Value-adding and Monitoring Activities of Venture Capital:A Synthesis Literature Review

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Abstract
This article provides a synthesis overview of the corporate governance literature related to the venture capital (VC) investors (or venture capitalists: VCs) bring to their portfolio companies, especially from the investment structuring to the exit date. The relationship between VC investors and investee firms has been studied mainly from the perspective of Agency Theory, through control mechanisms and incentives adopted by VC investors. However, this paper draws attention to the nature of non-financial value-added and analyzes the importance of cognitive and relational dimension of governance between the different types of VC investors. The studies reviewed in this article focus on two primary areas of inquiry: (i) active involvement of venture capitalists, (ii) venture capitalists monitoring. While much has been learned in each area, this review highlights several areas in which our understanding of the issues remains incomplete.
Keywords: Venture Capital. Private Equity. Value-added and monitoring. Governance.

1. Introduction

The financing of young innovative companies (YIC) has taken the attention of many researchers, government and non-governmental organizations. This interest is justified by its role in boosting growth (King and Levine 1993; Romain et al. 2004). These companies have special characteristics, which distinguish them from others; they have a high level of technology and specifically operate in the high-tech sector such as biotechnology, information technology sector and communication. However, these characteristics cannot be neutral; they are accompanied by a significant degree of risk that may influence the strategic and operational choices in this category of companies.

Indeed, regarding the financing plan, banks may not be able to meet the needs of innovative ventures featured by high risk, continuous monitoring and required support. In addition, venture capital is the only source of funding that provides both financial and non-financial assistance for innovative companies. This activism qualifies venture capitalists as active investors. This strong involvement aims to increase survival and success by developing the innovative capacity of these young companies.

In an article on the funding of R&D and technological innovation structures (Belin and Guille 2004) found that banks have little contribution in financing innovation. They found that the share of total debt given to YIC on average over the two years of the study (1998 - 1999) is less than 5%. However, banks tend to prefer speculation rather than to invest capital in innovative companies.

The venture capital financing initially appeared in the US in the 1940s and spread to Europe in the 1980s and where it knew a significant development, in the 1990s it emerge in other parts of the world, Asia, Central America, Middle East and Africa, and towards the end became a global financial phenomenon. In this regard, a number of fast growing companies operating in technology were financed by private equity, like Amazon.com, Apple Computer, Intel, Oracle, Skype, Business objects, 3Com, Yahoo !, Starbucks or Staples and Facebook.

In addition to government initiatives to encourage the spirit of innovation, Private Equity appears as a method of financing which was rationally developed to maximize the financial and non-financial structure of this class of business. It is defined by the Moroccan Association of Venture capitalists (AMIC) as a financial business of making a stake (as capital, debt securities convertible or not, as well as advances on partners' current accounts) for a fixed term in unlisted companies in need of equity or quasi-equity (AMIC, 2013).

Private equity is available in several forms including venture capital, and have frequently been divided into venture capital (VC) and Buyouts, VC- the, according to Sahman (1990, p. 473) “professionally managed pool of capital that is invested in equity-linked securities of private ventures at various stages in their development ” .

Since the beginning of 1993 and until the bursting of the Internet bubble, the amounts invested by private equity grew in both national and international level. After the collapse of the financial markets specialized in growth stocks, these investments have stabilized. According to the annual report of the Moroccan Association of Venture capitalists (AMIC, 2013), approximately 34 funds were registered in mid-2006 at the AMIC and managed by 20 management companies including only three management companies specialized in venture capital. From 1995 to 1999, the private equity invested MAD 400 million and became MAD 8 billion in the end of 2011. These funds are mainly invested in development stage projects (with 59.37% of the amounts invested by the growth capital and only 10.44% of the venture capital in 2008).

2. Active involvement of venture capitalists

Several studies have highlighted the strong involvement of type "hand on" venture capitalists at strategic and managerial levels within the innovative invested companies. The venture capitalists involvement beyond the fund invested is often referred to “smart money”.

The nature of financial intervention of these investors (equity based financing) and specificities of businesses financed, typically innovative, that have been identified above (such as, the weakness of guarantee, the high level of risk, etc ...) oblige VCs to be actively involved in the firm’s management to ensure a high level of return on investment. Many authors have found that this type of financing is associated with an active role through strategic and managerial support in terms of marketing, strategic HRM, production management and also financially through financial arrangements and fundraising complementary (Bottazzi et al. 2008; Hellmann and Puri 2002; MacMillan et al. 1989; Niemann 2011; Sahlman 1990; Sapienza 1992; Sapienza and Timmons 1989; Subhash 2009).

Moreover, beyond the supportive activities provided by venture capitalists, (Denis 2004) indicates that these investors can potentially help the invested companies to raise additional funds by certifying the quality of a start-up. In the same vein, the empirical study by Hsu (2004) confirmed the proposition that entrepreneurs are willing to renounce higher valuation offers of their start-up in order to affiliate with the VCs with better reputations. Therefore, the main reason for venture capital fundraising is the non financial value-added of this investors in the post-investment phase (Manigart and Struyf 1997).

In a study on 173 young high-technology firms in Silicon Valley Hellmann and Puri (2002) confirm that VCs contribute to the development of new businesses. Their results highlight the support given to the construction of the internal organization. In addition, they found that obtaining venture capital financing is associated with a professionalization of start-ups on several dimensions: an important role in the modernization and restructuring of the recruitment policy and the adoption of stock options, the hiring of an experienced CEO, the professionalization of management teams, and the hiring of a vice-president of sales and marketing. Their results show that the venture-capital-backed firms are also more likely and faster to replace the founder with an outside CEO. This effect is very significant for companies that have nothing to show yet, fairly significant for companies with a product on the market, but insignificant for companies that have already gone public.

In addition, venture capitalists use their business networks to help the entrepreneur find suppliers, customers, and potential partners. Through this relationship capital of the venture capitalists, the entrepreneur’s accessibility to the external resources becomes easier. Thus, the amount of this non financial value- adding does not have the same intensity for all venture capital firms; this value-adding may vary depending on the venture capitalist characteristics and ability, venture needs and entrepreneur experience.

According to Bottazzi et al. (2008), independent venture capitalists are much more involved in their portfolio companies than captive (bank, corporate, or government-owned) or semi-captive firms. This category of investors requires a rate of return greater than captive firms (Manigart et al. 2002). Moreover, the involvements of venture capitalists are more important for companies in the early stage than others in later stage (Cumming et al. 2007). It’s also related to the geographical distance between the venture capitalist and the company (Lerner 1995; Sapienza et al. 1996).

In this regard, due to the abundance of works dealing with financing decision criteria used by venture capitalists, (Sapienza and Timmons 1989) tried searching situational variables that influence the roles played by private equity investors. The results of this research show that the experience of contractors, business development stage, the participation of venture capital in the capital explains the importance of the roles of private equity investors.

Bruton, Fried and Manigart (2005) argue that VC firms were shown to have the same basic roles in all regions (i.e. U.S., U.K., Continental Europe and Asia), but the relative importance of these roles varies:

[…Interpersonal roles are more important in the U.S. and Asia than in Europe. Strategic roles, other than financier, are much more important in the U.S. than in either Asia or Europe. On the other hand, the financier role is more important in Europe. Networking roles appear somewhat more important in Asia (p. 747)].

However, Venture capitalists may engage in a number of value-adding activities, such as monitoring, support, and control. Those activities are largely non-contractible, yet may have real consequences. Industry insiders frequently distinguish between ‘‘hands-on’’ versus ‘‘hands-off’’ investment styles, and stress the importance of investor activism. A recent report by the European Venture Capital Association (EVCA, 2005), for example, notes:

[The degree of activism of Private Equity and Venture Capital investors will vary according to the nature and structure of investments made and the investor should therefore ensure adequate involvement relative to the circumstances of a particular investment].

The involvement of venture capitalists in the invested companies can be used as a support by the venture team when managing various business risks and enhancing venture performance. However, this involvement is a device to protect the investors from agency problems related to the relationship between venture capitalists and theirs portfolio companies' managers.

3. Venture capitalists monitoring

Venture capital investing in innovative, new or growing businesses is associated with many risks and problems; such as asymmetric information problems, agency problems which risks to lead to substantial costs. Agency theory perspective of the venture capitalists-entrepreneur relationship is one of the most dominant approaches in analysing the relation between the parties in venture capital financing, because it leads to a deep analysis of agency problems and fills the gap between the theoretical framework of agency theory and the real word of venture capital industry.
Jensen and Meckling (1976) have defined an agency relationship as «... *a contract under which one or more persons (the principal(s)) engage another person (the agent) to perform some service on their behalf which involves delegating some decision making authority to the agent* ». In the case of the venture capital invested firm, venture capitalist is considered as the principal while the entrepreneur is viewed as the agent.

However, in this relationship, venture capitalists meet different agency problems: Moral Hazard, Adverse Selection, hold up problems, Fred-Rodin, Windows dressing, etc. Indeed these agency problems are the consequences of a separation between ownership and management (i.e. separating ownership and decision), this separation may lead to a divergence of interest between the principals (V C) and agent (CEO). This divergence is materialized by hiding or dissimilating information and the agent not acting according to the principal interest or requirements of the contractual arrangements.

In such a context of agency conflicts, opportunistic behaviour by managers may arise. Barney et al. (1994) distinguished between two types of opportunistic behaviour that may face venture capitalists: managerial opportunism and competitive opportunism.

The first category of opportunism results from the SME manager's commitment in some activities like spending too much money on research and development, paying high salaries or keeping poor performing managers working at the firm, which can reduce the wealth of venture capitalists through a limitation of the potential value creation in the invested firm.

The second category related to managers engaging in actions that reduce the wealth of venture capitalists by leaving their current firm and starting new competing firms, disclosing proprietary technology to competing firms, or acting as advisors to competing firms.

According to Barney et al. (1994) venture capitalists will guard themselves from managerial opportunism by insisting on contractual covenants that make it easier for them to monitor, and if necessary, change current managerial actions.

Starting from an information asymmetry characterized by imperfect appreciation of the efforts made by the manager (the agent) and incomplete contract, we can distinguish between two types of opportunism that may arise in the context of the venture capitalists-entrepreneur relationship: opportunism ex ante and ex post opportunism.

The ex-ante opportunism (adverse selection) : is inspired by the concept given to the adverse selection by the founder of imperfect information theory Akerlof (1970). This means an information asymmetry between the entrepreneur (agent) who has a good quality of information about the project and its management team, and venture capitalist (VCs). The VCs don't have the true information about the future cash flows of the project and the ability of the management team to execute the business plan according to the requirements of the contract as elaborated the first round (or in the beginning of each round).

For example, the entrepreneur-manager may hide the income generated by his company in an investment round to secure financing in the next round on the assumption that the venture capitalist cannot observe the effort perfectly.

In venture capital financing, adverse selection refers to circumstances in which the management can hide private information about any intrinsic characteristics that might be relevant to the performance of a venture-capital-backed company.

The ex-post opportunism (moral hazard): this type of opportunism refers to the idea that, the parties of partnerships under certain circumstance can take actions, which cannot be verified or mitigated through the use of contracts.

This opportunism appears after venture capital funding, i.e. at the time of venture capital contracts execution. This risk refers to a situation where the management (agent) seeks to betray venture capitalist (principal) and violate the terms agreed in the contract since the venture capitalist cannot control all his actions. For example, the entrepreneur-manager may seek to focus on activities / products that are converged with his own interests so that option has no use for the company.

In this regard, the venture capitalists focus on two dimensions of corporate governance. The first is a cognitive system of governance based on assistance and exchange of competencies and cognitive resources. The second is a disciplinary system of governance, based on the mechanisms of incentives and control.

These governance mechanisms are used to mitigate the risks faced by VCs when financing innovative businesses and to monitor the portfolio company in order to better create and share value between all stakeholders.

On the other hand, in a study conducted by Mebarek (2003) on the governance practice in African enterprises indicates that a judicious mixing of venture capital financing in the capital structure of a company helps venture capitalists in achieving a higher level of transparency and minimising information asymmetry in the invested companies.

The involvement of venture capitalists in corporate governance and their active role "hands on" distinguish them from the traditional financial intermediation. Such involvement in governance begins at the time of contract design, to the extent that such contracts (or arrangements) are used to protect the venture capitalist and to be executed according to the performance of the company(the use of penalties for underperformance) (Sahlman 1990).

Moreover, other studies have focused on the extent to which the governance adopted by venture capital investors affect deeply the innovation process of a start-up directly or indirectly (Strömsten and Waluszewski 2012), and that this process of innovation influences the degree of venture capitalists involvement in the invested companies (Sapienza 1992).

Since venture capitalists play a central role in the governance' system of the fast growing entrepreneurial firms (Gabrielsson and Huse 2002; Rosenstein et al. 1993; Sapienza et al. 1996; Wirtz 2011), the table below synthesizes the mechanisms governance adopted in the context of venture capital financing:

Table 1 : Typical governance system for fast growing entrepreneurial firms

	Specific mechanisms	Non-specific mechanisms
Intentional mechanisms	– Direct stockholder control (specifically venture capitalists with frequent face-to-face interactions) – Investment agreements, business plan, etc. (Kaplan and Strömberg 2004) – Management team (TMT) (composition, formal allocation of responsibilities) – Board of Directors (proportion of external members including venture capitalists; diversity of functional experience)	– Legal and regulatory environment (regulations concerning capital investors, listing requirements, existence of a specific organized market, such as Alternext in France) – Existence of an organized profession of capital investors (recent in Europe but growing rapidly (Sapienza et al. 1996)
Spontaneous mechanisms	– Culture of decision-making by the management team (practice of power, dominant logic, political coalitions vs. valorization of competence) – Board process – Network of personal relationships among directors – Network of personal relationships among managers	– Network of venture capitalists (in finance, industry and politics) – Managerial labor market (animated by venture capitalists, sometimes the driving force in the replacement of start-up managers and in the professionalism of management teams) – Business culture that more or less values risk-taking (more in the early stage in the U.S. than in France) – Investors' dominant investor philosophy: Hands on or hands off

Source: Adopted by Wirtz (2011, p. 433) from Charreaux (1997, p. 427)

In the rest of this section, we describe and discuss some specific governance mechanisms typically used by Venture Capitalists:

3.1. Convertible securities

The innovative nature of funded targets raises equity investors to choose a more appropriate legal form with the aim of ensuring the optimal contract binding them with entrepreneurs of young companies. Indeed, the venture capital participation most commonly takes the form of convertible securities stock (Sahlman 1990; Cumming and Johan 2007; Kaplan and Strömberg, 2000). These convertible securities may help to implement optimal monitoring mechanisms by mitigating entrepreneurial signal manipulation (Cornelli and Yosha 2003).

Kaplan and Strömberg (2000) identify convertible preferred stock as the most often used security. Moreover, these convertible securities may facilitate intense monitoring and a large number of disagreements between the VC and the entrepreneur Cumming and Johan (2007). According to Gompers (1999), these convertible securities, helps encourage the entrepreneur to exert the proper effort and avoid inappropriate risk taking.

Hege et al. (2003) shows that that the US VCs perform better than European ones. The authors suggest that the use of convertibles may explain this difference in performances. Which reduces the importance of the manager shareholder agency problem, hence increases the performance. Indeed, the securities are more optimal allocation of flow right to reach high performance efforts from by the contractor (Schmidt 2003). However, in terms of their usefulness, firstly these titles encourage entrepreneurs to invest significant effort in the company compared to the case where the capital structure is mixed. On the other hand, in a study focused on a sample of 121 investment rounds in 74 entrepreneurial firms from 14 VC funds in 7 European countries (Belgium, Denmark, Germany, Hungary, Italy, Portugal, The Netherlands). Cumming and Johan (2007) found a positive correlation between the VCs' effort on advice and the use of convertible securities. This same study shows that when convertible debt or preferred equity is used, VCs provide on average 10% more contribution in terms of advice. Further, the VC financing theories suggest that their contracts include an automatic conversion provisions (e.g, Bengtsson and Sensoy 2011; Cumming and Johan 2007; Kaplan and Strömberg 2000; Sahlman 1990). In particular, the use of convertible securities allows the venture capitalist to automatically converts "convertible debt, convertible preferred stock, or a class of common stock" into common stock if performance is sufficiently good and under some specific conditions.

3.2. Shareholder agreement

The participation in the capital of innovative companies makes venture capitalists face a range of business and agency risks. These risks can be eliminated or transferred by the adoption of an optimal legal structure. To structure their relationship with the companies financed contractors, venture capitalists use the shareholders agreement; an extra-statutory and confidential document to balance the power between shareholders and managers and the rights of investors (venture capitalists), regardless of their capital share (Battini 2000). The shareholder agreement is a contract which organizes the obligations and the rights of the company with the existing shareholders and new investors and particularly to control the investment made by venture capitalist firms. Bengtsson and Ravid (2011) argued that contracts are less harsh if the start-up is located in a region with a larger VC market, or if the geographical distance between the VC and the company is shorter. Their results highlight the effect of distance on monitoring of venture capital backed firms.

3.3. Syndication

Many research papers were interested in syndication, a specific governance mechanism used in venture capital industry; it is a co-investment by two or more private equity firms. The literature on venture capital investment focused on the motivations that make VC firms syndicate their deals. However, this literature advances two major reasons for the syndication; a financial reason is based on the traditional view of risk sharing and diversification of venture capitalists business portfolio, and has aims to achieve an optimum couple profitability/risk (Admati and Pfleiderer 1994; Manigart et al. 2006). The other reason the syndication from a resource-based view[5] is considers syndication as an alliance to access other venture capitalists' various skills and share useful information in the selection and management of invested projects.

However, syndication is assumed to be positively correlated with performance. Dal-Pont-Legrand and Pommet (2010) argue that the nature of syndication matters: it has a direct impact on the decision to (re)finance innovative projects. They also discuss the condition under which the syndication for expertise was more profitable than the one for the pure risk diversification purpose.

3.4.Staged financing

The equity provision by venture capitalists in the invested company is not done in one round, but in a staged manner. This practice has been widely adopted by venture capitalists and called the "sequential financing" or "Staged financing", a specific control lever in the private equity industry, which aims to reduce information asymmetry, in this regard (Gompers 1995; Sahlman 1990) indicate that the structuring of funds provided in several financing rounds can limit the information asymmetry and asset risk.

The effect of staged financing in reducing information asymmetry is justified by the fact that the venture capitalists can increase their understanding of the invested firms from one round to another. By funding a company with several investment rounds, it becomes less risky during development (Barry et al. 1990).

Wang and Zhou (2004) found evidence that staged financing can achieve high efficiency, especially for highly promising ventures. It plays also a crucial role in reducing risks and controlling moral hazard. In particular, staged financing induces a higher effort from the entrepreneur.

Tian (2011), meanwhile, said that this type of financing provides protection against agency risks and to

[5] Bernile et al. (2007); Brander et al (2002); Cumming et al. (2007); Dal-Pont-Legrand and Pommet (2010); Desbrières (2001); Lockett and Wright (2001); Wright (2002); Wright and Lockett (2002), (2003).

face the hold-up problem, by reducing the entrepreneur's incentives to leave the firm for a new career; Which allows venture capitalists periodically to evaluate an investment and abandon it if the expected net present value turns negative (Barry et al. 1990). Tian (2011) further argued that investors located farther away from an entrepreneurial firm tend to finance the firm using a larger number of financing rounds, shorter durations between successive rounds, and investing a smaller amount in each round.

These results could be explained by the fact that in the case of a short distance between the venture capitalists and the invested company; the investors supervise easily the achievements of the goals fixed at the beginning of each round. In trying to explain the influence of the geographic distance on venture capitalists involvement (Sapienza and Timmons 1989) indicate that when VCs make investments in early stage ventures, they much prefer to invest in ventures located nearby in order to facilitate involvement.

3.5. Social interaction

Several studies have tried to analyse the governance of companies financed by venture capitalists through its structural mechanisms, such as the ownership structure of companies and; the Board of Directors composition. Barney et al. (1989) showed that a high level of business and agency risk is associated with a well-developed governance structure adopted by venture capitalists to control and monitor managers. Several authors have used the frequency of interpersonal interaction as a measure of governance due to the significant effect of the proximity between venture capitalists and managers (Niemann 2011; Sapienza and Gupta 1994; Sapienza et al. 1996; Wright and Lockett 2003).

For example, De-Clercq and Fried (2005) highlighted the importance of communication between venture capital firms (VCF) and portfolio companies as well as within the VCF in improving VCFs' value-added contributions towards their invested companies, and ultimately in enhancing the performance of these companies. The Interaction between managers and venture capital investor provides a business atmosphere propitious to create and share knowledge that will be used by managers for an efficient decision-making. This explains why does the social interaction between venture capitalists and managers of the portfolio firm companies positively affects ventures performance perceived by venture capitalists (De-Clercq and Sapienza, 2006).

3.6. Venture Capitalists' Representation on the Board

The Board of Directors is traditionally viewed as a strategic and effective governance lever for monitoring firms, and it has received lot of attention of many corporate governance researchers.

According to Charreaux (1997), both Board of Directors and the General Meeting of Shareholders represent specific mechanisms of governance. In the case of venture capital backed firms, the investors are usually represented on the board of directors and they typically receive no cash compensation for their responsibilities in the board of directors; if any cash is received by board members, it is paid to the partnership (Sahlman 1990). Barry et al. (1990) argue that the venture capitalists hold roughly one-third of the board seats in the invested company. On the other hand, Lerner (1995) highlighted that the distance between venture capitalists and the private firms is an important determinant of the board membership of venture capitalists. The venture capitalists play an important role in the decision making of the Board, including meetings of the members and the initiation of strategic choices (Bonini et al. 2012; Lockett et al. 2008; Niemann 2011; Sapienza and Gupta 1994; Wright and Lockett 2003).

3.7. Trust in venture capital-entrepreneur relationship

In spite of the use of many contractual arrangements that govern the relationship between venture capitalists and entrepreneurs, there is a need for the adoption of relational governance mechanisms in order to give a new life to the cooperation. As Arrow suggested before "*Virtually every commercial transaction has within itself an element of trust*" (1972: 357), by asymmetry, in the context of venture capital industry there is a need for a judicious mixing of trust into venture capital contracting to monitor entrepreneur – venture capitalists relationship with an optimal level of trust.

In general, the venture capital backed companies are innovative and operate in high technology industries such as biotechnology, information technology sector and communication. This greater level of innovation pursued by the venture is associated with a high level of risks, thus, a minimum level of trust is required in the relation between venture capitalists and entrepreneurs of the invested firms.

Additionally, several studies have highlighted the importance of trust in the relationship between partners in an environment characterized by a high level of risk and uncertainty (Das and Teng 1998; Deutsch 1958; Dyer and Chu, 2003; Schoorman et al. 2007).

Scholars have examined the importance of trust in venture capital industry, either in the relation between venture capitalist involved in a syndicated investments (Kollmann et al. 2014; Wright and Lockett (2003), or in their relation between the investors and the portfolio firms company (Bengtsson and Ravid 2011; Bottazzi et al. 2011; Zacharakis, et al. 2010; Duffner al. 2009; De Clercq and Sapienz, 2006; Bonnet 2005;

Shepherd and Zacharakis 2001). Therefore, trust can be considered in economic exchanges as a source of competitive advantage (Barney and Hansen 1994).

As a governance mechanism, trust is argued by Dyer and Chu (2003) to minimize the transaction cost and to have a mutual causal relationship with information sharing in a study conducted with a sample of 344 supplier-automaker exchange relationships in the U.S., Japan, and Korea. Trust between venture capitalists and entrepreneurs may enhance confidence in cooperation partner (Shepherd and Zacharakis 2001; McEvily and al. 2003; Das and Teng 1998; Ring and Van-de-Ven 1992). The previous relationship characterised by a mutual trust and openness of communication between venture capital and the entrepreneur are useful to enhance their mutual understanding. As noted by Sweeting (1991, p.619) "*Venture capitalists* [...] *were seeking to establish whether or not they could simply 'get along with' team members and trust them. The benefits of this mutual understanding and trust were evident even before the deal was made*".

In the context of venture capital, Shepherd and Zacharakis (2001) suggest that the parties need to balance between trust and control in order to achieve the optimal level of confidence in partner co-operation. Moreover, Bottazzi et al. (2011) find that trust among nations has a significant impact on the investment decisions of venture capital firms in a company in the specific country.

Accordingly, Cable and Shane (1997) have demonstrated that the cooperation between entrepreneurs and venture capitalists during the post-investment period is a necessary condition for the success of venture capital-backed start-ups. Thus, trust between parties is important to achieve cooperation in entrepreneur-venture capitalist association.

By empirically analysing the role of trust in the relationship between venture capitalist and entrepreneur, Duffner et al. (2009) found a significant mutual positive relationship between trust and success.

Das and Teng (1998) suggested "a higher trust level does not automatically dictate a lowering of the control level, and vice versa. All it means is more confidence in partner cooperation predicated upon certain levels of trust and control functioning as parallel phenomena." on the other hand, Bottazzi et al. (2011) found that contracts do not compensate for the lack of trust and that venture capitalists do not set up more sophisticated contracts in the absence of trust. Thus, both control and trust have are required for an optimal level of confidence in a partner relationship.

In addition, Nooteboom (2007) have argued that more trust does indeed allow for less control, but often trust and contract go together, because where contract ends trust must begin, and since trust has its limits, contracts are seldom left out.

Regardless of its relation with contract, the use of trust as a governance mechanism in the relation between venture capitalists and the venture capital backed firms should take into account the conditions under which trust will be a source of competitive advantage (Alvarez et al. 2003).

4. Discussion and conclusion

For the entrepreneurs and investors, this work enhances the knowledge about the structure and the organization of venture capital financing, by focusing, on the involvement of the venture capitalists in the governance of the backed companies. Both parties must prepare themselves for this involvement before structuring the investment, because it is a condition of their post-investment relationship. In terms of public efforts, the private equity industry should be supported by the government authorities for this type of funding promots employment, creates and boosting growth and hastens innovation. In addition, the venture capital funding plays a crucial role in supporting and developing the entrepreneurship's initiatives through their closeness to the entrepreneurial teams in their adventure. This can facilitate the vision for the government in its sector based policies and orientation, in encouraging private initiatives and supporting innovation.

Academically, this article highlights the structure of the governance system adopted by venture capitalists to deal with agency business problems in their portfolio companies. The boundaries of this system largely exceed the traditional framework developed by the agency theory. The agency theory model emphasises the divergence between the venture capitalist in terms of objectives and interests; this implies the use of some governance mechanisms based on the exercise of a strict financial and legal discipline featured with both incentives and control. However, and because of the importance of creating more value through the exchange of resources and knowledge in the invested company, the cognitive dimension of corporate governance may represent a new perspective to analyse the venture capital relationships. Therefore, the use of the cognitive lever for the case of entrepreneurial firms, May lead the corporate governance to play a central role in sustaining high levels of growth (Wirtz 2011). However, the cognitive cost due to the differences in knowledge between venture capitalists and entrepreneurs must be taken into consideration to ensure a real value creation. The cognitive dimensions of corporate governance get its foundation from knowledge-based and behavioural theories. It represents an alternative and complementarity approach to the dominant approaches (the contractual theories) of the governance when analysing the venture capital investments, specifically, the complementarity between the agency perspective and the resource-based view in analysing the relation between the venture-capitalists and the venture capital-backed firms are well-recognized (e.g. Croce et al. 2012; Meuleman et al. 2009).

Finally, by integrating both disciplinary and cognitive levers in the governance system of the entrepreneurial firms, venture may maximize its wealth for its various stakeholders and especially when the parties are socially embedded in local ties by cooperating in alliance with different corporative partnerships in an ecosystem managed by open communication, coordination, mutual trust, and long-term goals congruence.

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