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Does Reputational Risk Limit Opportunistic Behavior in the Venture Capital Industry?

Professor Katherine Litvak

Northwestern University School of Law

Friday, 29 May 2015

12:30 - 1:30 pm

Room 723, 7/F Cheng Yu Tung Tower

The University of Hong Kong

This seminar will have two parts. In the first part, Professor Litvak will provide the first systematic analysis of the role of reputation in limiting opportunistic behavior by venture capitalists ('VC') towards four types of counterparties: entrepreneurs, investors, other VCs, and buyers of VC-backed startups. Using a hand-collected database of lawsuits, she documents that more reputable VCs are less likely to be sued. Litigated VCs suffer declines in future business relative to carefully selected peers. These negative effects are stronger for more reputable VCs, and when VCs are defendants to multiple lawsuits or sued by entrepreneurs. These results suggest that reputational mechanisms help deter VC opportunism. In the second part, Professor Litvak will turn to a detailed analysis of one of the channels of reputation transmissions – capital withdrawal by limited partners. Professor Litvak finds that public pension funds respond to litigation-based shocks to VC reputation differently from other types of limited partners: instead of punishing litigated VCs by withdrawing capital, public pension funds increase their investment in litigated VCs, apparently to cover the shortfall caused by the exodus of other investors. These results indicate that politically-generated governance problems at the level of public pension funds reduce the effectiveness of investor governance in the venture capital industry.

Katherine Litvak's areas of expertise include venture capital, private equity, corporate and securities law, and corporate finance. She has previously served as an assistant professor at the University of Texas School of Law, a clerk for both the Hon. Ralph K. Winter of the U.S. Court of Appeals for the Second Circuit and the Hon. Frank H. Easterbrook of the U.S. Court of Appeals for the Seventh Circuit, as well as a John M. Olin Fellow in Law and Economics at Columbia Law School. Litvak received her BA from the University of California-Los Angeles, an MA from Harvard, her JD from Stanford Law School.

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email Flora Leung at fkleung@hku.hk to reserve a place.

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