding ground for cooperation

Investors and OMs tended to describe their work as almost entirely free of conflicting relations. In their view, the word “conflict” was used to refer only to out-of-control situations that reach extreme opposition and that preclude the maintenance of a work relationship between

VCS and OMs. However, numerous (n = 40) critical events, defined as situations with potentially high impact on the venture organization and economic performance, were mentioned by informants as revealing several tensions in most of the VC-Entrepreneur relationships. These events encompassed tension levels that can be divided into three categories. “Low tension” referred to situations in which entrepreneurs and investors faced a critical event but rapidly agreed on the adequate decisions and policies. Such a low-tension situation is exemplified by the relation between the PUBLIC WORKS Entrepreneur and ALPHA following economic difficulties in 2007 (critical event 17, see Table 3). The entrepreneur asked ALPHA to waive its priority dividends for a while, to allow the company to transcend this difficult time. ALPHA was reluctant at first, but it soon became clear to the two interlocutors that this concession was necessary given the situation. “Moderate tension” differs from low tension in that contradictory opinions emerged between the two partners but were overcome through a somewhat painful negotiation process. Moderate tension typically implied long discussions structured around arguments and counterarguments intended to convince the other. Such “moderate tension” situations can be illustrated by critical event 23 (see Table 3), when e-MARKETING also had to ask ALPHA to forgo its dividends following the “dot.com” crisis. The issue was settled only after long discussions between the parties. e-MARKETING was notably asked to close its R&D department, initially against the entrepreneur’s will, to reach a compromise. Lastly, “high tension” or “conflict” refers to situations when decisions were made (or not) with explicit disapproval of one of the parties, inducing mutual misunderstanding and long-lasting loss of trust. This is the case in critical event 8 (see Table 3), when the POLYSTYRENE manager categorically refused to sell his company despite ALPHA’s repeated written requests to do so.

Table 3 presents the 40 critical events identified and their respective tension level. It shows that only a few of them ($n = 5$) were high tension events (that is, conflictual), all of which referred to the situation in one firm: POLYSTYRENE.

[INSERT TABLE 3 ABOUT HERE]

Table 4 below presents measures of tension levels in the VC-OM relationship. The tension score was calculated by giving a value of 1 to events with a low tension level, a value of 2 to events with a moderate tension level, and a value of 3 to high tension events. The average tension score is the total tension score for a company divided by the number of years in ALPHA's portfolio.

[INSERT TABLE 4 ABOUT HERE]

These results indicate that non-conflicting relationships are not necessarily tension-free. Some tension is generally experienced in all VC-OM relationships, although very few evolve into conflicts. Conflicts characterized by an escalation of tensions due to long-lasting incompatibilities are rare at ALPHA. This can be explained by the notion of 'conflict,' which constitutes a "form" in the Simmelian sense: a situation that the involved actors clearly conceive with fear, and therefore try to avoid.

The remaining part of the article explores the mechanisms implemented by VCs and OMs to keep tension levels at low and moderate levels during critical events. We argue that such mechanisms play an important role in tension regulation because the overall level of tension cannot be explained solely by the nature of the critical events. Indeed, critical events that are similar in nature often lead to situations with different levels of tension (e.g. critical events 9, 27 and 30 in Table 3). Other factors, primarily the mechanisms that we will now describe, must therefore explain the differences in tension levels (cf. Tables 3 and 4).

Tension management mechanisms

During our field study, we identified four tension management mechanisms. All four mechanisms were activated in almost all VC-entrepreneur relationships with intensity levels ranging from “0” to “++” (see Table 5). To assess the intensity of the “talking continuously” and “accepting difficult decisions” mechanisms, we assigned each firm a score of “0” for no mention of any practice related to the mechanism; “+” when interviewees mentioned practices related to that mechanism; and “++” when such practices were mentioned explicitly several times, implying that they played a significant role in the partners’ relations. Examples of the situations related to the three intensity levels are found in the table illustrating each of these mechanisms in the next section.

To assess the intensity of “strengthening operational focus” and “showing commitment” mechanisms, we assigned each firm a score of “+” by default, considering that owner-managers were involved both in firm management and in the regional business community as a preliminary condition for ALPHA investment. We rated ventures “++” when the owner-managers strengthened their operational focus when facing difficulties or showed strong dedication to regional business associations. Similarly we assigned a “0” to ventures whose owner-managers did not increase their commitment to operations during difficulties or showed limited interest in local business networks. Again, examples for each intensity level are provided in the charts of the next section.

[INSERT TABLE 5 ABOUT HERE]

The next four sub-sections present each mechanism illustrated by situations exemplifying various implementation intensities. For each mechanism, a table offers a selection of three to four examples. Because POLYSTYRENE is the only case of conflict (i.e. high tension) within the sample, it has been used as an illustration in each sub-section. The other examples were chosen because they convey the variety of practices associated with each

mechanism. Finally, the position of ALPHA investors regarding each mechanism is presented systematically at the end of each of the four tables.

Two mechanisms (*talking continuously* and *showing commitment to a community*) were implemented on a continuous basis, whereas the other two (*strengthening operational focus* and *accepting difficult decisions*) were mobilized for a limited duration in periods of growing tension. When applied together, all four mechanisms constitute powerful means for preventing tensions from turning into conflicts.

Talking continuously

This mechanism consists of demonstrating a permanent and mutual will to communicate about the venture. When it is “high,” the flow of information and ideas shared by both parties is perceived as uninterrupted. Through this mechanism, entrepreneurs demonstrate efforts to communicate openly, without duplicity or restraint, concerning all information VCs require on the firm’s current results and future plans. In turn, VCs express their constant readiness to listen and provide advice by promptly sharing their evaluation of the situation. Both partners continuously confirm their interlocutor’s commitment to nurture the business.

This flow of information took place along both formal (general assemblies, board of directors’ meetings) and informal (spontaneous visits, phone calls or lunches) communication channels. Formal and informal channels may complement and supplement each other over time. In general, the older the investment, the more informal the interactions (cf. for example e-MARKETING in Table 6).

[INSERT TABLE 6 ABOUT HERE]

Talking continuously is a way for the entrepreneur and the VC to avoid “surprises” by being updated in real time. This creates a sense of team collaboration and helps keep tension levels low. Table 5 shows that the “talking continuously” mechanism was activated in most

situations (ten out of eleven with “++/high” or “+/medium” intensity). The only case where communication was not considered “continuous” (that is, with a score indicating “0/low”) was the conflictual one (POLYSTYRENE).

Showing commitment to a community

The second tension management mechanism encompasses several empirical elements. First, entrepreneurs and investors asserted and praised their participation in a regional community composed of SMEs located in the western part of France and of investors specializing in this territory (as opposed to national or international VC firms, referred to as “Parisian” or “Anglo-Saxon” firms by VCs and entrepreneurs alike). Entrepreneurs commonly referred to ALPHA as a “family” and people they felt “close to.” In addition, entrepreneurs and VCs shared “strong ties” (Granovetter 1983), that is, old and regular relations that resemble friendships more than strictly professional connections.

Second, VC and OM demonstrated that they shared similar values, namely a will to promote the economic development of the territory and to preserve local jobs. Such aims were sometimes given priority over the maximization of the firm’s financial value (see the AD-PAPERS example in Table 7).

Third, VC and OM showed concern about their partner’s reputation. Most entrepreneurs mentioned and praised ALPHA’s good track record based on the 500 deals signed with SMEs in the region over the past 30 years. Both parties endeavored to preserve the partner’s image in the community (see the DOORS example in Table 7).

The two relationships scoring “0/low” in Table 5 (“Showing commitment” column) were firms with head offices geographically more distant from ALPHA headquarters than the others. ELECTRIC CORP and WINE were indeed located outside of the core historic region of ALPHA’s activity; ALPHA had started doing business there only a few years ago.

[INSERT TABLE 7 ABOUT HERE]

Demonstrating a sense of belonging to the same community helps mitigate tensions. Indeed, this stance indicates to a partner that the other partner is aware of their mutual dependence in the relationship. In addition, both partners anticipate that they will interact again and engage in future deals. By sharing similar values, they make their behavior more predictable for the other.

Strengthening operational focus

This mechanism refers to parallel reinforcing efforts that are implemented – and considered relevant – by both parties when sudden economic events occur that threaten the venture (see Table 8 for examples). During such critical situations, OMs generally expended diligent and visible managerial effort to address the critical issue in a “focused” way. That is, by remaining focused on the resolution of immediate concerns without looking for grand solutions that did not yield short-term results (see the EXCEPTIONAL TRANSPORT example). Meanwhile, VCs supported the entrepreneurs’ actions by giving them quality advice or relevant contacts and by demonstrating their availability.

These parallel behaviors were those each partner considered appropriate to resolve difficulties. They consisted in reciprocal expectations and were intensely scrutinized by both parties. When one partner observed that the other one was adopting an appropriate stance, the tension level remained low. Abiding by expectations was a way for each partner to nurture trust in the relationship and prevent tensions from escalating into conflict. In contrast, when one considered the other’s behavior as inadequate, anxiety appeared, which triggered tension (POLYSTYRENE example).

Given that it was crucial for both partners to collectively probe ideas and agree on solutions, strengthening operational focus was often accompanied by an increase in the

frequency of exchanges between entrepreneurs and investors (see FUNERAL example in Table 8). This mechanism is reinforced by regular contact, as described in the “talking continuously” sub-section. Yet strengthening operational focus was substantially different from the first mechanism (“talking continuously”) in that the interpretation of the partners’ decisions had an immediate effect: collaboration was quickly reinforced or damaged depending on the partner’s reaction to dire situations.

[INSERT TABLE 8 ABOUT HERE]

Accepting difficult decisions

For investors and owner-managers, this mechanism consists of making decisions for the sake of the firm’s economic well-being that are opposed to their individual immediate interests or desires. Such decisions, characterized by reciprocal concessions and explicit unselfishness, signaled the partners’ dedication to the venture and strengthened the relationship while reducing tensions.

Table 5 shows that this mechanism has a “++/high” or “+/-medium” intensity in nine out of eleven cases, with a “0/low” score solely for ELECTRIC CORP and PUBLIC WORKS, where no situation requiring this kind of decision had occurred.

Table 9 presents two illustrative examples (e-MARKETING and FUNERAL) where the mutual acknowledgement of the partners’ efforts in favor of the common good reinforced trust and kept tensions at moderate levels between both partners. It also shows that the mechanism could also be found in the conflictual case (POLYSTYRENE). Quite remarkably, even in open conflict situations, accepting difficult decisions still acted as a mechanism that reduced the intensity of conflict. Such measures may not have been sufficient to fully restore the situation to normal, but they may have proven useful to prevent further deterioration of the relationship into a highly public dispute, for example.

[INSERT TABLE 9 ABOUT HERE]

When making particularly difficult decisions in which they mitigate their own individual interests by taking into account the interests of the other party, entrepreneurs and investors demonstrated their loyalty towards their partner. Adopting “reasonable” behavior rather than self-interested behavior regulates tensions and prevents them from spiraling into conflict. Both parties showed each other that their desire to pursue the relationship was stronger than the tensions that may pull them apart. The capacity to listen and to take the other’s interests into consideration was a major factor that helped preserve the quality of the relations. This capacity was indeed a reciprocal expectation held by both partners.

Discussion

In this study, we have argued that VCs and OMs exert efforts to keep tension intensity at low or moderate levels and to avoid high tension levels with detrimental outcomes. Tension intensity is thus a characteristic dimension of VC-OM relationships. VCs and OMs implement tension intensity management through four relational mechanisms: talking continuously, showing commitment to a community, strengthening operational focus and accepting difficult decisions. In contrast with conflict theory (Amason 1996; De Dreu, and Weingart 2003; Deutsch 1990; 1994; 2006; Jehn 1995; Pondy 1967; Rahim 2002; Thomas 1992; Tjosvold 1998a; 1998b), which has largely informed previous studies of the conflict-related dimension of VC-OMs relationships (Brettel, Mauer, and Appelhoff 2013; Collewaert 2009; Collewaert, and Fassin 2013; Higashide, and Birley 2002; Khanin, and Turel 2015; Parhankangas, and Landström 2006; Yitshaki 2008; Zacharakis, Erikson, and George 2010), we foregrounded tension management and tension intensity and relegated the more traditional conflict type approach to the background. We thus departed from classical conflict definition and proposed a definition that takes into account the fact that some disagreements can be overcome through

discussion without detrimental consequences. In contrast with studies that explore the impact of different conflict types on various outcomes (Brettel, Mauer, and Appelhoff 2013; Collewaert 2012; Higashide, and Birley 2002; Khanin, and Turel 2015; Parhankangas, and Landström 2006), we examine how VCs and OMs deal with tensions that appear in their day-to-day relationships and what kind of mechanisms they implement to handle them. We thus document how a cooperative style of tension management is achieved.

Our key findings are as follows. First, we assert an overall relation of congruence between tension management mechanisms and levels of tension between VC and entrepreneurs. Table 10 offers a synthesis of the case and suggests that the more mechanisms activated to structure the relationship, the lower the tension level. These are not generalizable results but rather a clear and strong indication that careful management of the relationship is likely to ease tensions.

[INSERT TABLE 10 ABOUT HERE]

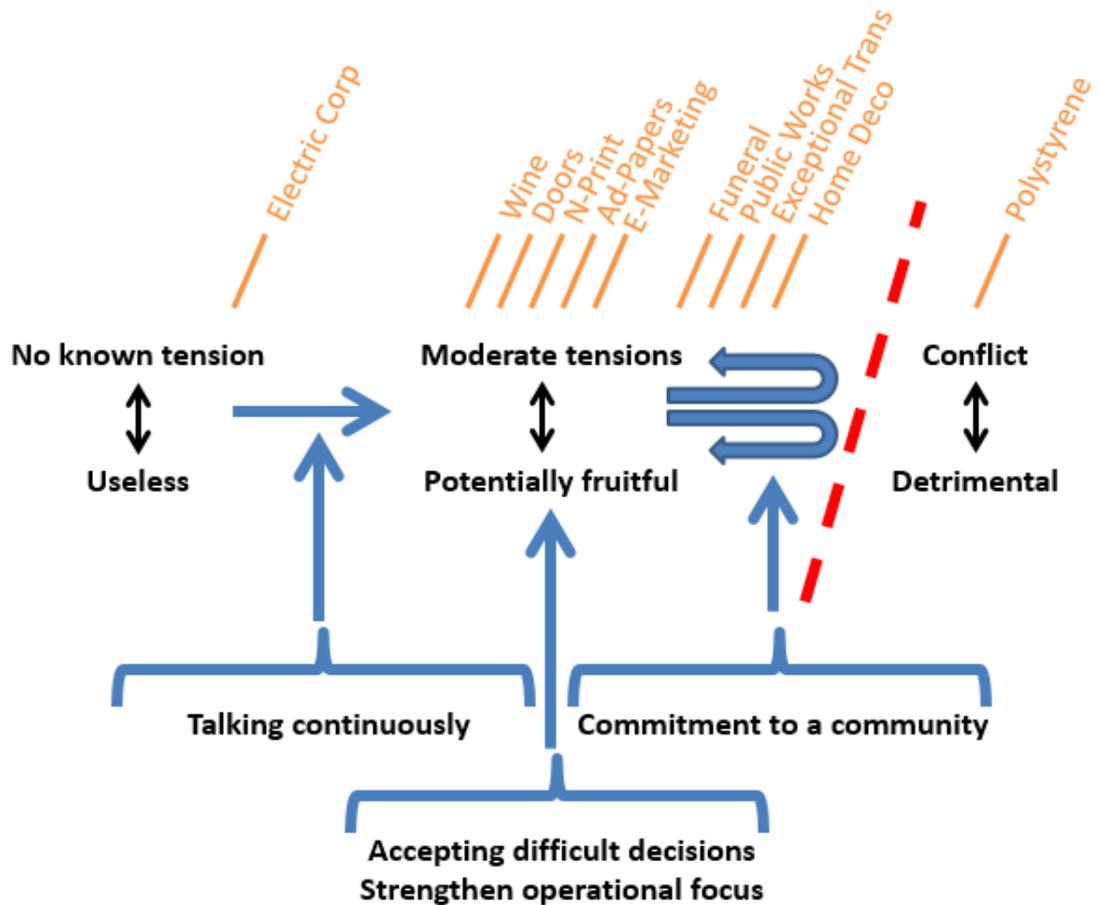
The second finding of this study is that “conflict” should be integrated within a continuum of tensions. This article sheds new light on an understudied dimension of “conflict”: its *intensity* (Eisenhardt, Kahwajy, and Bourgeois III 1997; Jehn, and Bendersky 2003). We thus challenge the existing conflict typology, as did Khanin and Turel (2015). We therefore contribute to the literature on conflict management in VC-OM relationships by empirically showing the importance of tension management mechanisms in order to understand the origins and consequences of ill-managed cooperation. We also demonstrate that, beyond the nature of the conflict—cognitive vs. affective, pacing vs. prerogative (for example Brettel, Mauer, and Appelhoff 2013; Higashide, and Birley 2002; Khanin, and Turel 2015; Zacharakis, Erikson, and George 2010) —, tension intensity also determines the detrimental vs. beneficial effects of tension. As our case study demonstrates, conflicts are unanimously considered by VCs and OMs as detrimental. However, so are situations that lack constructive arguments, that is tension.

Collaborations so peaceful or harmonious that they are bereft of critical events are commonly considered worthless. *Talking continuously* and *strengthening operational focus* sometimes entail tensions that benefit the venture. In other words, productive interactions are not synonymous with frictionless relationships. Preserving conditions for nourished interactions is indeed an explicit concern of both VCs and OMs. Following Eisenhardt, Kahwajy and Bourgeois III (1997) and Zacharakis, Erikson and George (2010), we suggest that there is an appropriate, *well-balanced* level of tension: neither zero nor too high. Tension that remains at low and moderate intensity levels ensures long-term exchanges of ideas without dysfunctional consequences, which is key to innovation and success (Stark 2009). Tension also improves the quality of decision-making processes by allowing different options to be considered (Eisenhardt, Kahwajy, and Bourgeois III 1997). This is the case at e-MARKETING, where tension levels were low but where exchanges between the VC and OM did not preclude contradictory points of view that were perceived as enriching their mutual understanding of the venture's future.

“We [OM & VC] had a meeting together two weeks ago, [...] among the possible development strategies for the company, we think about growing internationally. [...] I prepared a business plan, a financing strategy and so on and so forth and I asked him [ALPHA VC] about his opinion. He may well answer ‘I believe that you are mistaken here and there’ and his point of view will be important and useful to me.” (e-MARKETING OM)

As illustrated in Figure 1, the four mechanisms described in the “results” section are used to initiate and maintain this productive level of tension while preventing tension escalation.

[INSERT FIGURE 1 ABOUT HERE]



Our third finding is that VCs and OMs both actively seek to manage tensions in their relationship. This result confirms previous findings on VCs’ active behavior when managing tensions with their portfolio of ventures (Parhankangas, and Landström 2004), and extends them to entrepreneurs. Adopting both the VC’s and the entrepreneur’s perspective (as advocated by studies such as that of Zacharakis, Erikson, and George 2010) provides a better understanding of tension management practices as *a reciprocal dynamic relying on behavioral expectations from both sides*. Khanin, and Turel contend that “to prevent conflict escalation or the eruption of prerogative conflicts, CEOs could benefit from acting proactively and cooperatively in order to improve their rapport with VCs” (2015, p. 957). We extend their argument by asserting that both parties are responsible for conflict prevention. Our research demonstrates that VCs, like entrepreneurs, constantly try to behave according to their partner’s expectations and that these behaviors (described in the four mechanisms identified) are

powerful tension management mechanisms. This study notably finds that entrepreneurs demonstrate a *strengthened operational focus* and willingly *endorse difficult decisions* when facing critical events to avoid being perceived by VCs as shirking or opportunists. VCs also behave very actively to *avoid* creating disappointments on the entrepreneur side, which suggests that disappointments in the relationship can stem from either partner. The cooperative dynamic is reciprocal in the sense that each partner keeps observing the other one and remains cooperative as long as the other follows the same path. Some behaviors (such as *strengthening operational focus* and *accepting difficult decisions*), implemented when critical events occur, are clear signals of non-opportunistic behavior from the partner. Other behaviors (like *talking continuously* or *showing commitment to a community*) fulfill an anticipative function: they allow one partner to anticipate that the other one will behave as expected should a critical event happen—for example, from the VCs perspective, that the entrepreneur is expected to keep sharing information even if the firm’s results deteriorate sharply. “Cooperative goals” (Tjosvold, and Weicker 1993; Tjosvold 1998a) are thus not “given” features of partners involved in a specific relation but are socially constructed by actors in a diachronic and enduring process through the four mechanisms described in the paper.

Finally, our last finding is that VC-OM tension management practices are, like all social relations (Granovetter 1985), deeply embedded in their social context. It is indeed known that VCs and entrepreneurs’ behaviors ought to be understood as embedded (Ferrary, and Granovetter 2009; Granovetter 1985; Sorenson, and Stuart 2001; Tjosvold, and Weicker 1993). This conclusion also applies to VC-OM tension management practices. Our research shows how VCs and entrepreneurs are embedded in a dense network of close ties with other VCs and local entrepreneurs (that is, they have frequent interactions) and are more inclined to implement active tension management behaviors as depicted in our four mechanisms. Such active behaviors are motivated by both actors’ anticipation of future investment or general business

deals and the will to avoid tarnishing their reputation within the community. By *showing commitment to their community*, VCs and OMs prove the acceptance of their mutual interdependence. By *talking continuously, strengthening operational focus* and *accepting difficult decisions*, they preserve their image of “good” business partner within the community, which makes future business opportunities more accessible.

Conclusion

Our aim was to understand how VCs and OMs control tension intensity in their relationships. We thus studied a venture capital firm and eleven of its ventures. We identified four mechanisms that are mobilized to manage tensions: *talking continuously, proving strengthened operational focus, accepting difficult decisions* and *showing one’s commitment to a community*. The more these mechanisms are activated to structure the relationship, the lower the tension level. Declared conflicts are therefore rare because they constitute a “form” in the Simmelian sense: an anticipated situation that the actors try to avoid.

With regard to generalizability, the main limitation of this research lies in its single-case study focus. Further research could test whether the same four mechanisms are to be found when the actors’ profiles are different (VCs in other regions, countries, with different investment policies, majority shareholders, entrepreneurs in different sectors). Future research could also operationalize the metrics related to the implementation level of the identified mechanisms in order to conduct a systematic and large sample-based analysis of their correlation with the tension intensity levels of VC-OM relationships.

We enrich the existing VC-OM conflict literature with several contributions. First, we introduce a new variable (tension intensity) and consider “conflict” as the highest level on a continuum of tensions. We also document how a cooperative style of handling tensions can be achieved, and provide evidence of the active role of both parties in managing tensions.

Our results can be translated into practical recommendations for VCs and entrepreneurs on how to avoid tension escalation. The four mechanisms presented describe behaviors each partner should adopt in order to handle tensions effectively, in critical times (*strengthening operational focus, accepting difficult decisions*) as well as in calmer times (*talking continuously, and showing commitment to a community*). If they “want peace,” VCs and entrepreneurs should “agree to keep the peace.” Specifically, to avoid detrimental situations, they should anticipate conflict and act unselfishly. They should make concessions and prove their goodwill to their partner repeatedly, not because of specific and profound affinity, but because of an awareness of their mutual interdependency.

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Table 1 – ALPHA’s investment criteria

Criteria	ALPHA choice
Investment amount	Between €500,000 and €15,000,000
Average investment time	6 years (with some cases of investments in the same venture over a period of 15-30 years).
Number of ventures in the portfolio in 2010	150 (500 since the creation of the company)
Geographical position of targeted ventures	The western region of mainland France
Targeted economic sectors	None in particular, although it tends to avoid IT
Size of targeted ventures	Turnover between 5 and 100 million Euros
Required performance to qualify for investment	Profitable for a few years

Table 2 - Description of the eleven firms studied

Firm Name	Business/products	Date of creation	Dates of ALPHA entry in capital	No. of employees	CEO type	ALPHA Investment (in Euros)	Capital owned by the CEO (in %)	Capital owned by ALPHA (in %)	Capital owned by mgt. (in %)
POLYSTYRENE	Polystyrene for construction	1977	2001	152	Takeover ^a	4,940,000	44	28	-
PUBLIC WORKS	Public works (especially sports grounds)	1966	1988 & 2007	250	Founder	721,000	34	11	33
EXCEPTIONAL TRANS	Industrial exceptional transportation	1995	2006	2400	Founder	13,875,000	51	14.6	10
N-PRINT	Numeric printing	2001	2001	67	Takeover	183,000	55	27	18
AD-PAPERS	Advertising on paper and plastic bags	1976	2003	135	Transmission (2003)	1,379,000	45	44	11
e-MARKETING	Interactive relational marketing	1999	2000	35	Founder	210,000	>50	18.5	-
DOORS	Doors for individual houses	1995	2007	500	Takeover	15,350,000	57	8	10
ELECTRIC CORP	Electric engineering	1991	2008	230	Founder	4,900,000	70	20	10
FUNERAL	Funeral accessories & fashion accessories	1981	1994 & 2002	360	Takeover	1,279,000	52	31	-
WINE	Wine production	1912	2007	80	Transmission (2007)	6,500,000	75	25	-
HOME DECOR	Home decoration goods	1833	1981 & 2002	450	Transmission (2002)	595,000	90	10	-

Sources: interviews and ALPHA activity reports.

^a Unlike “transmission,” a “takeover” occurs when an entrepreneur buys the company without being a former employee

Table 3 – Critical events in VC-OM relationships

Event	Firm	Event Year	Event description	Tension Level ^a
1	POLYSTYRENE	2002	External Growth – acquisition of A	Low
2	POLYSTYRENE	2003	External growth – acquisition of B + accidental fire in B	Low
3	POLYSTYRENE	2005	External Growth – acquisition of C	Low
4	POLYSTYRENE	2006	External Growth – acquisition of D + restructuring of D	Low
5	POLYSTYRENE	2006	Exit of some individual shareholders	Low
6	POLYSTYRENE	2006	Extension of the main plant	Low
7	POLYSTYRENE	2006	Concentration of the sector + scissors effect between selling prices and costs: takes time for VC and OM agree to stop current projects	Moderate
8	POLYSTYRENE	2006	ALPHA wants to sell its shares urgently– OM refuses	High
9	POLYSTYRENE	2006	ALPHA demands that OM sell a subsidiary – OM refuses	High
10	POLYSTYRENE	2007	Difficult meetings – OM ignores ALPHA’s request to divest	High
11	POLYSTYRENE	2008	Better relations but ALPHA still wants to sell and OM refuses	High
12	POLYSTYRENE	2008	OM wants to change subsidiaries’ names – ALPHA refuses and OM finally abandons this project	Moderate
13	POLYSTYRENE	2010	Results below expectations	Low
14	POLYSTYRENE	2010	OM wants to grow externally - ALPHA refuses	High
15	PUBLIC WORKS	2007	Financial rate of convertible bonds – OM reluctantly agrees to abide by the shareholders’ agreement	Moderate
16	PUBLIC WORKS	2007	MBO & discussions about the valuation of ALPHA’s shares	Low
17	PUBLIC WORKS	2007	OM wants ALPHA to forgo its dividends for a while – ALPHA accepts	Low
18	EXCEPTIONAL TRANS	2008	New investment round – long debates on exit prices	Moderate
19	EXCEPTIONAL TRANS	2009	Company facing macro-economic crisis requiring cost-killing plans	Low
20	N-PRINT	2004	Disagreement on OM’s remuneration –VC finally accepts	Moderate
21	N-PRINT	2007	ALPHA urged the OM to make an OBO – ALPHA finally gives up	Moderate
22	AD-PAPERS	2005-2008	Legal changes leading to industrial changes	Low
23	e-MARKETING	2002	Dot.com crisis and OM is reluctant to sack the R&D dept.	Moderate
24	DOORS	2007	OM challenges quality of ALPHA feedback on financial reporting	Low
25	ELECTRIC CORP	2009	OM disappointed by a contact given by ALPHA – ALPHA did not immediately notice it	Moderate
26	FUNERAL	2004	New shareholders ask for new organizational structure	Moderate
27	FUNERAL	2005-2006	ALPHA demands the sale of a subsidiary, OM is initially reluctant to proceed	Moderate
28	FUNERAL	2006	ALPHA calls for the OM to sell the historic business of the group – OM accepts	Low
29	FUNERAL	2002-2006	OM wants to renegotiate ALPHA’s priority dividends – ALPHA is unwilling	Moderate
30	FUNERAL	2008	ALPHA demands that OM sell a subsidiary – OM accepts	Low
31	FUNERAL	2007-2009	Bad results and firing of OM family members	Low
32	FUNERAL	2011	CEO preparing his succession	Low
33	FUNERAL	2011	Question about the opportunity to participate in an MBI	Low
34	WINE	2007	Recruitment of an accounting chief officer following ALPHA’s investment	Low
35	WINE	2008	Disagreement between OM and a board member introduced by ALPHA – It takes time before the board member resigns	Moderate
36	HOME DECOR	2002	OM’s succession – negotiation of ALPHA exit and entry tickets	Low
37	HOME DECOR	2005	Strong increases in raw materials prices	Low
38	HOME DECOR	2005	Foreign direct investment – ALPHA is very pushy at first and finally accepts the OM’s decision not to persist	Moderate
39	HOME DECOR	2006	Need to make a strategic decision triggered by opportunity to become sub-contractor of a big industry player	Low
40	HOME DECOR	2010	External Growth	Low

^aTension levels were assessed by interpreting materials collected during the interviews. We considered critical events that led quickly to a consensus to be “low tension events”; those requiring more time to be settled by an agreement as “medium tension events”; and those leading to a decision taken despite declared opposition from the partner as “high tension events.”

Table 4 - Tension levels across firms

Name	No. of events	Low tension	Moderate tension	High tension	Tension score	Years in ALPHA portfolio	Average tension score	Overall tension level ^a
POLYSTYRENE	14	7	2	5	26	9	2,9	HIGH
PUBLIC WORKS	3	2	1	0	4	22	0,2	LOW
EXCEPTIONAL TRANS	2	1	1	0	3	4	0,75	LOW
N-PRINT	2	0	2	0	4	9	0,4	LOW
AD-PAPERS	1	1	0	0	1	7	0,1	LOW
e-MARKETING	1	0	1	0	2	10	0,2	LOW
DOORS	1	1	0	0	1	4	0,3	LOW
ELECTRIC CORP	1	0	1	0	2	2	1	MEDIUM
FUNERAL	8	5	3	0	11	16	0,7	LOW
WINE	2	1	1	0	3	3	1	MEDIUM
HOME DECOR	5	4	1	0	6	29	0,2	LOW
	40	22	13	5				

^a With average tension scores below 1, the overall tension level is considered as low. Scores between 1 and 2 are considered medium, while scores above 2 are defined as characteristic of high overall tension levels.

Table 5 – Tension management mechanisms

	Used on a permanent basis		Used in situations of growing tensions		
	Talking continuously	Showing commitment to a community	Strengthening operational focus	Accepting difficult decisions	Mechanism implementation level ^a
POLYSTYRENE	0	+	0	+	LOW
PUBLIC WORKS	+	++	+	0	MEDIUM
EXCEPTIONAL TRANS	++	+	++	+	HIGH
N-PRINT	++	++	+	++	HIGH
AD-PAPERS	+	++	++	+	HIGH
e-MARKETING	++	+	++	++	HIGH
DOORS	+	++	++	++	HIGH
ELECTRIC CORP	+	0	+	0	LOW
FUNERAL	++	++	+	++	HIGH
WINE	++	0	+	++	MEDIUM
HOME DECOR	++	+	++	++	HIGH

^aWe measure *mechanism implementation* by summing the “+”s attributed to each mechanism: intensity of between 0 and ≤2 intensity was considered LOW; between 2 <and ≤5 is MEDIUM; and above 5 is HIGH.

Table 6 - Illustrations of the “talking continuously” mechanism

Company	Example	Mechanism implementation level
EXCEPTIONAL TRANS	Private formal meetings between investors and the executive committee took place every month. 16 pages of indicators on cash, margins and backlog with accompanying comments were transmitted ahead of the discussions. <i>“You cannot work with some debt and other people’s money and not care about what they want. You must be absolutely transparent about figures.”²</i> The OM willingly went beyond communication requirements mentioned, for example, in the shareholders’ agreement.	HIGH ++
e-MARKETING	Regular quarterly reporting was required by the shareholders’ agreement, and gradually abandoned in favor of informal face-to-face or phone communication on an irregular but frequent basis. <i>“In the shareholders’ agreement, it is explicitly mentioned that I must report to them every quarter... It is not so formal anymore because we communicate often enough without that ... I often meet [VC] as we see each other in several different networks.”</i>	HIGH ++
ELECTRIC CORP	The OM felt that, with a venture experiencing a 25% increase in annual revenues for several years on a booming market, he did not need extensive information or advice from ALPHA. Reporting was required every six months. Yet some informal encounters could take place between quarterly meetings, as the OM explains: <i>“I sometimes meet [VC] now and then. We get on well together.”</i>	MEDIUM +
POLYSTYRENE	At the time of the study, communication between ALPHA and POLYSTYRENE was not as casual and friendly as it used to be but took place at set intervals and through formalized channels only. <i>“We used to call some of our informal meetings ‘board meetings’ by stating afterwards that we had held a board meeting to take such and such decisions [...]. Our discussions used to be quite informal. Now on the contrary, they [ALPHA] have become very strict on formalism. It is unthinkable to have a board meeting without prior invitations and without an agenda.”</i>	LOW 0
ALPHA	Changes in the mode of cooperation reflected the escalation in tensions between ALPHA and POLYSTYRENE. Emails replaced phone calls as it became important for both parties to leave a trail or evidence of their interactions. VCs tried to keep regular contact with all the OMs they worked with. What was important for them was to be confident they could detect difficulties early. A solution was to ask for formal reporting at first and then to adapt according to the relationship with the OM. <i>“It’s very important at first to get good quality reporting, to structure future exchanges of information. If it is not done within the first two years, it is then much more difficult to implement in case of trouble.”</i> All opportunities to keep in contact were subsequently taken. <i>“We send them some articles, when there is something new we give them a phone call. It is not a daily relationship but a relationship that we try to manage correctly over time.”</i>	HIGH ++

² Original quotations are in French. They have been translated into English in the tables.

Table 7 - Illustrations of the “showing commitment to a community” mechanism

Company	Example	Mechanism implementation level
N-PRINT	<p>The CEO was willing to provide pieces of advice for free to other entrepreneurs in ALPHA’s portfolio. <i>“I’d personally already helped [ALPHA] in the past. I gave a hand to a venture on a topic that I knew well [...] That’s how it works, we are a club.”</i> He personally benefited from the close relationships between OMs who share the same investor. Having a partner in common opened numerous doors and nourished a fruitful network of professionals. On a quarterly basis, face-to-face encounters were organized between OMs of the portfolio, who got to know each other. <i>“ALPHA’s entrepreneurial day is a very nice initiative. They organize it about once per quarter. I don’t attend all of them as it would take too much time, though. It is an opportunity to present one’s company. There is a nice atmosphere and you get to make connections.”</i></p>	HIGH ++
DOORS	<p>At the heart of the 2008-2009 economic crisis, OM made a special effort to preserve the reputation of the ALPHA CEO, who had agreed to pay a high price to enter DOORS’ capital. <i>“I considered that I had strong commitments toward him [ALPHA CEO]. We made a deal together and I consider it my duty to see that he is not losing anything because of it.”</i> OM had known ALPHA CEO for more than 10 years. They belonged to the same executive managers’ union, and the two men had become friends. The company where ALPHA CEO used to work before ALPHA had also invested in DOORS.</p>	HIGH ++
AD PAPERS	<p>For the OM, it was unacceptable to assert the predominance of his own interest over the company’s future. <i>“[A national PE investor] offered me the possibility of taking 20% of shares while they took control of the remaining capital. They said to me ‘you have five years to boost this firm, then we sell it together so that you get some money and retire to do whatever you want.’ As you may have guessed already, I wasn’t particularly motivated by the proposal.”</i></p>	HIGH ++
POLYSTYRENE	<p>Being part of the same regional business community and sharing a common attachment to local economic networks was sometimes clearly stated as an important criterion for choosing investors. Between members of the community, having conflicting relations was almost unthinkable for the OM. Serious measures of concealment were therefore taken to keep conflicting relations away from public attention. <i>“[ALPHA] often organizes gatherings between OM. On specific occasions they organize site visits and discussions. Until 2005 I used to be invited on a regular basis and I was attending some of them. Since 2006, as our crisis dates back to 2006, I have not been invited once.”</i></p>	MEDIUM +
ALPHA	<p>ALPHA was very active in various business networks from the region and they nurtured their contact with local managers as well as local organizations such as Chambers of Commerce, professional bodies, business and philanthropic circles etc. <i>“Considering ALPHA’s history, it is very unlikely that an OM has never heard about us. When we try to contact one of them directly, this explains why they usually are not reluctant to open their door and welcome us.”</i> This strategy became less effective as distance grew. <i>“The further you get from [ALPHA HQ city] the less [ALPHA] is known.”</i></p>	HIGH ++

Table 8 - Illustrations of the “strengthening operational focus” mechanism

Company	Example	Mechanism implementation level
EXCEPTIONAL TRANSPORT	<p>When the firm faced a sharp fall in revenues in 2009 (critical event 19), the reaction of the two owner-managers was to postpone external growth plans and to concentrate on measures with immediate effects. They also looked for ways to reduce operational expenses and sought new commercial contracts. This behavior was greatly appreciated by investors, who supported these efforts to tackle immediate challenges at hand.</p> <p><i>“Now, we really are on a strict diet. We are running after savings on a daily basis [...] Personally, I am glad we finally have no external growth this year, it is a chance to get back to the actual business.”</i></p>	HIGH ++
HOME DECOR	<p>Steady erosion of commercial margins had been impacting the company’s low-end products (critical events 38 and 39). ALPHA began intense discussions with the OM about possible off-shoring solutions. On this occasion, ALPHA helped the OM—dedicated to solving the critical situation but initially reluctant to execute the off-shoring project—to make up his mind about what to off-shore and what not to off-shore.</p> <p><i>“At ALPHA they listen and they give advice as well. Five years ago we built a production unit in Tunisia. ALPHA really helped us make up our mind regarding the project. [...] They told us ‘carry on, don’t be afraid, we have feedback from other ventures in such and such businesses and they are successful.’ It is reassuring to be supported by ALPHA”</i></p>	HIGH ++
FUNERAL	<p>In critical situations triggered by merger projects and economic difficulties, both partners demonstrated a surge in time and energy dedicated to the venture. Interactions took a flexible turn and showed the individuals’ commitment.</p> <p><i>“We meet [ALPHA investment manager] every week these days because of the current [merger] projects [...] I’ve called her once or twice, I’ve already sent her a memo. We keep sending each other memos, it is very, very flexible.”</i></p>	MEDIUM +
POLYSTYRENE	<p>The OM wanted to overcome financial difficulties by acquiring a distressed business in a new industrial sector (critical event 14). He scrutinized the plan until he was convinced it was realistic before mentioning it to his VC, who was taken by surprise by the project, and took it as a major breach of confidence. The OM’s plan was considered a mistake by investors: in their view the OM was not demonstrating strengthened operational focus but was instead getting distracted by fanciful growth projects. ALPHA then refused to grant the OM the authorization to proceed.</p>	LOW 0
ALPHA	<p>The VC paid a lot of attention to showing its commitment when contacted by OM or when situations became problematic. It knew that on these occasions it needed to show great dedication to the venture and be a valuable support to the OM.</p> <p><i>“You get more involved in companies that are asking you for advice and in those where help is needed. [...] When there are strategic or financial issues... here we are! We give our opinion during crises or during business transformations involving large investments, mergers, etc. We are present and we talk with the OM.”</i></p>	HIGH ++

Table 9 - Illustrations of the “accepting difficult decisions” mechanism

Company	Example	Mechanism implementation level
e-MARKETING	<p>In 2002, e-MARKETING went through financial turmoil during the dot.com crisis (critical event 23). The company needed extra financial liquidity to cope with daily operations. The owner-manager found ALPHA unwilling to take part in a new round of financing. ALPHA also insisted on the need to cut costs by closing down the firm’s R&D department. Despite his initial reluctance, the owner-manager agreed to close his R&D department. ALPHA therefore agreed not to cash in its convertible bonds and to postpone the payment of some of the financial interest.</p>	HIGH ++
FUNERAL	<p>The OM’s brother headed one of the subsidiaries. When the subsidiary’s performance started to deteriorate, some thought that managerial problems were to blame. Both partners made concessions to solve this critical situation: the OM finally made the painful decision to fire his own brother for the sake of the firm. Although the cause of the trouble seemed obvious, ALPHA gave the OM time to solve the situation. They merely put him in contact with an HR consulting firm, which conducted a management audit and came to the conclusion that the brother was the main problem.</p> <p><i>“ALPHA dealt with the issue very delicately because they knew my own brother was involved and that it was not an easy decision to make. (...) I owe to [ALPHA VC] the fact that this HR consulting company conducted an audit, which involved interviews with a dozen key interlocutors. Its conclusion was that my brother was part of the problem. ALPHA never said to me ‘you have to fire your brother’.”</i></p>	HIGH ++
POLYSTYRENE	<p>Because of explicit disagreement between the OM and ALPHA regarding an external growth project (critical event 14), both partners made concessions. Although he could have proceeded without his investors’ explicit consent, the OM finally decided not to carry on with the acquisition, knowing it would exacerbate opposition. He remained, in his own words, “downhearted” but “reasonable.” Despite the open conflict with the OM, ALPHA decided not to use their convertible bonds to gain the voting power to fire him.</p>	MEDIUM +
ALPHA	<p>ALPHA VCs mentioned the importance of keeping good relationships with the OM even during the exit. ALPHA was willing to forgo the maximization of their investment to maintain peaceful relations.</p> <p><i>“We won’t sell our shares at a lower price than what we paid initially, we will try to get a good NPV, but I want to say that if our NPV is 19.5% and not 20%, we will be very happy with it. We will not be ‘greedy’.”</i></p>	HIGH ++

Table 10 – Mechanism implementation level and tension level convergence

	Tension level	Mechanism implementation level	Convergence between the 2 indicators
POLYSTYRENE	HIGH	LOW	Convergence
PUBLIC WORKS	LOW	MEDIUM	Partial convergence
EXCEPTIONAL TRANS	LOW	HIGH	Convergence
N-PRINT	LOW	HIGH	Convergence
AD-PAPERS	LOW	HIGH	Convergence
e-MARKETING	LOW	HIGH	Convergence
DOORS	LOW	HIGH	Convergence
ELECTRIC CORP	MEDIUM	LOW	Partial convergence
FUNERAL	LOW	HIGH	Convergence
WINE	MEDIUM	MEDIUM	Convergence
HOME DECOR	LOW	HIGH	Convergence