The relationship between the early stage venture capital funds and portfolio entrepreneurs in Finland – Structuring of the initial deal and exploring the post-investment relationship

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**Abstract:**

This empirical research takes a closer look at the relationship between early stage venture capital funds and their portfolio entrepreneurs in Finland. The research looks at classic venture capital theory, venture capital contract theory, agency theory and self-determination theory to resolve the mysteries structuring the initial deal and exploring the post-investment relationship. The research is conducted through 4 dyad studies of Venture Capital Fund representatives and portfolio entrepreneurs in Finland. The dyad study is unique to this research area, since previous venture capital theories focus more on the investor’s perspective (Söderblom, 2016). The research ultimately resulted in an interesting discussion, finding key themes through a thematic analysis of the empirical material. The research demonstrates empirical, theoretical and practical contributions, which can be useful for any party, interested in understanding the relationship between the early stage venture capital fund and portfolio entrepreneur in Finland. In addition to the planned contributions, the research resulted in having an additional theoretic and methodologic contribution.

**Keywords:** Finland, venture capital, early stage, entrepreneur, autonomy, control, agency theory, venture capital contracts, self-determination theory, dyad study
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Sammandrag:
Denna avhandling undersöker förhållandet mellan tidiga skedets venturekapitalfonder och deras portfoliebolag, i en finsk kontext. Undersökningen använder sig av klassisk venturekapitalteori (Sahlman, 1990), venturekapitalkontraktteori (Kaplan & Strömberg, 2003 & 2004), agentteori (Eisenhardt, 1989) och självbestämmandeteori (Ryan & Deci, 2000). Forskningsfrågorna som undersöks är: (1) Vilka är de essentiella kontraktdetaljerna i strukturenderandet av den initiala venturekapitalinvesteringen i finska tidiga skedets bolag, (2) vad är balansen mellan autonomi och kontroll i förhållandet efter att den initiala investeringen har skett i Finland och (3) för de venturekapitalfonder och entreprenörer som gör sin initiala tidiga skedets investering, vilka är de praktiska implikationerna i Finland? Undersökningen är kvalitativ och har gjorts genom semi-strukturerade intervjuer (Bryman & Bell, 2011). Metoden för undersökningen var en dyad (Söderblom, 2016). En dyadstudie innebär att man undersöker ett förhållande mellan två parter och tar bådas åsikter i beaktande i undersökningen (Söderblom, 2016). Metoden är unik och har visat sig vara nyttig i denna undersökning eftersom tidigare forskning har fokuserat starkt på endast placerares perspektiv (Söderblom, 2016). Resultatet av den empiriska studien analyserades genom en tematisk analys, samt med inspiration av gioiometoden för att hitta nyckelman från intervjuerna (Braun & Clarke, 2006; Gioia et al, 2012). Slutligen diskuterar avhandlingen de olika identifierade nyckelman från den empiriska undersökningen och besvarar slutligen alla forskningsfrågor. Utöver den teoretiska kontributionen från avhandlingen har undersökningen visat en ytterligare teoretisk och metodologisk kontribution genom dyaden samt praktiska implikationer för vilken som helst intressent av tidiga skedets venturekapital investeringar i Finland. Slutligen har avhandlingen även hitta flera intressanta ämnen, som tangerar teman i denna avhandling, att vidareundersöka.
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1 INTRODUCTION

After the fall of Nokia during the IT Boom in the early 2000’s, Finland was greatly impacted, and as a result IT-talents scattered into the Finnish economy (Stifted, 2019). The combination of IT specialists and eager young entrepreneurs, has created many scalable IT related ventures, which today are world renowned (ibid.). What all these have in common, is that in order to scale the ventures, they need an aggressive amount of money injections to scale the company at a maximum phase. These money injections are done by venture capital (Abbreviation: VC) funds, which bet their money on expendable ventures, in the hopes of high returns. This phenomenon is still ongoing and growing today, placing the Finnish economy in the lead in Europe, with most venture capital invested in early stage startups compared to GDP (Finnish Venture Capital Association, 2019). The growing significance of early stage startups and venture capital investments relative to the economy makes it relevant to research further within the field (Finnish Venture Capital Association, 2019).

Previous research about venture capital is vast. However, there are still research gaps to be filled. Kelly (2000) concludes and proposes a clear call-to-action for further research regarding the relationship between structuring the VC relationship and post-investment risk management. The call-to-action is explicitly cited on page 213. This citation presents a clear theoretical gap to be researched:

“Irrespective of whether the venture capital fund invests at the same time with private investors or chooses to invest at some point in the future after them, a number of interesting issues remain largely unresolved to date. Do venture capitalists and private investors operate differently with respect to their approach to structuring their relationship with the entrepreneur and managing risk post investment?”

The first question that rises from Kelly’s (2000) call-to-action is how the VC fund and portfolio entrepreneur’s relationship is structured (ibid.). In addition to the structuring, Kelly (2000) brings up a second problem to be further researched, which is managing post-investment relationship. Kelly’s (2000) call-to-action has not been studied in a Finnish context. With the rising relevance of early stage VC and startups in Finland, the context is matching (FVCA, 2019; Stifted, 2019).

Previous theories about structuring and post-investment relationship between the early stage VC fund and entrepreneur is based on the contracts they have between them, setting the boundaries and rules (Kaplan & Strömberg, 2003 & 2004). The contracts define the level of control and autonomy in the relationship. In previous research
regarding VC relationships, the most commonly used theory is agency theory (Eisenhardt, 1989; Kelly, 2000, Kaplan & Strömberg, 2003 & 2004). Agency theory researches how to minimize the negative effects and costs of a relationship, in this context between the VC and entrepreneur. Regarding contracts, agency cost is measured through the financing round related contracts (Kelly, 2000). Advocates of agency theory propose that a certain amount of control needs to be applied to optimize the outcome of the relationship (Eisenhardt, 1989).

In contrast to advocates of agency theory, Ryan & Deci (2000) argue that the best productivity and sense of well-being is achieved by full autonomy and intrinsic motivation. According to Ryan & Deci (2000), this means that giving up any autonomy results in increased negative result. This approach is new, using Ryan & Deci’s (2000) self-determination theory within the context of venture capital. The study will look at VC contract theory, previous agency theory propositions and finally apply self-determination theory to create the discussion of managing post-investment relationship through balancing autonomy and control (Eisenhard, 1989; Ryan & Deci, 2000; Kelly, 2000).

Moreover, relationship studies about VC are usually over-reliant on the investors side of the relationship (Macht 2011, Collewaert, 2012). That is why this research will employ a unique method and perform a dyad study, which means interviewing both the VC fund representatives and their portfolio entrepreneur (Söderblom, 2016). Like in Söderblom et als (2016) research, this method exceptionally incorporates the additional viewpoint the entrepreneur, which provides a much more nuanced understanding of the relationship between the investor and the entrepreneur (ibid.).

This research aims to broaden theory about structuring the initial VC deal of early stage companies and exploring the post-investment relationship between the VC funds and portfolio entrepreneurs in Finland (Finnish Venture Capital Association, 2019). As presented in the figure below, this research will use contract theory, agency theory, self-determination theory and the dyad study to solve the problem area. The aim of this research is mentioned in table 1 below.
Table 1, Aim of the research

<table>
<thead>
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<th>Aim 1</th>
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<td>Empirical</td>
<td>Theoretical</td>
<td>Practical</td>
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<td>The empirical aim of the research is to create insight regarding the essential details about structuring the initial deal in Finland. This would include exploring the process and contracts, which are essential in the deal structuring (Kaplan &amp; Strömberg, 2003 &amp; 2004)</td>
<td>The theoretical aim of the research is, with the help of earlier studies, to perceive how venture capital investments are structured and furthermore explore the post-investment relationship (Kelly, 2000; Ryan &amp; Deci, 2000).</td>
<td>The practical aim of the research would be to chart practical implications for early stage venture capital funds and entrepreneurs going into their initial deal.</td>
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The research questions are defined as the following:

1.1 Research questions

RQ1: What are the essential details in structuring the initial contract between early stage venture capital funds and entrepreneurs in Finland?

RQ2: What is the post-investment balance of autonomy and control between early stage venture capital funds and their portfolio companies in Finland?

RQ3: For early stage venture capital funds and entrepreneurs going into the initial funding round, what are the practical implications in the context of Finland?
1.2 Boundaries to the study

The figure above presents the problem area and the components that set the boundaries of the study. The empirical study will be conducted as an abductive study, assisted by semi-structured interviews (Bryman & Bell, 2011; Söderblom, 2016). The abductive study has allowed this research to bounce back between empirical material and theory to create the best possible outcome (Bryman & Bell, 2011). This research will end up
broadening the understanding of early stage venture capital theory, early stage entrepreneurs and provide practical implications based on the study.

Bengtsson & Sensory (2009) conducted research on the evolution of the venture capital contracts. They suggest that the nature of the term sheet and shareholder agreement is largely dependent if contracts are conducted for an initial money injection or follow-up financing (ibid.). The initial structuring is well dependent on which stage the company is in, which makes it logical to research only early stage VC funds and portfolio entrepreneurs (ibid.). Since the contracts are the most defining control mechanisms of the relationship in practice, the dynamics of the relationship may change depending on the contracts (Kelly, 2000; Bengtsson & Sensory, 2009). More specifically, Sensory (2009) mentions that both the contracts and the relationships are different, depending on if the funding is about the initial money injection or a follow-up round (ibid.). This research examines the initial money injection round.

1.3 Definitions

The formal venture capital market: Formal VC is defined by Crispin-Little & Brereton (1989) as private or public organizations or people granting a set amount of capital to a professional company, more namely, the VC fund (Crispin-Little and Brereton, 1989). In Finland it is usually in the corporate form of a “Kommandiittiyhtiö”. The VC company strives to maximize the profit compared to the base investment (ibid.). VC funds may have different investment focus areas, like B2B software, health technology and so forth (Finnish Venture Capital Association, 2019). In general, VC money is used to exponentially grow the company (Sapienza, 1996).

Agency Theory: Agency theory in this context is mainly based on Eisenhardt’s (1989) research. Agency theory analyses the relationship of the principal and agent. The principal in this case is the VC fund and the agent are the portfolio entrepreneur. The agent theory analyses the negative effects and costs of starting and maintaining a relationship (ibid.).

Self-determination theory: Ryan & Deci (2000) cover three different types of motivation in their self-determination theory. Amotivation, extrinsic motivation and intrinsic motivation. They argue that intrinsically motivated and autonomously operating people have the highest productivity and sense of well-being (ibid.)
External regulators: External regulators are a part of the extrinsic motivation (Ryan & Deci, 2000). The external regulators are compliance, punishments and external rewards. In this research, the external regulators are the contracts (ibid.).

Control: Control in this research is mostly based mostly on Kelly’s (2000) and Kaplan & Strömberg’s (2000 & 2004) views on the contractual perspective of the relationship. This research later presents different contractual mechanisms that will problematize the ways of controlling the relationship in practice (ibid.). Control is defined foremost by majority of shares, share votes and board control.

Autonomy: Autonomy will be used in this research according to Ryan & Deci’s (2000) context. Ryan & Deci (2000) propose that the more autonomy a person or organization has, the more intrinsic motivation one has and the more intrinsically motivated one is, the better sense of well-being and productivity you have. Autonomy is in this research foremost defined as having majority of shares, share votes and board control.

Balance: Balance remained undefined in this research until the empirical research was conducted. The level of balance is one of the core questions to be explored in this research.
2 VENTURE CAPITAL

Venture capital, abbreviated as VC in this study, is the money which is used to help grow companies fast (Sahlman, 1990). The injected amount of money in the growing company is done by VC funds and are high risk investment objects (ibid.). VC funds raise money from institutions, individual parties and others to invest in high risk business but offers high potential pay-off (Sahlman, 1990). This research will mainly use Sahlman’s (1990) book on classic venture capital theory.

The increasing significance of early stage venture capital backed companies, makes it interesting to research the relationships in this context to further understand the welfare of the economy (Birch, 1981; Acs et al, 2008; Stifted, 2019; Finnish Venture Capital Association, 2019). Birch (1981) mentions that continuously studying relationships within the venture capital field is essential.

2.1 Venture capital funds in general

The hard fact about starting a new venture is that majority of the companies fail (Bygrave, 1994). The VC funds need a few big winners to offset the losers. Most of the VC funds have many partners and different staff to support the fund, for example: partners, associates and administrative support (Sahlman, 1990). Here is a short list of general information about VC funds (Sahlman, 1990). As the table points out, the economic life of a fund is usually 10 years usually (ibid.). This draws attention to the fact that VC funds are not long-term operations, they are built with a clear goals and time limit. Table 2 also goes through basic compensation schemes and facts relating to the operations (ibid.)

<table>
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<th>Table 2, General VC fund information</th>
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<tr>
<td><strong>General VC information</strong></td>
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<tr>
<td>- The average economic life is 10 years (72%).</td>
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<td>- The usual general-partner capital contribution is 1% of the funds committed capital.</td>
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<td>- The standard compensation for managing a fund (for over 50% of surveyed companies) is 2,5% of committed capital through the whole economic life of the fund.</td>
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- 88% of the funds get 20% of the realized gains on the fund.

- The venture fund normally specializes on industry or different stages of investment. Only some VC funds focus on specific technology while others concentrate on the stage of the company.

- As mentioned earlier in the research, deal pricing is one of the key factors of success for the VC funds. Deal pricing means in practice at what valuation and investment the deal amounts to (ibid.).

- The average holding period for a VC holding is 4.9 years (ibid.). One-third are held for more than six years (ibid.).

- Two thirds of the VC funds are limited partnerships, the remaining one-third of industry capital was invested in independent capital firm forms (Sahlman, 1990). It is notable that this is according to a data set in the US (ibid.).

- Typically, the invested amount in the VC fund is invested in the first three to five years from the start of the fund (ibid.).

Bygrave (1994) emphasizes that investments do not always have to be financially profitable. Some venture capitalists reflect that they have a form of social responsibility (ibid.). This includes among other things: (1) Developing social impactful technology, (2) Generating jobs in areas with high unemployment and (3) Supporting minority entrepreneurs (ibid.) From the year of 1994 when Bygrave wrote this, “impact investing” has become quite the phenomenon, at least in Finland (Nordic Startup Guide, 2018; Sitra, 2019; Finnish Government, 2019). Several impact investing VC funds have been set up during the last year in Finland (ibid.).

### 2.2 The History of Venture Capital

According to Gomper & Lerner (2001), the very first VC company dates back to 1946. The company was established by MIT President Karl Compton, General Georges F. Doriot (Professor at Harvard Business School) and some local business leaders (ibid.). The company was called American Research and Development (ibid.). ARD made successful investments, for example a Digital Equipment Company which grew from its 70 000-dollar investment to 355 million (ibid.). During the same decade, a few other VC
companies was established. They were also closed-end funds, such as ARD. Later, the first VC partnerships/funds were formed. Among these were Draper, Gaither, and Anderson. During the 1960s-1980s, VC was reportedly highly profitable according to Sahlman (1990). For instance, between 1965 and 1984, the realized compound rate median of return exceeded 26% per year. In comparison, during the same period, Standard & Poor’s 500 yearly percentage was 16%. One third of the VC investments between 1965 and 1985 resulted though in absolute loss (ibid.).

Later in the 1980’s, VC companies started to not only invest in early stage companies, but other types of firms as well (Bygrave, 1994). VC companies invested in larger and also later stage deals, management buyout financing and as well as investing in public companies (ibid.). Sahlman (1990) conducted research that explained some general industry background of VC. Of VC, showing that 89 of the 658 largest VC backed corporations controlled 58% of the capital in general. This proves that, in 1988 it was more likely for VC to back corporations that they could control (ibid.). In the same year, 65% of the capital invested was in later-stage companies, meaning 65% of was privately held. 20% of capital was invested in leveraged buyouts or acquisitions (ibid.). The remaining 15% went to early stage companies.

Bygrave (1994) mentions in his research that in the early 1990’s, visible VC funds of the whole world managed 35 billons and invest annually 2 billons. In comparison, in the early 1990’s, IBM’s yearly R&D amount was 5 billons. Bygrave (1994) mentions that this is not a significant amount of money looking at what he calls “the grand scheme of things”. In 2018, VC investments reached 130.9 billion (Pitchbook, 2019). In Finland the invested VC money into startups reached 479 million, which represents 0.096% of the Finnish GDP (Finnish Venture Capital Association, 2019).

2.3 Venture capital in Finnish context

In addition to the history mentioned above, on a world-wide scale, this research elaborates on a short review of the VC history in Finland. Reflection in this research analysis, about the changes over time, will be supported by the history section.

Reviewing the Finnish context shortly: In the beginning of 1990s, Finland was not so well specialized in the IT industry (Lahti, 2009). 10 years ahead of that, with Nokia thriving, Finland had become one of the world’s most IT intensive countries in the world (Koski et al., 2002). Today, the majority of VC investments are made in the IT sector (Finnish Venture Capital Association, 2019).
Scandinavian culture in general strongly values equality, ensuring social security (Lahti, 2011). In comparison, the US has a more individualistically driven society, including completion and self-seeking interests rather than striving for solidarity (ibid.). Liquidity in the Finnish stock market is relatively low, especially after the IT bubble burst (Selosmaa, 2007). The banking industry in Finland is dominated by a few large players (Lahti, 2009). The low liquidity and high amount of concentration in the banking sector may imply a lack of capital in the country, which might result in low growth and economic welfare in the future. Hyytinen (2005) describes that 15 years ago the Finnish formal VC market was characterized by independent, young and small VC funds (Hyytinen, 2005). In addition to the private funding market (VC and angel investments), Finland has a variety of public funding organizations (Lahti, 2011). These include: Finnish Industry Investments ltd., Business Finland, Finnish Innovation Fund Sitra, Finnvera, The Employment and Economic Development Center and The Foundation for Finnish Inventions (ibid.).

### 2.4 Venture Capital Lifecycle

The VC life cycle is typically 10 years (Bygrave, 1994). Like business angels, VC invests know-how from organizations as well as monetary resources (ibid.) There are three different sizes of ventures that VC companies are interested in investing in: (1) Life-style (5 year projection under 10 million in revenue), (2) Middle-market (5 year projection 10-50 million in revenue) and (3) High-potential (5 year projection 50+ million in revenue) (ibid.). This research will be looking at the (1) Life-style category, defined as “early stage” in this research.

As in the figure below, this is what would be described Venture Capital cash flow. The figure presents all the involved parties in the lifecycle of the VC company and the arrows portrays the capital flow.

**Figure 2, Venture capital cash flow**
As mentioned earlier, this research focuses on the early stage investing VC funds and their portfolio entrepreneurs. Other stages are defined according to Plummer’s (1987) research, representing all the different stages of VC investing (ibid.).

1. **Early stage and seed investments**

There are many interpretations of seed stages (Sahlman, 1990). Though the consistent consensus is that a small amount of capital is given to an entrepreneur to determine if the venture is worth exploring further (ibid.). Typically, in technology ventures, one might build a prototype and test the market potential (ibid.). This stage might also include conducting market research to validate the business idea (ibid.).

2. **Startup**

During this period the company is less than one year old (Sahlman, 1990). This phase usually focuses on injecting money to product development, test marketing and prototyping (ibid.). In addition, this stage includes studying management team-building, market-penetration potential and conducting a business plan (ibid.).

3. **First stage – early development**

If the investment survives the first stage, the prototype works and the market studies look good enough, this is the next stage (Sahlman, 1990). In this stage, management is expected to establish the manufacturing process and start to set up correct quantities of production (ibid.). Companies are rarely profitable at this stage (ibid.). To clarify, this research is focusing on companies at this stage.

4. **Second stage – expansion**

At the second stage, the company has produced enough products to get real feedback from the market (Sahlman, 1990). Predictions of future market-penetrations may still be hard to estimate but at this stage, the companies are able to understand their limitations and their speed of production (ibid.).

5. **Third stage – low on cash but profitable**
During the third stage there is likelihood that sales figures grow fast therefore lowering the investment risk owing positive profit margins (Sahlman, 1990). But rapid expansion at this stage needs more capital than then company generates itself (ibid.). For instance, new manufacturing facilities that expand the market (ibid.). At this stage, banks are more likely to give larger credit, on account of the growth. (ibid.).

6. Fourth stage – rapid growth toward liquidity point

This stage is similar to the previous stage (Sahlman, 1990). The company minimizes risk with the successful growth but still needs capital to penetrate more markets (ibid.). Commercial bank credits might play a more important role here (ibid.). The company might consider IPO, acquisition or LBO, since the cash-out point is getting closer (ibid.).

7. Mezzanine investment – Bridge stage

The Mezzanine stage is where the company has a clearer idea on how to cash-out (Sahlman, 1990). In practice, this means that the VC-investors can gain liquid assets as compensations for their stake of the company (ibid.). At this stage, “IPO windows” may be open (ibid.). Some restructuring could possibly occur at this stage of the ownership and furthermore some VCs may liquidate as early as here (ibid.).

8. Liquidity stage – cash-out or exit

As the name suggests this is where VC money is liquidated into cash and further distributed to the investors of the VC fund (Sahlman, 1990). The form in which the company is liquidated is highly dependent on the term sheet that was constructed in the first investment (ibid.). This portrays how important the term sheet is, even in the last stage of the VC and entrepreneur relationship.

To summarize, it is good to remember that there are other versions of defining what stage the company is at. This research does not aim to create the best definition, but rather choose an existing one and select a stage to focus on.

2.5 The relationship between the venture capital organization and the entrepreneur

As Bygrave (1994) mentions, the fund-raising terms should be attractive to both parties to reach a deal. This is the foundation for building a working relationship between the VC fund and portfolio entrepreneur (ibid.). Sahlman (1990) points out that venture capitalists who abuse their power find it hard to attract the best entrepreneurs (ibid.).
For a successful process, Sahlman (1990) insists that it takes effort and skill from all individuals involved and certain outside control factors as well. The underlying logic of the difference between VC on private investors is that the private investors make the entrepreneurial venture “investment ready”, meaning ready for VC (Kelly, 2000; Freear et al 1990). Freear, Sohl and Wetzel (1990) were one of the first to notice the difference.

When the investment decision is made and the deal is signed, monitoring starts, which presents difficulties, as the probability to succeed is small (ibid.). Both the agent (entrepreneur) and principal (VC) in this case always have different knowledge about the venture in general (ibid.). To avoid these problems the venture capitalists set a framework and investments so they have control over their investment (ibid.). Sahlman (1990) points out that the most important mechanism for controlling the ventures are:

(1) The process of staging injection of money, in practice, the term sheet and shareholder agreement. This research looks deeper in to the process of structuring the initial injection of money (ibid.). Sahlman (1990) argues that entrepreneurs accept the term sheets and shareholder agreements because they have great confidence in meeting their targets. This implies that the entrepreneur could be over-optimistic deciding on the term sheet (ibid.).

(2) Another control mechanism that this research will be looking into, is the active level of involvement that the VC company will have with their portfolio companies (ibid.).

(3) In addition to these two, this research will also look into how VC uses the contracts to reach an agreement the entrepreneurs.

(4) Adverse selections in the contracts will also be touched upon (ibid.).

(5) The compensation schemes.

(6) Mechanisms related to liquidity.

(7) Additional implications of using convertible preferred stock.

(8) Evaluation techniques.
(9) The last topic that Sahlman (1990) mentions will also be employed in this research is: Being aware of the whole VC fund structure, which is presented in figure 3 of this research.

A typical area of interest in VC theory is the relationship between the external investors and VC fund management (Sahlman, 1990). External investors signify the organizations, meaning those organizations/people who invest in the VC fund (ibid.). In this context, conflicts arise, as the VC acts as agent and the external investors as principals (Sahlman, 1990; Eisenhardt, 1989). This is why contracts between the VC and the external investors are also important (Sahlman, 1990). For future research, this topic could be appealing to examine further.

As a side note and upcoming trend, the well-being of the VCs portfolio entrepreneurs has also become relevant to take into account (Icebreakers.vc, 2019). Icebreakers VC fund recently wrote an article about the importance of their portfolio entrepreneurs well-being (ibid.).

2.6 Structuring the venture capital deal and terms

Bygrave (1994) starts by offering a reminder that everything in life is negotiable, even the VC term sheet. In addition, he emphasizes not to go chasing VC money if one is not familiar with the terms and conditions (ibid.) The ultimate deal is where both parties feel that they have been treated fair (ibid.).

Typically, deals with VC companies start with an oral agreement (Bygrave, 1994). After this, before proceeding to binding legal documents, the entrepreneur usually receives a letter of intent and a term sheet. The term sheet is an excellent way to avoid future issues and deal killers (ibid.). The term sheet is usually just a few pages and could be compared to the table of content for the shareholder agreement. Structuring a VC term sheet comes down to four different parts (ibid.):

1. The amount of the investment
2. The form of the investment
3. The share of the equity represented the investment
4. The term sheet and shareholder agreement
The term sheet and shareholder agreements exist mainly to protect the investors from incompatible behavior according to the original deal (Bygrave, 1994). The best way for the entrepreneur to get familiar with the contracts is to go through them with a legal counselor, to ensure that every paragraph in the terms and conditions is understood (ibid.). Optimally, this is done without the pressure of a time limit due to the need for money (ibid.) As could be concluded from the empirical material of this research, there may be negative consequences for an entrepreneur on a deadline. An example of a negative consequence is having to accept an unfavorable clause in the contract. Bygrave (1994) mentions that the entrepreneur should pay particular attention to the voting rights, antidilution provisions, board seats, provisions and stock restriction agreements. (ibid.)

According to Sahlman (1990), the term sheet consists of three different characteristics and three different elements that addresses the fundamental problems. The three different characteristics are: commitment of capital with the option to jump ship, compensations systems linked to created value (sales often) and ways to make the management distribute proceeds of investments (ibid.). The three different fundamental contractual problems are: sorting (how to find the best VC funds and the best entrepreneurs), the agency problem (how to minimize present value that exists in the agency costs) and operating-cost problems (how to minimize operation-cost that exists presently, including tax (ibid.). This research examines the fundamental problem of agency cost which the contractual part brings forth.

The figure below is the Finnish Business Angel Networks investment process. This research will look specifically at the due diligence and the post-investment activity phases of the process, but in the context of VC. In this research, FIBANS investment process works as inspiration to use in the context of VC investment processes in Finland.
Figure 3, FIBAN investment process

Presentation → Chosing the companies → Due diligence → Closing discussions and valuation → Post-investment activity → Exit

Source: Finnish Business Angel Network (FIBAN, 2019)
3 VENTURE CAPITAL CONTRACTS

Kaplan & Strömberg (2000) mention, the contractual part between the VC and entrepreneur is how the relationship is controlled in practice. Eisenhardt (1989) also observes that as well that the contract is the determinant of the relationship dynamics between the VC and the entrepreneur. This chapter will investigate into Kaplan & Strömberg's (2000 & 2004) researches about venture capital contracts and Kelly's (2000) research, regarding the relationship between the informal private investor and the entrepreneur. This research does not construct or analyze venture capital contracts from top to bottom. Instead, this study assumes that the reader is familiar with a basic shareholder agreement. The aim is to find the essential details in the structuring process of the initial early stage VC deal and discuss the balance of control and autonomy in the relationship between the VC and entrepreneur. This is done from an abstraction level, not only focusing on the contractual part but rather using contracts as a tool to identify problems.

3.1 Securities

As Sahlman (1990), Kaplan & Strömberg (2000) and Gompers (2004) indicate in their research, the most commonly used type of security for a VC fund is convertible preferred stock. According to Kaplan & Strömberg’s (2000) research, 189 of 200 financing rounds used convertible preferred stock as security. Convertible preferred stock has different forms which will be presented. The first alternative is when an investor is allowed to convert the preferred stock at a specific data to common stocks (ibid.). The multiple depends according to the shareholder agreement (ibid.). Another convertible preferred stock alternative is to get discounted valuation in the next investment round (ibid.) The form is not homogenic, it is determined by on the different clauses of the contracts (ibid.).

3.2 Cash flow rights

Cashflow rights in this context, refers to a fraction of the portfolio company’s equity value that the investor (VC) and entrepreneur have a claim to (Kaplan & Strömberg, 2000). The most common way of cashflow rights are vesting stocks according to performance or time (Ibid.).
3.3 Voting rights

The voting rights in this context is the percentage of votes measured that investors and management have in corporate decisions (Kaplan & Strömberg, 2000). In practice, this means the number of votes that investors and management have according to their stock type and amount (ibid.).

3.4 Board rights

As Kaplan & Strömberg (2000) mention, board rights and seats also affect the controlling of corporate decisions. These rights are usually connected strongly to the voting rights, but they do not need to be identical (ibid.). Usually, the board seats are filled with founders, VCs and external board members (ibid.). Kaplan & Strömberg’s (2000) research notes that the median amount of board members is 6. The amount does not differ much from early stage to later stage financing rounds (ibid.).

3.5 Liquidation rights

Liquidation is one of the common theoretical security designs in a shareholder agreement (Kaplan & Strömberg, 2000). Liquidation rights states when the VC in different agreed settings are allowed to liquidate assets (ibid.). It can also be used to threaten the entrepreneur to perform or to make a business decision (ibid.).

3.6 Contingencies

Kaplan & Strömberg (2000) mention that contingencies in VC contracts are different according to different theories. Out of 200 samples of VC contracts, 41 had contingencies in their contract (ibid.). The most usual form of contingency is some kind of financial goals or indicators (ibid.). Kaplan & Strömberg’s (2000) research highlights that the control of the company is largely dependent on the performance of the company. This effectively means if the company performs well, the VC gets the monetary reward but gets less control and liquidation rights (ibid.). Compensation as an increasing function compared to the performance is also proved to be effective, since less capable entrepreneurs are willing to take the deal (ibid.).

3.7 Other terms

Other terms that Kaplan & Strömberg (2000) states as important is: (1) antidilution protection (protecting the investor from dilution in rounds that are lower than in the invested round), (2) vesting and non-compete clauses (vesting meaning earning stocks
over time, according to time or/and performance in the company) and (3) evolution of contracts over time and rounds.

### 3.8 The term sheets and shareholder agreement

The contractual part in practice usually consists of a term sheet, which is followed by a shareholder agreement (Abbreviation: SHA) (Kaplan & Strömberg, 2000). Bengtsson & Sensoy (2009) suggest that with their research the term sheet is heavily dependent on the VCs previous history in financing companies. Sensoy (2009) also suggests that the term sheet and shareholder agreement is highly dependent on the initial structuring of the contract or follow-up financing round (ibid.). For this study, the initial structuring will be focused on.

### 3.9 Contractual safeguards

Kelly (2000) concludes in his research that contractual specificity is relevant at a greater degree in four different settings when: (1) management has more relevant experience than the investors in the industry, (2) investors want active involvement to manage risk, (3) especially small sums and relatively large capital sums are at risk and (4) when the investor’s stake in the outcomes are seen as relatively high.

Kelly (2000) quantitative study asked private investors about the 10 most general contractual safeguards. The following figure presents the results of the importance of each contractual safeguard. Table 3 has three columns. First and to the left of the column is the “% rated “very important””. This is the grade of the highest importance in Kelly’s (2000) quantitative questionnaire. The two other columns show the type of investors which rated, divided into “Solo Investors” and “Syndicates” (ibid.).

**Table 3, Contractual Governance: Importance of contractual safeguards to private investors**

<table>
<thead>
<tr>
<th>% rated “very important”</th>
<th>Solo Investor (n=33)</th>
<th>Syndicates (n=61)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Investor veto rights over acquisition and/or divestitures</td>
<td>49(67)</td>
<td>71(84)</td>
</tr>
<tr>
<td>Investor approval required for strategic plans and/or budgets</td>
<td>58(76)</td>
<td>61(77)</td>
</tr>
<tr>
<td>------------------</td>
<td>--------</td>
<td>--------</td>
</tr>
<tr>
<td>Management can be forced to seek an exit by investors</td>
<td>24(27)</td>
<td>26(34)</td>
</tr>
<tr>
<td>Investor approval required to hire and/or fire senior personnel</td>
<td>18(36)</td>
<td>21(39)</td>
</tr>
<tr>
<td>Management compensation levels must be approved by investors</td>
<td>30(49)</td>
<td>48(64)</td>
</tr>
<tr>
<td>Share options may not be issued without investor approval</td>
<td>46(7)</td>
<td>57(75)</td>
</tr>
<tr>
<td>Non-compete contracts required of management upon termination</td>
<td>36(70)</td>
<td>61(75)</td>
</tr>
<tr>
<td>Investors veto rights over capital expenditure</td>
<td>30(46)</td>
<td>43(57)</td>
</tr>
<tr>
<td>Investor must countersign cheques above a certain amount</td>
<td>12(18)</td>
<td>18(26)</td>
</tr>
<tr>
<td>Restrictions on ability to raise additional debt or equity finance</td>
<td>73(88)</td>
<td>80(89)</td>
</tr>
<tr>
<td>Management equity ratchet provisions are included</td>
<td>33(49)</td>
<td>25(34)</td>
</tr>
<tr>
<td>Specific dispute resolution mechanism is agreed in writing</td>
<td>21(36)</td>
<td>28(38)</td>
</tr>
</tbody>
</table>

Kelly’s (2000) research points that the relationship between the parties seem to be much more positive and trustworthy than agency theory indicates. Kelly indicates that having VC companies involved in an investment round does not change the contractual safeguards. The contract itself though, is much more comprehensively documented.
Kelly (2000) speculates that VC funds pay more attention to the form and nature of the contract.

Close interaction with the managing team was seen as important in managing risk according to Kelly (2000). According to Kelly (2000), no formal mechanisms are set up to solve future disputes, which confirms Osnabrugge (1999) and Landström et al’s (1998) studies, saying that contracts may be incomplete and important for the relationship to prove flexibility. One of the main conclusions according to Kelly (2000), regarding the contract is the fact that it exists not to protect, but rather to promote the interest of shareholder.

Osnabrygge’s (1999) and Kelly (2000) confirm that crafting a more flexible framework for the contract is essential according to their studies, rather than creating the “optimal contract design”. Kelly (2000) also indicates that the development of the contract should be in a manner that encourages the process of raising capital for the company.

### 3.10 Meetings

Supporting Eisenhardt (1989), Kelly (2000) insists that VC companies present a value addition which is even better than informal private investors due to (1) being able to join the portfolio boards (2) making introductions to different persons of interests to the portfolio company (3) facilitating the whole process of potentially raising more capital and (4) advising timing and manner to create value. MacMillan, Kulow & Khoylian (1988) argue that according to their study, the entrepreneur perceives to contribute more the relationship than the VC fund. The private investors in Kelly’s (2000) research claim to be involved an average of 16 hours per month in the venture they invested in, half of that time face-to-face.

### 3.11 Monitoring

There is usually undefined but periodic and consequent reporting from the VC to the organizations (Sahlman, 1990). In addition to this, an annual meeting with all the general partners is held (ibid.).

A common shareholder monitoring method is through the board of directors (Fama & Jensen, 1983). When board members provide richer information, the executives of the company are more likely to behave and make decisions that are in the stockholders’ interest (ibid.) The richness of information can be measured by the with frequencies of board meetings, board members tenure length, the number of board subcommittees, the
number of board members with experience from industry and manager positions and the number of board members representing specific stakeholders (ibid.)

One of Kelly’s (2000) more interesting findings was that two out of three investors preferred to rely on the relationship between the entrepreneur rather than setting contractual safeguards. Kelly’s (2000) interpretation of the findings showed that the contractual safeguards existed to clarify mutual behavioral expectations from both the agent and principal (Landström, Manigart, Mason, and Sapienza, 1998).

### 3.12 Summary of venture capital contracts

According to Kelly (2000) and Kaplan & Strömberg (2000 & 2004), all of the controlling mechanisms mentioned above are common. From the VC’s perspective, Kaplan & Strömberg (2004) have identified four generic agency problems: (1) venture capitalists concern for performance by the entrepreneur, (2) that the entrepreneur knows more about their ability/quality than the VC, (3) there will be post-investment disagreements where the VC fund wants a different decision and (4) the entrepreneurs’ human capital worth is so high that it can be used as leverage against the VC fund (ibid.). These morale hazard risks, misunderstandings in the VC and entrepreneur relationship, will be discussed and tackled in the conclusion part, to analyze the structuring of the deal and to explore the post-investment relationships (Söderblom et al, 2016).


4 POST-INVESTMENT RELATIONSHIP

One of the goals of this research is to explore the post-investment relationship between the early stage VC fund and portfolio entrepreneur. As earlier stated, this will be done by the help of agency theory, which looks at the relationship between the VC and entrepreneur analyzing the costs and perks of beginning this relationship (Eisenhardt, 1989). In addition to the agency theory, this research uses SDT related theory to explore the post-investment relationship (Ryan & Deci, 2000). The SDT will provide discussion of how autonomy versus control is balanced and perceived in the relationship.

Figure 5 below breaks down the post-relationship components. As presented in the figure, this research uses contract theory as a base when researching the relationship. This research breaks down the contracts into agency theory and self-determination theory. Finally, this research takes a look at control and autonomy to discuss the post-investment relationship balance.

Figure 4, Post-relationship theory map

4.1 Agency theory

Agency theory focuses on the relationship between the Principal (VC) and the agent (entrepreneur). Comparable to the traditional principal agent problem, this research assumes that efforts and actions by the entrepreneur are hard to observe objectively
(Kaplan & Strömberg, 2000). However, the evidence that correlates with the actions and efforts can be measured (ibid.). One of the most measurable pieces of evidence are revenue and contract clauses (ibid.) This research will look how this evidence is presented in contracts and how it affects the post-investment balance of control and autonomy between the VC fund and the entrepreneur. Kelly (2000) concludes in his research that VC, in comparison to private investors, take more care, time and attention in the screening process, with the agenda to draft an “optimal contract”.

The requirements that VC funds set for the relationship with the portfolio entrepreneur are usually high-pressured and very clear, comparable to revenue or other growth goals (Sapienza et al, 1996; Sapienza et al, 1994). These ways to monitor the entrepreneur are set because of the perceived agency problem that the VC fund has, thus causing risk to the relationship between the investor and the entrepreneur (Söderblom, 2016). To strengthen the reasoning behind using agency theory, Kelly’s (2000) research argues that in the context of the relationship between an investor and entrepreneur, agency theory fits very well (Eisenhardt, 1989). Kelly’s (2000) research uses agency theory in the context of private investors and in this research, it will be applied to the context of VC. In addition, Eisenhardt (1986) encourages agency theory to be explored in different contexts.

In the 1960s and 1970s, some economists started to explore risk taking among individuals and groups (e.g. Arrow, 1971; Wilson 1968). More texts started to describe risk sharing as a problem, which happens when cooperating partners have different views on risk sharing (ibid.). In general, agency theory assumes that the future is uncertain and monitoring the relationship between the agent and principal can minimize the risk taking in decisions (Eisenhardt, 1989). Originally agency theory is broader theory about risk sharing (ibid.). Agency problems occurs when cooperating parts have different labor goals and visions (Jensen & Meckling, 1976; Ross 1973). The agency theory concentrates on the relationship of two parts; one that delegates work (The principal), and the other that performs the work (The agent) There are two basic problems that arise in the agency problem: (1) the goals and desires conflict and/or (2) that it is expensive for the principal to find out what the agent is actually doing. This research will discuss both problems that arise after the structuring of the contracts. Moreover it will look closer on the contractual part according to Kelly’s (2000), Kaplan and Strömberg’s (2000 & 2004) research about contractual mechanisms, which
Eisenhardt (1989) also mentions as being the steering wheel that balances the relationship.

Eisenhardt (1989) describes the agency problem in a VC context to be critical in the following situations: (1) goal conflict, (2) degree of uncertainty with respect to outcome and (3) uncertainty of how the agent (entrepreneur) deal with tasks, which again leads to monitoring of the agent (Eisenhardt 1989, Kelly 2000). All these arguments are supported by Sapienza and Gupta (1994), that noted a high level of tasks and high level of outcome uncertainty in entrepreneurial ventures.

4.2 Agency Theory in an organizational context

Eisenhardt’s (1989) research paper is about ways to apply agency Theory in organizational research. This makes Eisenhardt’s (1989) research very well applied as one of the main sources in this research context. Agency theory is an important and widely used theory in organizational framework and is fitting to use in different testable propositions of research, like this study (ibid.). Eisenhardt (1989) implies that agency theory is theoretically relevant in the context of VC (Kelly, 2000).

Agency theory can be used in many different settings and based on many different variants (Eisenhardt, 1989). Most frequently, agency theory is applied in organizational phenomena (Eisenhardt, 1989). Eisenhardt (1989) mentions that agency theory is applicable on both a micro and macro level. In the research climate, agency theory is especially applicable when analyzing a micro level dyad phenomenon, which is the method used in this study (ibid.). Therefore, a combination of both dyad study and agency theory is appropriate for this survey.

Agency literature is divided into two different camps, which are known as the two frontrunning interpretations (Jensen, 1983). These two are positivist agency theory and principal theory (ibid.). They differ in mathematical rigor, style and dependent variables (ibid.). The positivist stream focuses more on situations that are less mathematical than principal agent theory (ibid.). In accordance, this study will use the positivist agency theory lenses, since this research looks at a relationship and is qualitative to its nature.

4.3 Positivist Agency Theory

The positivist researchers focus on researching scenarios where conflicting situations regarding the goals and desire may arise (Eisenhardt, 1989). In addition to this, the positivist researchers describe the governance mechanisms that limit the self-serving
behaviors (ibid.). In this study, in practice, the governance mechanisms are the contractual mechanisms of the shareholder agreement between the VC and entrepreneur (ibid.).

Two propositions exist to capture how the positivist agency theory is proposed in the context. The first one is about how contracts that are outcome-based will be effective in the process of curbing the agent’s opportunism (ibid. page 60).

“Proposition 1: When the contract between the principal and agent is outcome based, the agent is more likely to behave in the interest of the principal”

The second proposition implies that (2) information systems will curb the agent opportunism as well (Eisenhardt, 1989, page 60).

“Proposition 2: When the principal has information to verify agent behavior, the agent is more likely to behave in the interests of the principal.”

In small, new ventures, the investor (principal) is more likely to be risk-averse (Eisenhardt, 1989). The agency theory overall, predicts that risk-neutral managers choses the behavior-based contract and risk-averse executives are more likely to choose an outcome-based contract. Focusing on the right information systems, outcome uncertainty and risk minimizes the agency problem according to Eisenhardt (1989).

4.4 Self-determination theory

Furthermore, Eisenhardt (1986) points out that with another theory to complement agency theory, the result is better. For this research, one of the additional theories is the Self-Determination Theory (abbreviation: SDT) by Ryan & Deci (2000). The SDT looks at the whole spectrum of motivation, covering everything from total amotivation to full-intrinsic motivation. This research specifically looks into how autonomy in work effects, motivation, productivity and sense of well-being.

The SDT, is an academic approach to personality and motivation (Ryan, Kuhl & Deci, 1997). SDT uses organismic metatheory while applying traditional empirical methods, highlighting personality development and behavioral self-regulation. The center of self-determinations explains organismic meta theory and the SDT in general on their webpage (Center of Self-Determination theory, 2019):
“SDT is an **organismic** dialectical approach. It begins with the assumption that people are active organisms, with evolved tendencies toward growing, mastering ambient challenges, and integrating new experiences into a coherent sense of self.”

The theory is based on human growth and psychological needs, which lead to self-determination (Ryan, Kuhl & Deci, 1997). The SDT has established that there are three core psychological needs: competence, autonomy and relatedness (Ryan, Kuhl & Deci, 1997). Once these are enhanced, self-motivation and mental health increases. As demonstrated in the figure below, this research focuses on the psychological need of autonomy from SDT (ibid.).

As presented in Figure 6, this study focuses on autonomy, which is only one of the components to SDT (Ryan & Deci, 2000). The figure below presents the two other cores of SDT, which comprises competence and relatedness.

**Figure 5, Three cores of SDT**

The SDT argues that full autonomy will contribute to the highest productivity and best sense of well-being, while agency theory claims that the right amount of control can optimize the outcome (Ryan & Deci, 2000; Eisenhardt, 1989). These two theories differ
in their approaches towards the relationship between the investor and entrepreneur, creating a basis for the problematization of the post-investment relationship. This brings forth the question: How can the VC fund and entrepreneur create balance between autonomy and control in their relationship? To answer this question, it is logical to explore the VC and entrepreneur post-investment relationship with both agency theory and SDT (Eisenhardt, 1989; Ryan and Deci, 2000).

4.5 Autonomy

There is varying but clear information stating the importance of autonomy for entrepreneurial motivation (Van Gelderen, 2010). Literature about the need for control has also been explored by previous literature (Albert et al, 2013). Most entrepreneurs wish to be autonomous, but in some cases, like VC injections, the entrepreneur has to trade-off autonomy (ibid.).

To define autonomy in the most suitable context, this study has chosen Ryan & Deci’s (2000) research concerning self-determination. Full autonomy is defined as when you have no external regulators and when you are intrinsically motivated (Ryan & Deci, 2000). SDT argue that more autonomy equals a better outcome (Ryan & Deci, 2000). Ryan & Deci’s (2000) is arguably the most fitting autonomy related theory, since it is widely used in an organizational context (ibid.). Eisenhardt (1989) also mentions agency theory is best problematized alongside with another theory, which makes it fitting to use SDT. As Ryan & Deci (2000) remarks in their abstract of the research: the significance of SDT can well be used in the domains of education, health care, sport, work, religion and psychotherapy. Consequently, as “work” is mentioned, it fits the context of this research (ibid.).

Autonomy is important in this setting since much of the post-investment relationship is based on how much the investor controls the entrepreneur, since every investment seems to come with a trade-off regarding autonomy and control (Kelly, 2000).

4.6 Intrinsic motivation

Ryan & Deci (2000) explain intrinsic motivation as potentially being one of the single most positive potentials of human nature. Ryan & Deci (2000) explain intrinsic motivation to be constructed of a natural inclination towards spontaneous interest, mastery, assimilation and exploration, which is essential for social and cognitive
development. These represent the principal sources of enjoyment in life (Csikszentmihalyi & Rathude, 1993; Ryan, 1995).

4.7 **Extrinsic motivation**

Ryan & Deci (2000) demonstrate in “The Self-Determination Continuum” different types of motivation. The main components of the self-determination continuum is presented in figure 6 (Ryan & Deci, 2000) The figure also displays the focus from SDT to this research, which is the external regulations. In this research, the external regulations are measured by the contracts between the VC and the entrepreneur (Kaplan & Strömberg, 2003 & 2004).

As can be seen in the figure, the research in this study does not focus on the whole SDT continuum. It focuses on the extrinsic motivation. Extrinsic motivations and the external regulations are the logical focus from the SDT since this research is based on the relationship problematization of the contracts (Kaplan & Strömberg, 2003 & 2004). The contracts are clear external regulators, which take into account the components Ryan & Deci (2000) mentions to be central: Compliance, external rewards and punishments.

**Figure 6, SDT Continuum**
Autonomy is present due to the fact that any kind of external regulations applied in the relationship affects the autonomy, since the external regulations are rules applied from someone else, therefore the autonomy is affected (Ryan & Deci, 2000).

4.8 External regulations

External regulations are made up of compliance, external rewards and punishments are what is included to the external regulations (Ryan & Deci, 2000). As mentioned, this research will look at the external regulations in the post-investment relationship between the early stage VC fund and portfolio entrepreneur. In this study, the external regulation consists of the contracts.

After reviewing theory about autonomy, this research has found a clear focus on the external regulations of the extrinsic motivation (ibid.). The external regulations are the least contributing elements to autonomy, which seems logical since they are externally regulated and not intrinsically motivated.

As Baer (2009) mentions in the study about “Governing Corporate Compliance”, the actions and programs that the corporation applies in order to improve and educate the employees are needed in a corporate environment. Baer (2009) concludes that corporate compliance should encourage early and continuous interaction with the so-called regulator and the entity itself. In this study, the contract between the VC and the entrepreneur will be the measurements of compliance (Kelly, 2000).

Ryan and Deci (2000) argue that in order to facilitate an external regulation to be integrated in an organization or contract, the experience of autonomy is essential. Context can provide external regulation successfully if there are very salient threats and rewards which the employee feels competent enough to comply to (ibid.). The interesting part is to research the VCs and portfolio entrepreneurs. Are there any correlating factors in how the intrinsic motivation is facilitated through the external regulations? Are VCs taking into account this fact to awaken a sense of intrinsic motivation? This essential means: How is post-investment autonomy facilitated through contracts in VC backed companies? This study contributes to a broader theoretical understanding of the external regulations of autonomy and motivation. Are the Finnish VC backed entrepreneurs autonomous in their work? To which extent are the external regulations applied?
4.9 Summary of Theory

As reflected upon in the theory, this research started out by mapping the VC market. More specifically, this research was aimed towards the Finnish ecosystem of VC funds and portfolio entrepreneurs. This research has used classic venture capital theory, taking into account the contractual details, which then usually sets the structure of the relationship (Kaplan & Strömberg, 2000). After that, the research describes agency theory which is one of the most used theoretical frameworks in the field of venture capital. The reason for the common use is the matching context of the relationship, which is between and controlling principal (VC) and agent (entrepreneur). As a last theoretical theme, the research takes a unique perspective relative to earlier theory. This self-determination theory aims to problematize topics of the post-investment relationship, relative to agency theory, bringing both autonomy and control into the post-investment context. As added to the figure below, this research aims to (1) mention essential details in the structuring of the early stage VC deal and (2) create a discussion about balancing post-investment control and autonomy.

Figure 8 below is an enhanced version of figure 5. This figure below shows the components of analyzing the post-investment relationship between the early stage VC fund and entrepreneur. As outlined with red color, this research focuses on answering how the deal is structured and the balance of the relationship, taking agency theory (control) and SDT (autonomy) into account.
4.10 Propositions

*RQ1*: What are the essential details in structuring the initial contracts between early stage venture capital funds and entrepreneurs in Finland?

Proposition 1: VC funds, principally in this context use specific control mechanisms from the term sheet and shareholder agreement to control the relationship. In addition to balance out the controlling part of the relationship I speculate that they try to create room for autonomy by communicating systematically and showing willingness to collaborate and co-create.

*RQ2*: What is the post-investment balance of autonomy and control between early stage venture capital funds and their portfolio companies in Finland?

Proposition 2: VC funds have some “must-have” contractual mechanisms to guide the post-investment relationship in the initial building of the contact. Otherwise, based on the previous theory within the field (Sapienza, 1996; Kaplan & Strömberg, 2000 & 2004), I think that the nature of relationship is built and often perceived in a positive manner.
RQ3: For early stage venture capital funds and entrepreneurs going into the initial funding round, what are the practical implications in the context of Finland?

Proposition 3: Based on theory, this research could potentially create practical implications. In practice, the essential parts of the process to structure the initial deal. In addition, this research hope and suspect to find surprising and hidden messages about the relationship between the early stage VC funds and portfolio entrepreneurs.
5 METHOD

The following chapter covers this empirical study’s methodology (Bryman & Bell, 2011). This research is qualitative to its nature has an abductive approach (ibid.). The primary data and empirical material were gathered through semi-structured interviews (ibid.). The study was performed as a dyad which in this case, meant interviewing both the VC fund and portfolio entrepreneur (Söderblom, 2016). This made the method unique from previous researches, since earlier studies is over-reliant on the investor perspective (Söderblom, 2016). Söderblom (2016) examined the relationship risks between business angels and entrepreneurs with the dyad study (ibid.). Among one of the conclusions of Söderblom’s (2016) studies, theories developed in the research are highly applicable also in VC context, vice versa.

This is an explorative study (De Bakker et. Al. 2005; Eisenhardt & Graebner, 2007; Björklund & Paulsson, 2015). This methodology seems most fitting to answer the research questions of the study, since this research explores the relationship of the two research objects, the VC funds and the portfolio entrepreneurs (ibid.). This type of study is arguably the most suitable since the propositions between the constructs are based on new qualitative empirical material (De Bakker et. Al. 2005).

5.1 Abductive approach

As mentioned in the figure below, the abductive revising has allowed me to reach a better result, thanks to being able to revise the theory, method and research at any time (Bryman & Bell, 2011).

The figure below displays how the research has been abductively approached (Bryman & Bell, 2011). After the first version of theory, method, data and results, the research started revising all these components again in order to research the best possible results (Bryman & Bell, 2011). The research continued with the same process loop until the study as whole felt saturated (ibid.).
Figure 8, Abductive approach

5.2 Qualitative method

This research is qualitative to its nature (Bryman & Bell 2011). Braun and Clarke (2006) mentions, qualitative research includes a series of questions and it needs to be very clear how these questions are related and supports the research question. This is sort of the fundamental methodological reminder to stay focused on the research question. As Braun and Clarke (2006) also mention, it is normal that the research questions might change during the process of writing, which has been the case in this research as well, to reach the best possible result.

The strength in using a qualitative method in this research is to really perceive a deeper understanding on an emotional level of the two parties (Söderblom, 2016). A face to face interview allowed this study to examine further into very specific questions that arose during the interview (Bryman & Bell, 2011). By taking this qualitative approach, this research was permitted to identify deeper meanings of autonomy and control, which Kelly (2000) describes in his contractual safeguards to affect the autonomy and control.

Eisenhardt (1989) encourages agency theory to be expanded into different research areas and richer context. Hirch et al (1987) encourages using agency theory with complementary theories. This is one of the main arguments to why this research uses the

To give a clearer picture I will expand on the topic of the research and the research questions themselves. This research was consequent by using terminology from previous researches in order to be more consistent and create easier opportunities for further research (Bryman & Bell, 2011; Kelly, 2000; Kaplan & Strömberg, 2003 & 2003; Ryan & Deci, 2000). Especially the terms “structuring” and “post-investments” were often used in previous research, which then matched and is used for the topic of this research (ibid.).

5.3 Data collection methods

This thesis was, as mentioned conducted using semi-structured interviews (Bryman & Bell, 2011). The data from the semi-structured interviews are the primary data of this research (ibid.). Söderblom (2016) used a dyad study in the context of venture capital, which served as the bases for the choice of data collection method in this research. The dyad study is conducted between two persons with some form of relationship (ibid.). Therefore, in this study it is used to gain understanding of the relationship between the VC and entrepreneur (Macht, 2011: Söderblom et al, 2016). The results from the dyad data on this research has not been discovered in a Finnish venture capital setting, which indicates a rare and different angle (Söderblom, 2016). As Söderblom (2016) remarks, research in this area is often focused on the investor perspective. This is why the dyadic method works for exploring and comparing both sides of the relationship (ibid.).

The alternative ways of gathering primary data are unstructured, semi-structured and structured interviews (ibid.). The unstructured interview typically consists of one question and free discussion, unlike the structured interview which is conducted with a set of question and no room for free discussion (ibid.). The semi-structured interview is a hybrid/combination of the earlier two and is therefore the most suitable for this study’s interviews. The semi-structured interview gave me the opportunity to discuss new topics that were not mentioned in the planned interview questions (ibid.). A quantitative research would also have been an alternative (Bryman & Bell, 2011; Söderblom, 2016). Alternative, but as discussed later on, doing a quantitative approach based on the results of this research could be working well.
5.3.1 Interviews

The interview objects are 4 venture capital funds from Finland and 1 portfolio company from each fund, in total amounting to 8 interviews. By having multiple dyads, a more diversified picture is obtained, thereby reaching the research objectives (Söderblom, 2016). In this case the objectives are to learn about (1) the structuring of the initial early stage VC fund deal and (2) the balance of autonomy and control between the early stage VC funds and the portfolio entrepreneurs. These two objectives in the dyad samples fit the research, since the relationship in the research context is between two different interview objects of the dyadic research. One technical detail about one of the VC funds came to knowledge during the interview; they are structured as a limited company and not as a usual fund but their operations are similar to a funds. They fitted the research objective in all the other criteria. The empirical material in total was enough to repeatedly see clear patterns. During the last interview, the data felt saturated (Bryman & Bell, 2011).

Table 4 below gives a simple picture of what the four dyad profiles looks like. As presented, the most important components are the facts that all the dyads are from Finland and focus on early stage companies.

Table 4, The Dyad

<table>
<thead>
<tr>
<th></th>
<th>Dyad Alpha</th>
<th>Dyad Beta</th>
<th>Dyad Charlie</th>
<th>Dyad Delta</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Interviewees</strong></td>
<td>VC fund and Portfolio entrepreneur</td>
<td>VC fund and Portfolio entrepreneur</td>
<td>VC fund and Portfolio entrepreneur</td>
<td>VC fund and Portfolio entrepreneur</td>
</tr>
<tr>
<td><strong>Country</strong></td>
<td>Finland</td>
<td>Finland</td>
<td>Finland</td>
<td>Finland</td>
</tr>
<tr>
<td><strong>Initial VC investment stage</strong></td>
<td>Early</td>
<td>Early</td>
<td>Early</td>
<td>Early</td>
</tr>
</tbody>
</table>
5.3.2 Data collection

The questions and the script for the semi-structured interview guide was carefully built and subsequently accepted by the thesis mentor. The interview guide can be found in appendix 1. The languages of the interviewees were Swedish, Finnish and English. I used the language that the interviewee found most comfortable, which helped to create a smoother interview discussion (Bryman & Bell, 2011).

The first point of contact with the interview object was through an introduction by a person from the researches professional network, alternatively by directly cold e-mailing the person in question or messaging through LinkedIn. These messages consisted of a description of the research, the interview guide and discussion concerning suitable dates, time and place. When a meeting was set, the researcher travelled to meet the interviewee, therefore making the process as easy as possible for the interviewee. The researcher booked a time slot of 60 min consistently for every meeting. The researcher aimed for brutal honesty, without provoking conflicts. In addition, and according to the nature of semi-structured, the researcher let the interviewee talk freely, to find potential hidden information (Bryman & Bell, 2011). Furthermore, for transcribing purposes the researcher used their computer but also utilized their phone for recording the interview. The researcher also got permission to contact all the interviewees afterwards to clarify topics from the interview.

5.3.3 Coding

As a coding method, this employed a combination of the gioia method and thematic analysis (Braun & Clarke, 2006; Gioia et al, 2012). Both methods present a systematical way to code the data (ibid.). The coding of the primary date in this research is closer to the thematic analysis process. As displayed in the figures below, this research followed the 6-step process of the thematic analysis (Braun & Clarke, 2006). The main reason why this research using a thematic analysis instead of gioia is that the thematic analysis allowed the researcher to conduct an abductive approach. This research is using abduction as abstraction level (Weick, 1989; Locke, 2008). This gave the researcher the freedom to bounce between empirical research and theory in order to reach the best possible outcome (ibid.).

The 6-step process used for the thematic analysis is visualized below (Braun & Clark, 2006). As presented in the figure, (1) first, this research familiarized with the data, (2)
generated initial codes, (3) searched for themes, (4) reviewed the themes, (5) Defined the themes found and finally (6) produced a report.

**Figure 9, Phases of thematic analysis (Braun & Clark, 2006)**

This gave a very clear to analyzing the collected data (Braun & Clark, 2006). The thematic analysis and six step process gave a structured way to address the material and transcriptions. By simply looking at the data and not thoroughly analyze it, the key discovery may not have been found.

During the coding process, the research ultimately found 8 main themes, which are presented in the empirical chapter. The 8 themes were carefully picked out by using the process in figure 10 above.

The Harvard reference system is used throughout this study (ibid.). The tools for finding articles consisted of Google scholar, Scopus and Hanken’s Hanna library. To ensure the quality of the publishers, this research also used CABS (Abbreviated: Chartered Association of Business Journals; CABS, 2019).

The interviews were conducted in both Swedish, Finnish and English, depending on which language the interviewee felt most comfortable. Ultimately, the transcription was translated into English in order to find reoccurring themes from the data (Braun & Clark, 2006).
The main theories that this research are all highest graded journals (4*) in the CABS database or have been published at a top university as a doctoral thesis. CABS ratings are elaborated below. The 4* grade is called “Journals of distinction” (CABS, 2019). These journals are globally recognized examples of excellence (ibid.). By using exceptionally ranked theory, this research can build on the foundations of earlier studies recognized as excellent and thereby give this research outstanding theoretical substance.

**Table 5, CABS ranking**

<table>
<thead>
<tr>
<th>Main theories</th>
<th>Journals</th>
<th>CABS ranking</th>
</tr>
</thead>
<tbody>
<tr>
<td>Kelly (2000)</td>
<td>PhD, University of London</td>
<td>No Cabs ranking but published in nr. 2 Business School in Europe (Financial times, 2019)</td>
</tr>
</tbody>
</table>

The American psychologist journal which published Ryan & Deci’s (2000) most cited work with 32 000+ citing does not have a CABS rating. But an article which is published in the year of 2000 is based on Ryan & Deci’s (1989) previous piece about self-determination, which is published in the highest-ranking journal.

This research essentially builds only on previous research rated as excellent by Chartered Association of Business Journals (CABS, 2019). This has been the fundament way of reviewing and choosing the appropriate literature.
5.4 Data analysis

The semi-structured interviews were recorded by the researcher’s phone. Thereafter they were transcribed carefully within the next 48 hours, to ensure the quality of the material (Eisenhardt, 1989). The interviews were anonymously conducted (Bryman & Bell, 2011). This ensured transparency in the discussion between the researcher and the interviewee (ibid.) After the interviews, the researcher got assistance transcribing the interviews. The next step was to proofread every transcription twice. The second proofreading included correcting details and picking out key themes and topics for the analysis. In this process, the researcher used the method of a thematic analysis and inspiration from the gioia method (Braun & Clarke, 2006; Gioia et al, 2012). The transcription document was conducted in accordance to standard transcription guideline (Bryman & Bell, 2011).

5.5 Research strategy

The different topics and articles this research utilized during the process of the research are mentioned in the “Literature review” and “Literature quality list”, which the research have as a separate attachment to the thesis. During the process of finding literature appropriate to the topic, this research reviewed about 15 different research areas, covering close to 100 scientific articles. These research areas are elaborated in the literature review attachment. In addition to this, the researcher wrote a diary during the whole writing process. The research mapped the long-term and short-term goals for this document, to reach the results in a more logical manner. The diary can be found as a separate attachment by the name “Research Diary”.

The area of venture capital is familiar to the researcher from earlier. The researcher has been a part of a software startup company in Helsinki, which raised pre-seed funding and tried to raise seed funding. This has given an insight to the hands-on tasks conducted during the pre-fundraising process. In addition to the interviews for this study, the researcher has met personally with 10 venture capital companies and about 20 business angels, which provided the study with a good understanding of the discussions, in a Finnish context. Throughout the whole process, the researcher kept close contact with the master’s thesis mentor and other professors from Hanken. This ensured several senior researchers input, helping me to conduct the research and produce excellent findings.
5.6 Research ethic and philosophy

Regarding the research ethic, most of the responsibility lies in the researcher’s hands (Paulsson & Björklund, 2015). In comparison to the university courses, the institution bears the responsibility of acting ethical (ibid.). Through a well-planned methodology and interviewee point of contact, the researcher ensured an ethical way of researching (Bryman & Bell, 2011). The data collection was conducted according the General Data Protection Regulations (GDPR) and in accordance to Hanken’s guidelines (Hanken, GDPR, 2019).

This study has taken a pragmatist view (Hanken Research Design, 2019). This means that theory and analysis in this research are not absolute statements of truth (ibid.) The study is better defined as a helpful and a warranted assertion that explains this phenomenon, which helps to answer the research question (ibid.). Due to the qualitative nature, this research is built by constructs and propositions (Bacharach, 1989). Familiarizing with Bacharach’s (1989) paper, this research aware of the assumptions of delimitations of time, space and values.

These dyadic interviews were conducted anonymously (Bryman & Bell, 2011). This would potentially give the interviewee more courage to answer the questions more openly (ibid.).

The timetable for this study was from the end of August 2019 to December 2019. During this period, the thesis was conducted with the help of the master’s thesis supportive courses, mainly to assist with the methodology. The writing of the thesis writing took full time and attention; therefore, the timeframe was realistic. As mentioned in the introduction, the researcher wrote a literature preview document and a diary of the process, which can be found in the attachments. These attachments helped the researcher to pursue all the research questions following a common thread (Paulsson & Björklund, 2015).

5.7 Summary of method

The qualitative nature of the research fits well into the context of analyzing the relationship between the dyads (Bryman & Bell, 2011). This study took on a dyadic nature which worked best, both before gathering data and after (Söderblom, 2016). The dyad gave a unique way to examine the relationship of the VCs and entrepreneurs (Söderblom, 2016). The coding proved to be successful using a thematic analysis, which provided a
systematic toolkit for breaking down the empirical method in a logical manner (Bryman & Bell, 2011). The CABS journal ranking also proved that this research is built on exceptional literature, recognized with the highest grades (CABS, 2019). In addition to this, the university (Hanken) provided great assistance through mentoring and methodology courses throughout the writing.
6 EMPIRICAL RESULTS

The data gathering of this study began by conducting and interviewing the venture capital funds, after which the researcher asked the venture capital fund for permission to interview a portfolio company. In one of the dyads, the venture capital fund wanted to choose the interviewee, in the other ones, the researcher had the freedom to ask anyone from the portfolio. All the interviews were successfully conducted. With the thematic analysis and taking inspiration from the gioia method, the study found central themes in the discussion (Braun & Clarke, 2006; Gioia et al, 2012). The 8 themes that were found will now be presented below in this chapter.

6.1 Positive relationship

The first reflection from the dyadic studies is the positive look on post-investment relationships between the VC fund and the entrepreneur. The general consensus in all these cases is the fact that both parties’ root for the success of the entrepreneurial venture during the process. So, when all the agreements are signed, the VC will do everything in its power to make the entrepreneur succeed. Much of the positive relationship seems to be based on the fact that there are not many control related issues in the relationship of specifically early stage venture capital backed companies. This research will get back to this later on. The post-investment relationship between the investor and the entrepreneur is usually active, usually consisting of weekly interactions.

“We think that both are of course shareholders. Both wants, (pause) wants to make it big in the future” (Cited by Dyad Alpha VC Associate)

Though, it is important to remember that even the initial contract structuring is done in a positive manner and atmosphere. The conflicts in the relationship seem to arise only if the company has economical struggles and the contract counterparts have to go to the contact for solutions. For these cases, it is essential to have a dependable structure of the contracts.

6.2 Unique community

According to the dyadic studies, the early stage startup community in Finland seems to be unique. One of the truly extraordinary parts of the community is in this case a sense of goodwill to share top network with each other. One of the venture capital funds mention this as a competitive edge in their investment strategy as well. They are able to access unique talent from the goodwill of network sharing.
“The whole community is a part of the incentive” (Incentive in the context of why entrepreneurs choose to partner up with Dyad Alpha VC fund) (Cited by Dyad Alpha VC Associate)

Another unique feature that is discussed by entrepreneurs is the unique help that one gets get from the government. The Finnish government can from example provide a wage for the first year of operations. In addition to this, they have different private funding programs from the Business Finland entity.

The whole community aspect brings a unique cultural factor into the context. Further research that discuss how this affects the early stage venture capital scene would seem relevant to examine future.

6.3 Autonomy

Both VC funds and early stage companies insist on the fact that an early stage company should have full post-investment control in terms of voting right on the basis of shares. It seems to be essential for the operational side of the company to change the direction of strategy in an agile way. The only contractual veto that most of the venture capital funds insist on is a budget veto. The budget veto seems very logical since the venture fund company injects money and therefore wants a say in for example the salary according to two of the interviewed venture capital funds. As one portfolio entrepreneur mentioned, his decision-making would not have been affected even if the company had been bootstrapped, meaning it would be able to grow without external financing.

“It was a big-time investment to make the contract, just to make sure everything worked. The only thing the investors got was a Veto right for the budget. So, I only have to approve the budget with them, and then they could say yes or no to that, and then we have to do it again if they did not approve. Otherwise full control, and then I’m also, we made sure that I control the board as well. So, I didn’t give away too much. So, they were pretty lean, they didn’t want that much control.” (Cited by Dyad Delta portfolio entrepreneur)

This citation below confirms word by word that the autonomy level is high post-investment. Even if full autonomy is obtained for the entrepreneur post-investment, one market standard control mechanism regarding cash-flow rights is applied. That is the vesting of shares. Vesting standards are usually a 4-year period with a 1 year so called cliff.
The dialogue with Dyad Charlie portfolio entrepreneur shows the autonomy in a clear way:

“Exactly. If you would compare that, let’s say that you bootstrapped and let’s say you have a VC and you look at the decisions of where you were going with the product and with your business would you say would it be the same?

It would have been the same.”

(Dialogues cited from Dyad Charlie portfolio entrepreneur)

6.4 Control

It is clear that the relationship between the early stage venture capital fund and portfolio entrepreneur, when we talked about control of the company, it was about the voting rights according to the share, since it makes up the ultimate decision making in a company. When looking at negotiating control before the money injection in the company, the entrepreneur was the underdog. This was often because the companies need money in order to operate, and therefore are in a compromised position. This might make the entrepreneur to agree on terms that may otherwise not be accepted. One example of this was a venture capital company that was able to apply an anti-dilution right to one of the dyad entrepreneur’s contract.

The SHA plays an essential role in the controlling of the company which will be discussed further below. The most important fact is that the entrepreneur has to pay attention to every detail mentioned in the contract. One of the portfolio entrepreneurs exemplified that without knowing the intention of the venture capital company he was close to signing a contract that would have allowed the VC to fire him, which would essential have let the company buy the shares at a minimum price as they were not vested. Thorough is vital.

Being the lead investor matters too, as the lead investor usually dictates the terms for the other involved investors, which seems logical since they have the most money at stake. Another thing that is good to be aware of as an early stage entrepreneur is the fact that most early stage entrepreneurs have not gone through due diligence with a VC fund. For VC funds though, due diligence is part of their daily job. This creates a gap of knowledge between the two parties, which sometimes seems to be exploited. The exploitations do not necessarily have to be harmful towards the entrepreneur but often still unfavorable.
Many of the dyad portfolio entrepreneurs mentioned that they went into discussions unprepared, which made them in a weaker position due to lack of knowledge in the due diligence process of raising funding.

“Well I think I went to the negotiations where I'm unprepared because I have never really thought about raising investments. I was just trying to very quickly learn about that stuff and I don’t think I really realized at that point at least in the beginning how strong my negotiation process” (Cited by Dyad Beta portfolio entrepreneur)

The Dyad Beta portfolio entrepreneur was in a unique compared to the rest of the portfolio entrepreneurs in the dyads because Dyad Beta entrepreneur was not in a hurry or in dire need of rising money. This is why he reflects upon himself being ignorant of the strong position. Also benefited, not only from the monetary investment but from the publicity of the investment.

6.5 The contracts

Within Finland, one of the first mentionable facts concerning VC backed entrepreneurs’ relationships is a very transparent approach to the contract from both sides. Exploitation is looked upon negatively as it will result in a bad reputation. This seems to be because of the active early stage startup community in Finland. A clear benchmark for how the contracts are built: 3 out of 4 venture capital funds mentioned that contracts from seriesseed.fi is a market standard. One even went as far as claiming that any other contract than Seriesseed should be questioned.

“In Finland the terms are always the same because everybody uses seriesseed.fi paperwork in the beginning, you are not going to be seeing any other. If you see any other paperwork you should run.” (Cited by Dyad Charlie Portfolio Entrepreneur)

Seriesseed is updated regularly in accordance with changes within the early stage company culture and surrounding.

The usual documents that are used in an early stage investment process are (1) the investment agreement, (2) SHA and (3) the term sheet. These were used in all the dyads.

As this study briefly touched upon in the previous theme about control, paying attention to detail is essential in the development of contracts. Especially since the entrepreneur is most probably in a weaker position regarding prior knowledge of due diligence. One of the companies admits to a mistake they made with a venture capital fund but did not
want to elaborate on the mistake even if the interview was anonymous. Another entrepreneur did not want to disclose the contract details about the liquidation rights. This proves the delicacy of the relationship, though the relationship has a positive and co-creative atmosphere to it, there seems to be some sensitive, hidden matters regarding very specific clauses.

Three quarters of the companies used preferred shares, while one company used common shares. Preferred shares appear to be the market standard, both in Finland and the US according to the dyad interviewees.

“For example, if company X has 60% money from the Arabic country, then they have clauses that are based on Arabic law” (Cited by Dyad Alpha VC Associate) (Free translation from Swedish)

Like Dyad Alpha indicates, the cross-border details matter in the contracts and clauses. The interview did not go into detail regarding cross-border specifics but these are to be taken into account.

Another additional input regarding cross-border comparisons was stated by Dyad Charlie portfolio entrepreneur and Dyad Charlie fund manager. This could be looked into in the future through a comparative study:

“Because in Central Europe quite a few investors still play with a playbook from the early 2000’s or even late 90’s or something like that where the rules are a bit different. I wouldn’t say that there is no super bad terms in that sense.” (Cited by Dyad Charlie Portfolio Entrepreneur)

“Would you say that there’s any time sort of a negative let’s say atmosphere if you think about these sorts of contractual controlling clauses and contracts? Post investments, would you say that there are some times conflict on how they’re built?

I would say yes. Yet again, he comes to cross border investments. In Finland terms are in general, pretty good on founders.”

(Dialogue with Dyad Charlie VC fund manager)
6.6 Self-determination

The interesting problematization in this study is that agency theory claims that the best outcome is achieved by certain level of control, while self-determination theory advocates full autonomy in terms of achieving most intrinsic motivation, which would result in best productivity and sense of well-being (Ryan & Deci, 2000). The fascinating part about specifically early stage investments is that in terms of voting and board control, the VC actually prefer the full post-investment control of the entrepreneur. The only control the VC seem to want is a veto on in the budget of the company. From a VC perspective it is understandable, in the sense that they provide the money and therefore want to know how it is allocated. So, the VC is in a sense feeding operational autonomy to the entrepreneur, simultaneously wanting a say in how the budget is allocated.

“Next round, I’m gonna lose the majority stake. But I will still try to remain in control. I would say that it doesn’t matter if the entrepreneur doesn’t have like a controlling stake if venture capitalist is believing him and his vision. Because no one can be as insightful in the business as the entrepreneur himself. So, let’s say if the venture capitals are trying to make too many decisions then that’s not gonna work.” (Cited by Dyad Delta portfolio entrepreneur)

As cited above and mentioned in two other dyads, the follow-up rounds are gamechangers with regard to the sense of control. But then again Dyad Delta points out that in terms of operational tasks, the entrepreneur, being the hands-on person will always have more insight regarding the business itself. So, when the entrepreneur loses control, the power dynamics may change. This would be great to research further.

Fascinating enough, all the VCs advise the entrepreneur to have autonomy during the early stage in order to have operational power and thereby be able to be agile. The interesting part to identify would be where the threshold is for the VCs wanting to obtain voting majority and vice versa for the entrepreneur.

6.7 Context of Finland

Both the entrepreneurs and VC funds mentioned cross-border differences. This was in regards to questions concerning if they would invest in cross-border companies or if an entrepreneur would seek cross-border funding. They point that Finland had a working, founder friendly culture in terms of early stage companies. The level of pro-bono input
in early stage founders are mentioned as unique in Finland, which might give a competitive edge when compared to other cultures.

“I think in today’s economy, it is not hard to get money if you have a good idea” (Cited by Dyad Alpha Portfolio Entrepreneur)

This also indicates the broad availability of early stage venture capital, which may seem obvious in Finland but as mentioned, might be very different in another country.

An interesting input regarding the organizational structure of the VC funds in Finland is that Dyad Alpha VC Associate mentioned that all the VC funds in Finland are in the corporate form of a “kommandiittiyhtiö”, which is a specific legal form.

6.8 Hidden messages

As mentioned earlier in the thematic summary of the empirical research, there are hidden messages regarding anti-dilution and liquidation rights in the contract. Even if the interviewee objects were anonymously interviewed, two of them could not elaborate on details concerning these two clauses in the shareholder agreement. Speculatively, maybe it could have hurt the company to reveal details. This will be further discussed at the end of the research, as a potential future research area.

“Companies in the later stage are usually stricter with the liquidation rights”. (Cited from Dyad Alpha VC Associate)

It seems as though the liquidation rights are tied to the longer-term vision since it is a clause that is relevant in exit scenarios. This could also be potential to research in the future.

6.9 Summary of the empirical material

The following figure presents the key findings. The key findings are presented in accordance to the 8 main themes that were found.

Figure 10, Key findings

| Positive relationship: | The relationships is more positive than perceived in earlier literature. |
**Unique community**: The community brings a new cultural perspective to the research area.

**Autonomy and control**: Full autonomy seems to be impossible due to the nature of trade-off for money but the autonomy seems to be divided into operational and strategical components.

**The contracts**: Seriesseed is the Finnish market standard version for contracts.

**Self-determination**: Does not seem to be affected in the initial early stage venture capital funding round.

**Context of Finland**: Some unique features are found in the Finnish context, like the community.

**Hidden message**: Sensitive parts are left out from the interviews even if they were conducted anonymously. What does this indicate?

The data and dyad method proved to be very fruitful in many ways. The dyad was able to pick out contrasts in the interviews that would not have been possible by one-sided interviews. The research was able to identify interesting themes with the help of the systematic thematic approach. This allowed the research to pick out similarities in the empirical material in order to draw the best possible conclusions.

The interesting part of the discussion between autonomy and control is that it seems obvious that some autonomy has to be given up in order to receive an investment. The data indicates that there might be a difference in operational and strategical autonomy/control. This will be elaborated on in the analysis chapter below.
7 ANALYSIS

The empirical part of the research was proven to be rewarding. The research found 8 main themes. Differing from earlier research, the dyad study was able to identify important factors regarding Finnish context, which neither Kelly (2000) nor Kaplan & Strömberg (2003 & 2004) mention in their researches. As follows, the research will now analyze the empirical material in the same order as the theory was presented. As displayed in the figure below, this means first looking into (1) early stage venture capital in Finland, next (2) venture capital contracts and finally (3) the post-investment relationship. From there, the research will illustrate the identified conclusions and finally answer the research questions. The figure 11 below presents the order of the analysis.

Figure 11, Order of analysis

7.1 Early stage venture capital in Finland

To fundamentally understand and dig deeper into exploring the post-investment balance of autonomy and control in the relationship between the venture capital fund and the entrepreneur, it has been essential to paint a picture of how venture capital work for early stage companies in Finland. One of the strongest fundaments in early stage Finnish VC scene lies in a well-developed early stage startup community, which young entrepreneurs and university students play a vital part in creating. According to VC history, the market has change drastically in numbers compared to now (Bygrave, 1994; Finnish Venture
Capital Association, 2019). Especially since the first time Karl Compton and other notable figures founded the first VC company back in 1946 at MIT (Gomper & Lerner, 2001). As mentioned in the beginning of this thesis, VC market in Finland and the rest of the world have developed to be an essential part of the economy, relative to GDP (Finnish Venture Capital Association, 2019). Confirming Sahlman’s thoughts (1990) with this research, the nature of the early stage VC sector driven by high risks and high rewards, especially in Finland for early stage startups backed by venture capital. Previous theory and practice have made it clear that the venture capital scene in Finland has proven to be unique regarding its of community and support from the government (Finnish Government, 2019; Stifted, 2019). After the fall of Nokia, it affected effect on the Finnish economy thereby scattering IT talents who subsequently created successful ventures and communities that support the growth of early entrepreneurship (ibid.).

The companies in this research were limited to the stage of early stage companies (Sahlman, 1990). Some entrepreneurs that raised pre-seed while some that raised seed funding (ibid.). The idea of this research’s limitation was to create a clear niche, which would assist in generalizing conclusions of early stage group, which this research has done successfully. In previous theory, it has been deemed difficult to obtain overview of the whole VC industry, rather in different targeted groups, like early stage companies (Sahlman, 1990; Gomper & Lerner, 2001; Li,M. et al, 2016).

As Bygrave (1994) mentions in his research about venture capital almost 30 years ago, this research proves same fundament regarding fund raising. Both parties should be attracted to the deal in order to reach an agreement (ibid.). The evidence from this study indicates clearly the same in the Finnish context. The post-investment relationship is seen as a positive interaction, both are rooting for one another to succeed. The study confirms that the only scenario where things might get more difficult is if the companies end up in a bad monetary situation. This is why the shareholder agreement plays an essential part in order to set clear terms for unforeseeable future challenges.

As confirmed in this research in line with Bygrave (1990), VC funds still might use too much power in order to make a deal with the portfolio entrepreneur. As mentioned by one of the portfolio entrepreneurs, they had to agree on an anti-dilution clause in the SHA because they were practically out of cash. This use of power is therefore still a problem, which none of the venture capital funds brought forth in their discussions. Here the dyad study proved fruitful, finding the power moves of the VC funds towards the entrepreneur. Confirming Sahlman’s (1994) earlier research, entrepreneurs still seem
over optimistic to accept easier terms, due to lack of knowledge in the due diligence process. This could speculatively be generalized to only early stage venture, raising money and creating fund raising related contracts for the first time. This research proves that the core phases of the deal which Bygrave (1994) mentions, still exists today, normally consisting within the context of (1) investment agreement, (2) shareholder agreement and (3) term sheet.

Looking at the whole spectrum of the VC fund, there are other relationships including the whole spectrum of VC, as mentioned in figure 3. As proven in figure 3, the chain starts with limited partners, investing to the venture capital fund, which invests in the entrepreneurial venture and ultimately if the portfolio is successful, the private person might end up investing in the fund as a limited partner. It has been important to have an understanding of this, in order to understand the VC funds function on a deeper level, which practically means how the cash flows in and out from the VC fund.

7.2 Structuring the initial early stage venture capital contract in Finland

As Kaplan & Strömberg (2000) concludes and this research confirms, contracts seem to be the cornerstone to a healthy behavior in the post-investment relationship of early stage VC funds and entrepreneurs. Kelly (2000) states that in the context of private investors, there might be unwritten norms outside the contracts steering the relationship, but this research proves that in the Finnish venture capital scene it is more formal. The contractual mechanisms and clauses are proven in general to be similar to what Kelly (2000) mention in his doctoral thesis, which results in a good match in this context.

This study has discovered that both the VC fund and the entrepreneur were concerned with details regarding the contract. Furthermore, the interviews proved that paying attention to fine details, specifically wording is essential. One of the entrepreneurs exemplified by mentioning that he came close to missing a sentence in the contract, which would have allowed the VC fund to kick him from the company and resulted in the VC fund buying the entrepreneur's un-vested shares to a minimum price. This confirms and extends to the Finnish context, that Kaplan & Strömberg’s (2000) conclusion that securities and different clauses in the contracts are not homogenic, you need to pay attention to each specific detail. In this dyadic study, convertible preferred stock was the standard as well.
Regarding specific clauses that are perceived as standard in shareholder agreements, the following was discovered. One cash flow right was popular among the early stage deals in Finland, which was vesting. It was the vesting of shares, which was set as a standard throughout the Seriesseed contracts. Many contracts prepared by Seriesseed suggests a vesting period of 4 years and a one-year cliff, meaning that the share vesters have to work at least one year to earn their first share. This seems logical in the sense that investors can assure the entrepreneur’s commitment for the company for at least one year, no matter what. This extends clearly the conclusions about cash flow rights in the Finnish context.

Voting rights from the convertible stock was held with a majority by the entrepreneurs’ post-investment in all the cases. In this study, early stage VC funds also made clear that this was both sides intentions, in order for the early stage company to make pivotal changes quickly without any problem in decision making. Post-investment board rights were often required by the VC fund, meaning that the entrepreneur traded strategical autonomy/control. Reflecting again on the autonomy of decision making, this did not affect the decision making of the board in favor of the VC. This proved that VC funds just requires to be kept informed on the official decisions made, thereby needing to be part of the boardroom.

Liquidation rights proved to be trickier in this research and context. Only a few of the VCs were open about the fact that their liquidation multiple was times one and they had the right be paid back before other parties could capitalize on results from exit or company result. One of the entrepreneurs though, wanted to keep this secret, even though they were anonymously interviewed in the research. As with the anti-dilution rights, this shows an extreme sensitivity towards information, raising the question, what can be so secret regarding the liquidation rights and anti-dilution rights?

This study confirms that the term sheet seems to be used by most but is not mentioned as especially important in the due diligence and contract writing process in Finland. The term sheet just shows initial commitment for all parties involved, while the investment agreement and shareholder agreement show the final commitment of the relationship.

Taking into account Osnabrygge’s (1999) and Kelly’s (2000) conclusions, this research confirms that it is more important to have a flexible approach towards the framework and contractual safeguards, rather than having a “optimal contract design” from the
beginning. Therefore, this research proves that being aware of the process gets the best end goal. This also confirms Osnabryge’s (1999) and Kelly’s (2000) conclusions.

7.3 The post-investment relationship of initial early stage venture capital investments in Finland

In this study, the VC fund is the principal and the portfolio entrepreneur is the agent. The problematization with agency theory in this context is clear, trying to optimize the cost and gain side of the post-investment relationship by having the right balance of control and autonomy. As Kaplan & Strömberg (2000) mention in their research, some so called “signals” can be used to measure the success of the entrepreneur’s effort. In this research, revenue is proved to be one of the clear parameters for success. It was also revealed that having a veto in the budget was a clear control mechanism, trying to optimize cost of budgeting mistakes in the relationship. This seems understandable from both sides, so that if someone invests their money into a venture, they also want to have a say in how the money is allocated, but not want to micro-manage operational tasks.

The dyads in this research confirms a surprising factor to be unique in the Finnish context, which is the early stage startup community. A deeper level of discussion is needed in the future to understand the phenomenon of early stage venture capital in Finland. This research proves the need to research the Finnish early stage startup community further in the future.

Reflecting on the agency theory with the two problems that Eisenhardt (1989) mentions, (1) goals and desires do not conflict in this context. In this research, both the principal and agent have the same goal, which is increasing the valuation of the company. Eisenhardt (1989) mention this in his first proposition on page 60:

“When the contract between the principal and the agent is outcome based, the agent is more likely to behave in the interest of the principal”

The second problem that Eisenhardt (1989) mentions is clearly expressed in the research with for example the budget allocation veto that two of the VC funds required. In addition to the budget veto, the VC funds seem to advocate giving the entrepreneur freedom regarding voting rights and clauses regarding decision making on the operational side. This research confirms Eisenhardt’s (1989) second proposition on page 60, by having a budget allocation veto, the VC fund is able to confirm the agent’s behavior. This also confirms a risk-averse approach by the VC fund, which Eisenhardt (1989) discusses in
his research. All VC funds are confirmed to be involved as board members in the companies, according to this research. This confirms that VC funds use some kind of information systems to decrease the agency cost, which is usually done through attaining a board seat in Finland (Eisenhardt, 1989).

This study's reflection on the positivist agency theory scenario, between early stage VC funds and the portfolio entrepreneur, does not seem to be in conflict regarding desire and goals, even if the relationship is of principal to agent character. This study confirms that both the principal and agent want one another to succeed. The only conflict of goals and desires seem to be in the pre-investing phase, where the VC fund might have more power to include clauses that are favorable to them. In one of the dyad cases, the entrepreneurs had to agree on anti-dilution right for the VC fund. The VC fund acquired the power position by knowing that the company needed cash fast and was therefore able to push the boundaries of the contracts.

The interesting part here is to compare the agency theory in this context with autonomy from SDT. This study, aligns with Eisenhardt’s (1989) research, confirming actions that minimize agency cost and has done that in the context of VC.

Agency theory argues that the optimal outcome of the post-investment relationship is achieved by controlling the agent with the right mechanisms, while self-determination theory claims that best results in terms of productivity and sense of well-being is achieved with full autonomy. The challenging part in this context is the fact that this research has not found these two theories being used parallelly before. Self-determination theory and agency theory are both encouraged to be used in an organizational context, which is one of the reasons they were possible to use in this study.

This research has found that a clear extrinsic motivator for both the VC fund and the entrepreneurs is the monetary rewards. The clear external regulators found in this research are the clauses set in the contracts. This confirms earlier theory, claiming that contracts are the fundament of the relationship (Kelly, 2000; Kaplan & Strömberg, 2003 & 2004). By getting investments in the venture to scale economically and get even a bigger reward is the goal is confirmed by this research. This is clear from the empirical material, that the entrepreneurial passion for founding a venture increases the chances of reaching the extrinsically motivating goals.
This research will now explore further the discussion of the post-investment relationship of the VC fund and entrepreneur regarding the balance of autonomy and control. This study confirms one matter regarding the fact that all VC fund representatives actually prefer operational autonomy to the portfolio entrepreneur. This is regarding the post-investment autonomy of operational freedom the entrepreneur holds. This means, concretely that the voting right majority lies in the hands of the entrepreneur. The early stage VC acts according to what Ryan & Deci (2000) point out to be essential, creating and facilitating an experience of autonomy in order to reach optimal productivity and sense of well-being. An interesting question would be to ask the VC funds if and why they are facilitating autonomy on purpose. The only control mechanism VC funds want is a veto on the budget. This sort of creates the logic that they only want the agent to principal relationship in allocating the money, not in operational details. Full autonomy is not to be achieved and the budgeting where the entrepreneur loses strategical control of the company, giving a veto to the strategical decision-making of the company. Another topic which could be appealing to find out is about follow-up financing rounds in later stages and to find the pressure point where the entrepreneur lose the control of operational control of the company. I will get back to this in the section concerning further research.

This research had unique approaches compared to previous research in VC field of study (Kelly, 2000, Kaplan & Strömberg, 2003 & 2004). This study investigated the structuring of the early stage VC deals and problematized autonomy and control in the context of the research. Literature about VC usually looks heavily on the side of VC, while the dyadic nature of this research takes into account both relationships. Results from these unique perspectives are further elaborated below.

### 7.4 Post-investment autonomy and control

By gaining a capital injection to the company, the entrepreneur has to give up something, which in the context of early stage companies in Finland points out to be heterogenic according to this research.

Comparing agency theory and autonomy from self-determination theory in this context is eye opening (Kaplan & Strömber, 2000; Ryan & Deci, 2000). What this research suggest clearly is that early stage venture capital companies as principals to the agents, use their controlling power towards the entrepreneur, by giving them as much operational control as possible so as to be able to develop venture. In a sense, this suggests that the consensus between the early stage VC fund and portfolio entrepreneurs
is the fact that the entrepreneur has full freedom of steering the venture’s future operationally, at an early stage at least. Through the interviews it became clear that the possibility of making quick decisions is important and by minimizing the involved decision makers, the execution is faster. The research proves that entrepreneurs do not see the venture capital contracts blocking the autonomy to operate after an initial investment by the early stage venture capital fund.

So, to summarize regarding a conclusion of the autonomy, full autonomy seems to be hard to achieve, without any consequences. The trade-offs in early stages seem reasonable, which both the VC and entrepreneur agree on in this research. The trade-offs are proven too often be budget veto and a board seat. This simply gives space for the VC fund to be a strategic partner of the company, without taking any operational control. An interesting follow-up would be investigating how this balance of control and autonomy continues during the follow-up rounds, since VC backed companies often raise more than one financing round (Kaplan & Strömberg, 2004).

Kelly (2000) discusses, in his research, some clauses are not put in to the shareholder agreement in the context of private investors, because the VC and the entrepreneur have a high level of trust of acting according to some norms. This never came to discussion in the interviews of this research. It could be that this is the case, but results from this research did not sign any connections to what Kelly (2000) concluded about this in his research. This research indicates that VC deals are more formal which kills the “norms” and non-contractual mutual expectations that exist in an angel round.

Implications from the empirical material confirm that the follow-up rounds play a vital part in the creation of the initial early stage funding round contracts. No particular examples are made but the discussions did, several times reflect on how a future scenario would affect the contract.

Key trade-offs in this research is that when raising the initial early stage VC capital, someone invests their money to a venture and they want to have a say in how the money is allocated, but not how micro managing tasks are operationally executed.

The research ended up recommending a figure based on the analysis of the study. This figure is based on FIBANS “investment process” which is visualized earlier in the research. This figure 13 presents the key parts from the analysis to the structuring of the initial deal and to the analysis of the post-investment relationship. The most important
contributions are the two new components which autonomy and control are divided into: Strategical and Operational components. These findings are elaborated below the figure.

The figure below zooms into the due diligence process and the post-investment relationship phases. The research confirms and picks out key-takeaways regarding these two phases. Out of the discussion about the post-investment relationship grew the two new components of autonomy and control, which also are visualized in the figure.
Figure 12, Initial deal of early stage VC: Due diligence and post-investment relationship in Finland

Operational autonomy/control

Strategical autonomy/control

A positive relationship
Consider the autonomy threshold in follow-up rounds
Budget veto as control mechanism
Use the unique community
Full operational autonomy
Voting majority

Presentation → Chosing the companies → Due diligence → Closing discussions and valuation → Post-investment activity → Exit

Formal contract creation
Seriesseed.fi
Budget veto
Vesting
Flexible contract and process
Pay attention to the details
8 CONCLUSIONS

This chapter concludes all the findings of the research. In addition, this chapter answers the research questions and confirm/deny the propositions. After the conclusion, further research possibilities and post-research comments are discussed.

8.1 Results

RQ1: What are the essential details in structuring the initial contract between early stage venture capital funds and entrepreneurs in Finland?

Formal but flexible contracts

This study confirms that creating a formal contract is important. The usual contracts are: (1) the term sheet, (2) the investment agreement and (3) the shareholder agreement. This study has proven different conclusions in relation to Kelly’s (2000) argument of the existence of informal agreements outside the contract. Going into an initial deal with a venture capital company seems to put weight on not having unspoken norms but rather having written all the rules out that will apply.

This research indicates that the entrepreneur and the VC fund should benchmark existing contracts to create a firm first document of the initial VC investment in Finland. Seriesseed seems to be without exception the correct benchmark in Finland.

Budget veto and vetos regarding the expenditure is one of the few control mechanisms. This importance of this is also confirmed in Kelly’s (2000) research, where a majority of the interviewee objects ranked this as “very important” to include in the contract, according to Kelly’s (2000) quantitative research. It could be interesting to research the same context of this research with a quantitative study at some point, to prove the results from a statistical perspective. Another benchmarked control mechanism is vesting. The research indicates that it is essential to ensuring the commitment of the entrepreneur.

As Osnabrugge (1999) and Kelly (2000) conclude in their research, it is more important to have flexible framework, rather than an optimal contract. The empirical material confirms this and as well that the final contracts are heterogenic.

Essentially in early stage venture capital rounds, the process seems to be very detailed and it is of importance that one has knowledge concerning proper contract structuring. This is especially because the VC fund might use weak knowledge in their favor.
Comparing the VC contracts and relationships to private investors, this research confirms that VC contracts seems to be more formal regarding the contractual side. This research has proven different conclusions comparing to Kelly’s (2000) argument of the existence of informal agreement outside the contract.

This research has confirmed the first proposition and found essential details of structuring the initial deal of early stage venture capital funds and portfolio entrepreneurs in Finland.

*RQ2: What is the post-investment balance of autonomy and control between early stage venture capital funds and their portfolio companies in Finland?*

**Operational autonomy but compromises regarding strategical autonomy**

This research proves that the first fundament on the discussion about autonomy and control is that both parties go into the relationship with a positive attitude. In the early stage, full autonomy regarding voting rights from the shares to the entrepreneur is proven to be consensual from both parties. The interesting question is when the threshold for control should appear in the follow-up rounds. Budget veto and vesting are the only mentioned control mechanisms from the contract that affect the post-investment balance. One of the VCs had the unique Finnish early stage startup community as an investment strategy perk. This confirms the effect on the transparency of the initial deal discussions, which is positive. For example, the community provides a standard template for contracts from seriesseed.fi.

This research extends knowledge regarding that the entrepreneur feels and usually has full operational autonomy in early stage VC backed companies in Finland. This means that they have a voting majority from the shares. As mentioned above, it is all about a trade-off. There is not a desire from the entrepreneur or the VC fund to achieve full autonomy, even if Ryan and Deci (2000) state that this is the optimal state of productivity and sense of well-being. The trade-offs in terms of contracts are usually budget veto and board seats in Finland.

Without planning it, this study has contributed to dividing autonomy and control into two different components: Operational autonomy/control and Strategical autonomy/control. This will be elaborated on later in the chapter and could be interesting to research further.
This study research has found the “must-have” control mechanisms and confirmed the second proposition of the research, giving an insight to the post-investment relationship balance.

**RQ3: For early stage venture capital funds and entrepreneurs going into the initial funding round, what are the practical implications in the context of Finland?**

**Be detailed and positive**

As practical implications, based on the answers to RQ2 and RQ3, the research has produced a list of practical implications for going into the initial venture capital investment.

**Table 6, Practical implications table**

<table>
<thead>
<tr>
<th>Practical implications table</th>
</tr>
</thead>
<tbody>
<tr>
<td>- It is a positive relationship; both want the same thing.</td>
</tr>
<tr>
<td>- Be detailed when you structure the initial deal and contract.</td>
</tr>
<tr>
<td>- Take support from the community.</td>
</tr>
<tr>
<td>- Educate yourself and find good benchmarks of other deals.</td>
</tr>
<tr>
<td>- Use seriesseed.fi for contract document models.</td>
</tr>
<tr>
<td>- Be flexible about the process.</td>
</tr>
<tr>
<td>- Take into account potential follow-up rounds and how they affect you.</td>
</tr>
</tbody>
</table>

This table illustrates similarly as Kelly (2000) concludes in his doctoral thesis in the context of private investors: The process is much more important to learn and apply than some forms of “optimal contract”. This confirms the same findings as Söderblom (2016). In a Finnish context of early stage venture capital investments, this table can be used as guide, portraying what to practically be aware of the initial process. The table also displays a unique combination of theories that lead to the practical implications of this research.
This confirms the third proposition of this research, by finding the practical implications to the context.

As both this research and Sahlman (1990) confirms, entrepreneurs in early stage venture might be over-optimistic and uneducatedly agree to unfavorable contract terms, the figure above will hopefully serve as a practical tool for entrepreneurs seeking early stage venture capital funding.

### 8.2 Additional contributions

The research had clear aims of contributions from the beginning, divided into three aims, empirical, theoretical and practical. These were answered successfully through the research questions. In addition to the planned contribution, the research ended up with additional theoretical and methodologic contributions which are presented below.

**Strategical and operational autonomy/control**

This research brought out the discussion of both autonomy and control. Without planning, the research suggests a differentiation of autonomy and control into two components in this context: Operational autonomy/control and Strategical autonomy/control. In previous research regarding the topic, autonomy has not been divided into different components and used consequently in an organizational context.

This research contributes by separating these two into different components. This will hopefully provide a more nuanced and detailed discussion about autonomy and control in the future.

**Methodologic contributions**

This study used the unique method of a dyad study (Söderholm, 2016). As Söderholm’s (2016) research, this dyad study proved to be successful in the context of venture capital in Finland. The dyad has proven to be a methodological contribution by finding academic value through the contrast of the dyad study. One concrete example is the power moves utilized by the venture capital companies, which were not mentioned by the VC funds. This shows significant value and strengthens the argument to use this method in research similar to venture capital relationships or organizational relationships in general, conducted through an academic study. This research works as proof of a successful dyad study.
8.3 Limitations

This research focused to exploring and examining the relationships, which made the dyadic nature of the study optimal in this case. In a more extensive study in the future, a combination of quantitative and qualitative data could be useful to explore the topic even further. This could be conducted by benchmarking Kelly’s (2000) quantitative research.

This research limits itself to the Finnish context. As the empirical material and several interviewees point out, cross-border differences are huge.

8.4 Suggestions for further research

As mentioned above, cross-border differences seem to be huge in this context. For further research, a comparative research could be fruitful, to learn about cross-border differences.

At the end of every interview, the interviewee elaborated their thoughts concerning the future of the topics. A few suggested to examine further the automatization of the contractual process or deal flow. One VC associate claimed that the capital flow into companies will get easier and more accessible, using the term “Capital as a Service” to explain the phenomenon. How automatization and artificial intelligence plays into this picture could be interesting to explore in the future.

Maybe one of the clearest future research objects is the unique Finnish startup community. What makes it so unique? How does it affect the venture capital scene in Finland? What can others learn from the Finnish startup community and vice versa.

Like a few interviewee objects mentioned, contracts are made in case something goes wrong. It could be interesting to research how the contracts affect cases that have gone wrong.

The hidden messages and secrecy behind some of the clauses like anti-dilution and liquidation rights could be another interesting topic to explore further. How this would be done is still questionable. One alternative could be to look at several funding rounds and find conclusions based on the whole “funding cycle” of a company. As Bengtson & Sensory (2009) suggest, the nature of the contract changes vastly depending on the follow-up funding rounds.

Another interesting variable to look further into is the breaking point when the entrepreneur has to give up the autonomy of the company, regarding voting rights,
shares and board seats. It would be contributing to figure out the breaking point and what makes the entrepreneur give this up.

As mentioned in the theory section earlier, a new trend is rising among VC funds, which is taking care of the well-being of VC backed portfolio entrepreneurs (Icebreakers, 2019). This could be interesting to research further within the context of venture capital.

As the Dyad Alpha Portfolio Entrepreneur mentions, the hype surrounding VCs has not experienced a global recession. It could be interesting to spin-off theory in this research area as well.

8.5 Post-research comments

The process of the research has been successful. The timetable and ambition level have been kept as planned. Choosing to use the dyadic nature to the research was one of the best choices. It created a viable discussion between both the early stage VC fund and portfolio entrepreneur.

Reflecting and using the "FIBAN investment process" (2019) in this research made the researcher realize that it would contribute to building a similar holistic process to the venture capital scene. This master's thesis touched upon topics within the investment process of venture capital in Finland but did not paint the whole picture. This will hopefully be used as framework for future research (ibid.).
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ELECTRONICAL SOURCES

CABS (Chartered Association of Business Schools); https://charteredabs.org/academic-journal-guide-2018/; 16.12; 15:46


Sifted; https://sifted.eu/articles/slush-startups-tech-finland/?fbclid=IwAR28mXcdsGMKshpwy89cyMlsAuPvzZYJE8Qma-3n6kJzCWXhe3oYFVY1E; 29.11.2019; 16:00

ABBREVIATIONS

Ibid.: abbreviation of the Latin word ibidem (Harvard University Press, 2019)

SHA: Shareholder agreement (Kaplan & Strömberg, 2000)

SDT: Self-determination theory (Ryan & Deci, 2000)

VC: Venture capital (Gompers & Lerner, 2001)

CABS: Chartered Association of Business Schools (CABS, 2019)
APPENDIX 1

INTERVIEW GUIDE, Venture Capital company, Target length 60 minutes, Semi-structured

1. Introduction

**Double check recording device**

1.1 Thank you for this opportunity. Explain the nature of the research. Interview time, structure (semi-structured), anonymity, dyad.

1.2 Present myself.

1.3 Present my research (theory, method and research questions).

Note:

- This gives the interviewee an overview of the coming 60 min.

2. The interviewee’s background

2.1 Tell me about your background and what made you go into venture capital?

2.2 Shortly present the VC fund, which will be kept anonymous in the research.

Note:

- This section has more generalized questions to get the discussion going

3. Relationship of the VC and the Entrepreneur

3.1 During the initial investment process and contract building, have you ever been thinking about the issue of finding balance of control and autonomy in the relationship of the VC and entrepreneur? What are your thoughts on this?

3.2 As mentioned, when I presented the research, this study focuses on the balance of control and autonomy between the VC fund and the entrepreneur in early stage companies. From a control point of view, research (Ryan & Deci, 2000) points out that compliance, like contracts is one effective way to regulate the persons motivation but limits the autonomy. In practice, this research uses the contracts (term sheet & shareholders’ agreement) to measure the control and autonomy. This includes securities, cash flow rights, voting rights, board rights, liquidation rights, contingencies and other terms.
From a contractual perspective, which clauses would you say that are affecting the entrepreneur’s autonomy the most?

3.3 In the initial investment term sheet and shareholder agreement, do you have any general systematic framework when you build the initial term sheet and shareholder agreement?

3.4 How would you describe optimal contracts for an initial investment?

3.5 How would you describe a perfect balance between control and autonomy?

Note:

- This section will be the main discussion section, asking details related to the research questions.

4. Future

Would you say that any trend regarding the VC to entrepreneur relationship is changing? Looking at the next 5-10 years.

Note:

- This would wrap up the discussion
APPENDIX 2

INTERVIEW GUIDE, Portfolio company, Target length 60 minutes, Semi-structured

1. Introduction

Double check recording device

1.1 Thank you for this opportunity. Explain the nature of the research. Interview time, structure (semi-structured), anonymity, dyad.

1.2 Present myself.

1.3 Present my research (theory, method and research questions).

Note:

- This gives the interviewee an overview of the coming 60 min.

2. The interviewee’s background

2.1 Tell me about your background and what made you pursue the business idea.

2.2 Shortly present how you found the VC fund as partner, which will be kept anonymous in the research.

Note:

- This section has more generalized questions to get the discussion going

3. Relationship of the VC and the Entrepreneur

3.1 During the initial investment process and contract building, have you ever been thinking about the issue of finding balance of control and autonomy in the relationship of the VC and entrepreneur? What are your thoughts on this?

3.2 As mentioned, when I presented the research, this study focuses on the balance of control and autonomy between the VC fund and the entrepreneur in early stage companies. From a control point of view, research (Ryan & Deci, 2000) points out that compliance, like contracts is one effective way to regulate the persons motivation but limits the autonomy. In practice, this research uses the contracts (term sheet and shareholders’ agreement) to measure the control and autonomy. This includes securities, cash flow rights, voting rights, board rights, liquidation rights, contingencies and other terms.
From a contractual perspective, which clauses would you say that are affecting the entrepreneur’s autonomy the most?

3.3 In the initial investment term sheet and shareholder agreement, do you have any general systematic framework when you build the initial term sheet and shareholder agreement?

3.4 How would you describe optimal contracts for an initial investment?

3.5 How would you describe a perfect balance between control and autonomy?

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