Managing a Venture Capital Firm:
Lessons Learned from Industry Veterans

In May 2013, the National Venture Capital Association gathered a group of veteran venture capitalists who are currently serving as managing partners at their firms, or who have done so in the past, and asked them to share their experiences in that role. In the spirited conversation that followed, the VCs discussed what practices have worked well (and not so well) for them in putting together a portfolio, managing operations, and nurturing talent across multiple business cycles.

The purpose of this paper is to capture the insights and experiences shared by the panel participants and present them in a way that may benefit current managing partners at other firms, as well as general partners who aspire to join their ranks. For ease of reading, the major takeaways for each discussion topic appear in summary, followed by supporting quotes from participants. To enable the participants to speak freely and without fear of divulging proprietary or confidential information about their firms' internal practices, insights and opinions are presented without attribution. A list of panel participants can be found in Appendix A.

Across many topics, the participants agreed more frequently than one might expect from a group of fiercely independent VCs. That said, the group differed sharply on some issues, such as the efficacy of bringing in outside consultants, the desirability of complete consensus in portfolio pick, and instituting policies to govern use of cell phones and laptops in meetings. Above all, there was palpable enthusiasm about the venture capital field, despite its many challenges. As one participant put it, "Our business is to make lightning strike in a bottle, then do it repeatedly."

The "Right Stuff" for Managing Partner

Managing a venture capital firm requires a very particular set of skills—skills that differ from those that make for a successful venture investor. As one participant put it, "You can't just turn a rock star investor into a managing partner." Ironically, however, most GPs position themselves for management roles through their mastery of the latter skill set. Of course, performance is important, but aspiring managing partners should add leadership and relationship-management savvy—as well as a flair for process—to round out their management skills.

- "A managing partner needs to have the right disposition to work with limited partners, to think about marketing the firm, to take the helm on budgetary issues—in short, to have a grasp of how a VC firm can be run most effectively."
- "You need to be expert at the venture capital business: not just the deal stuff, but the other pieces of it, like the dynamics of working with limited partners and entrepreneurs, the terms, and being able to project the portfolio."
- "The managing partner should be a good process person and know what needs to be done to keep a team motivated."
- "There's a big difference between a leader and a manager. A leader has a vision and inspires others to help make that vision a reality. A manager understands process and how to keep everyone organized."
- "At the beginning of the firm, you need good leaders. Then at some point management skills become more important."

Despite the need for managing partners to broaden his or her focus, the discussion participants unanimously rejected the idea that the managing partner shouldn't do deals.

- "There should be an understanding that the managing partner may do fewer deals, because he or she is dealing with management issues. There should also be an agreement that the managing partner will be compensated for deals that he or she

helps with, but doesn't lead. That's only fair, because of the time and hassle of dealing with all the management issues that arise."

Making the Most of New Talent

The group agreed that mentoring young professionals was key to ensuring a firm's longevity, and discussed how they did it at their respective firms.

- "The key to development in the VC field is intuition-building. Young professionals need to see not only the good companies, but also the troubled ones, so they can better discern between them."

- "Venture capital is an apprenticeship business. The only way people learn the ropes is by following the example of those who have done it many times. So we team a senior investor with a junior professional on every deal."

- "We have a formal mentoring program where every associate gets assigned a partner for six months, then rotates through the firm so that each one has direct exposure to all the partners."

- "We have open meetings that all partners and associates sit in, and we invite younger people to portfolio-company board meetings as well."
- "Getting younger people involved at the board level also introduces them to the other venture capitalists we invest with. That exposes them to a wider variety of thinking on putting together deals and handling challenging situations."

In terms of written reviews, most of the roundtable participants' firms do performance reviews at least annually, and more than half conduct reviews every six months for younger professionals. "360" evaluations done by outside firms were viewed as valuable by about half of the group, but a few participants were skeptical or dismissive of their value.

The group also discussed the special challenges of bringing in new VC professionals who are not "young," such as successful entrepreneurs who have deep operating experience but are new to venture investing.

- "These people are moving from being a 'player' to a 'coach.' That's not always easy."

- “When you start in the business as a young person, you have time to prove yourself. When you come in later on, you want to hit the ground running.”

- “It might be smart not to allow them to make investments for a year. Until then, they can work closely with senior partners.”

- “These kinds of professionals can be dangerous, because they parallel the partners in age and business experience, but venture investing requires different skills than entrepreneurship.”

- “We sometimes bring in successful CEOs we have worked with in the past. After an exit, we’ll offer them office space for a year so they can learn more about the firm and figure out if they want to join us or [whether we want them to join us]. Often the individual discovers he or she doesn’t want to become a VC and starts a new enterprise—possibly one that we’ll invest in. Or they might join the firm, and by then they know about how things are done, and it works out great.”

Firm Culture

The roundtable participants agreed that it's important for venture capital firms to have mission statements and goals.

- "In the old days, VC firms were like a golf team: Everyone went out, did their thing, and posted their scores so the total could be added up. But today, business models have become important—especially being able to defend a model relative to the capital you're raising. If you're going to be competitive, your business model needs to be understood by every professional in the firm."
- "We created our firm to last 100 years, and we make decisions based on that goal."

Some participants pointed out that the most important component of firm culture is its people and how they work together.

- "You have to find people who have the right ethical compass and understand that this is a long-term business. You've got to earn your way in. If there's too great a sense of entitlement, it may not be a good cultural fit."
- "At our firm, we applaud responsibility and authenticity. It's terribly important to me personally, because I don't want to go to work every day in an environment where everyone's worrying about politics. Plus, it makes it hard to make decisions. That's why we're absolutely dogmatic about an authentic culture."
- "In my experience, an apolitical culture works best in a VC firm. That means everyone, down to the receptionists, owns mistakes very rapidly. When people know they're not going to be put in the penalty box, they'll readily come forward and say, 'That was me.' And that's how problems get resolved quickly."
- "It just takes one person to spoil an open, healthy firm culture. So we are pretty quick to fire people who are negative influences."

The discussion turned to the importance of instilling a culture of respect, both within the firm and for those with whom the firm works – including entrepreneurs, limited partners and key service providers such as lawyers, consultants, etc.

- “I don’t think you can legislate politeness and respect. But they’re important, and they come from a shared sense of values—values that come from the firm’s leadership.”
- “Firm management needs to lead by example. For instance, listening is important during partner meetings, which means no multi-tasking. Plus, if you’re trying to multi-task, you’re missing stuff.”
- “Give your entrepreneurs the attention they deserve. Show them that they are the most important part of the equation. Also, be polite. Remember, this is a service business.”

This topic sparked considerable passion among the group. In fact, several of the roundtable participants’ firms have a no-mobile device rule for partner meetings, or limit when devices can be used (i.e., individuals can use smartphones or other devices, but only for a minute at a time, or only for urgent exceptions such as incoming term sheets or family medical emergencies).

- “When someone starts typing on a laptop when a presenter is trying to make an impression, it tells everyone else, ‘Whatever he’s saying is not important.’ I hate that.”
- “I don’t believe in banning laptops, because sometimes the person typing is taking notes.”
- “The single biggest complaint I hear from entrepreneurs is that venture capitalists are on their BlackBerrys and laptops during board meetings.”
- “We need to be respectful to the entrepreneur. They’ve worked hard to get there. And we can’t give them 40 minutes of undivided attention? That’s pretty sad.”
- “I agree. The entrepreneur’s life is on the line. That deserves respect and attention.”

- “But when you cut people—especially young people—off from their devices, you can almost see their anxiety. And all of us do need to stay in touch.”

- “There’s been a push-back against constant connectedness in certain circles. At some business meals, the rule is that everybody puts their smartphone in the middle of the table. The first one who picks it up has to pay for the meal.”

The group chuckled at that last idea, and a few participants said they’d try it out.

Also on the topic of intra-firm interaction: The group agreed that annual or biannual off sites are a good time to review culture, business models, and core values. In addition, there’s usually some social or fun aspect that fosters team building. One participant pointed out that off sites also provide opportunities to identify people with exceptional potential: “Off site meetings are a great forum for big-picture discussions about the future of individuals’ careers, and the firm as a whole. They should happen regularly, either annually or biannually.”

Time Management

As one participant put it, “It’s important that everybody knows where everyone else is.” That’s why most VC firms use a public calendar.

- “When I’m acting in a managing-partner role, I care deeply about time management. The question in my mind is not specifically ‘Where are you spending your time?’ It’s more general: ‘As a firm, are we devoting enough time to activities that move the ball forward?’ For instance, does it make sense for us to go to all these conferences all the time?”

- “Our business model requires doing deals with the highest-quality firms, and I want our people to be spending time with other top-notch venture investors, getting an understanding of what they’re doing. To me, that’s a more effective use of time than going to speak at a conference, since many of those engagements tend to be more ego driven and less effective in moving the ball forward.”
- “When it comes to time, it’s important to stay flexible. This is a seven-day-a-week job.”

While some firms penalize partners if they are late for meetings—for instance charging a nominal amount for every minute a partner is tardy—the roundtable’s participants generally found that unnecessary.

- “In the beginning, we thought we might have to do something like that, but everybody who wanted to sell their deal to the rest of the partnership showed up early. So we found we didn’t need it.”

Career Advancement and Management Structure

The roundtable members agreed that succession planning is vital to the long-term health of a VC firm, and that leadership and compensation are essential to effective planning. Four out of the six participants' firms will move younger people up the "food chain" mid-fund, if performance warrants promotion. (For instance, if partner status is at 100 percent, there are tiers below that level that individuals would move up in 25-percent increments.) Another participant cited his firm's practice, in which a reserve of carry is set aside so it can be awarded to an individual for exceptional performance. If the reserve remains unallocated, it's split among the partners.

- "Great performance must be recognized and rewarded, no matter where in the firm it comes from."

- "Whatever system you use to incentivize people, it's important that it's clearly communicated. Salespeople perform when they understand their compensation system, and the same applies for venture professionals."

On the topic of compensation and advancement for younger professionals, transparency was deemed essential.

- "Younger partners want to be fairly compensated, but it's not all about money. They also want a voice. Firm management needs to provide ways for younger partners to play a role in key decisions."

- "It's important to clearly lay out the roadmap to partnership, including the way compensation progresses, the milestones that need to be met in order to advance, and the expected timeframe for advancement."

- "People today have faster expectations for advancement, so when you bring people into the firm, it's wise to ensure that everyone's on the same page."

- "Sometimes a young VC will come in and say 'We need to do a financing because I need a markup for my portfolio."

- "It takes handling about three funds for a younger person to make general partner at our firm. That translates to roughly nine years—possibly less for a more senior person coming in."

When it comes to compensation for top-tier management, there was general agreement that equality was desirable, though there was variation on that theme.

- "The core people at top should all be equal. And there should be a path for a younger person to become part of that group."

- "At my firm, we have a management company on top of the general partnership. The only people we invite into the management company are ones we think of as 'lifers.'" An extra percentage of our profits go into the management company to provide incentive to keep talented and loyal people in the firm."

- Another panelist suggested a different model: "Each fund stands on its own, so individual economics are determined by the fund or funds in which the person is participating. As long as the person participates in the fund, they benefit economically."

- "It works well if all partners are basically equal. Though the managing partner should probably be compensated a bit more for dealing with all the management issues."

- "The ideal tenure for a managing partner is 10 to 15 years, but it can be tough to get a managing partner to step down. If you have an equal compensation program in which the managing partner doesn't make much more than other senior partners, it makes stepping down a lot less painful."

The roundtable then tackled the potentially thorny issue of encouraging partners, including a managing partner, to leave.

- "It creates resentment when founding partners don't want to let go of their leadership role—especially when they are not contributing as much as more active and successful partners."

- “Raising a new fund can offer an opportunity to move out an underperforming managing partner. You can tell him or her that they won’t be part of the new fund because of performance—which is another reason regular reviews are a good idea, because then the data are there and performance concerns won’t come as a surprise. Or the other partners can make clear what needs to happen in terms of future performance if the managing partner is to continue on to the next fund. That not only gives notice, it gives the individual a chance to turn things around.”
- “We operate by consensus—up until we don’t have it. At that point, people start saying things like ‘You may want to put more money into that deal, but it’s not happening.’ Those kinds of messages start to shift the workplace environment, leading to change.”

Another participant criticized that approach as passive, but the VC advocating it said it was quite the opposite—and quite effective. When the talk shifted to vesting, seven years was the most common term cited, though periods of 10 to 15 years were also mentioned.“To me, seven years is right, since the fund will be invested and will have gone a long way toward achieving a return on the investments. To use farming terms, the fund will be in the ground and will be close to cultivation.”

- “We go for 10 years, because the whole idea is to harvest the portfolio. You don’t simply want to be there for the buy-in, but when the money comes out as well.”

Working with Limited Partners

On the topic of working with limited partners, the group generally agreed that it was important for a firm to build a diversified base.

- "We try to manage our LPs like a portfolio."
- "We look at it things geographically, trying to mix LPs from the U.S., Europe, and Asia. Then we consider the category of institution: for instance, endowments, state pensions, etc."

The discussion explored the importance of aligning the interests of VCs, LPs, and entrepreneurs. The long-term interests of all three groups should be considered, it was agreed.

- "My goal is to build great companies, and that helps the entrepreneur. But VC firms also need to focus on producing a return for their limited partners."
- "I get calls from LPs sometimes, and they say 'What are you doing for me this year? I need a markup…I get compensated on an annual basis.' There's a misalignment on the economics between LP and GP."

Communication was considered essential.

- "Truth and frequent communication are essential for positive LP relations. There are fewer misunderstandings."
- "LPs are not dumb. They want their money back. So you should explain things to them. For instance, you might say, 'Sure, this investment has been on the books for five or eight years, but we're really keen on this company, and here's why our patience will pay off.'"

Almost all the discussion participants had annual meetings with LPs, and some conducted quarterly portfolio reviews with all of their LPs, or an advisory committee comprised of the key ones. The meetings take place in person or via teleconference, and many of the participants' firms provided LPs with a brief written summary of the capital structure and progress of each company in the investment portfolio.

Instead of holding an annual meeting, one of the VC firms represented in the roundtable makes an effort to visit its LPs twice a year. Of course, he pointed out, the ability to conduct those types of visits depends on the number of LPs a firm has.

- "I was talking to an LP who was bemoaning the fact that the industry doesn't run on personal relationships as much as it used to. When I asked him how many partnerships he was involved with, he told me 450. I had to laugh, but it points to a reality: The VC industry has become larger and more institutionalized."

As some participants observed, LPs don't just scrutinize portfolios, but a VC's operations.

- "I get the LP's point of view. If GPs have not returned capital and have taken huge management fees, they have an absolute right to be cranky."

The Decision-Making Process

Some of the roundtable participants provided a quick overview of the decision-making process at their firms.

At VC Firm A, the full partnership does not vote on seed capital deals of less than 2 million, just the two general partners overseeing the process. On larger deals, everyone gets a chance to vote initially. There are three levels of votes: YE (for yes enthusiastic), YS (yes satisfactory), and N (no). Voting takes place every week, and the results are recorded. The majority rules when it comes to initial investments, while a two-thirds vote is required for a follow-on investment. At the end of the meeting, the general partners vote again to ensure they agree on how the full partnership voted. “So far, there hasn’t been a case where we voted against the larger group.”

VC Firm B no longer has each company present to the full partnership, because scheduling was difficult and the firm didn’t want to lose out on promising deals because of a slow decision-making process. The firm is diversified in terms of industry sectors, so each sector-specific group recommends a deal. Decisions require the approval from a representative of another group (for instance, if the life sciences team is advocating a deal, at least one IT partner needs to vote in its favor). Instead of seeking a 100 percent consensus, decisions are decided by a majority. “We want to have some dissenting voices.”

VC Firm C employs a one person / one vote strategy, which includes partners and some junior members. Even so, the majority rules. “We want younger people in the firm to feel comfortable to speak and disagree with more senior people.”

VC Firm D also aims for consensus on deals, though it recognizes that that approach works best in a firm like its own: a small one with a single office. If one person is uncomfortable about a deal, it’s up to the others to try to turn him or her around. If they can’t, the firm will pass on the deal. “If there’s opposition to a deal, then the people supporting it need to bring in enough data to beat the opposition into submission. If that doesn’t happen, we won’t do the deal.”

At VC Firm E, anyone within the partnership (partner to associate) can source a deal and bring it forward. If there’s interest, a more senior person is put on the deal. The goal is to have two senior partners actively working with one or two associates on each deal. When the partnership votes on a deal, the goal is consensus. There can be one dissenting vote, but if two people voice strong opposition to a deal, the firm passes on it. “We use the same criteria for follow-on

investments as we do new ones. We don't continue to support a company just because we've invested in the past. It has to merit further investment."

The group concurred that decisions for follow-on investments need to be rigorously made, and at many firms, the standard is a higher one.

- "Did the company achieve what they said they were going to achieve? If not, why not?"
- "I think a few years ago there was a more of an expectation that investors would automatically follow on, but today there's more scrutiny and rigor."

The roundtable's consensus was that inside rounds—where only existing investors participate in a follow-on investment—should be looked at even more closely than follow-on investments with outsiders joining in. The group agreed that inside rounds weren't the preferred option, but as one participant put it, "They're sometimes a necessity if you really believe in a company." In sectors where inside rounds are more typical, such as life sciences, they are generally planned in advance. "Managing reserves for such situations is very important," one participant observed.

On the topic of portfolio reviews, the participants agreed that regular assessments—for instance, on a weekly basis—help with planning, including ensuring that reserves will be available when needed.

Several firms assign reserves to deals at time of initial investment, so additional funding is available if needed. They then review the situation regularly, assessing factors such as a company's progress or changes in the syndicate doing the funding.

Most of the firms represented at the roundtable don't make significant strategy shifts mid-fund.

- "Allocations change, and that's fine as long as there is good communication to LPs about what's changing and why."

On the topic of planning a syndicate of the firms going in on an investment together, the group agreed that it was wise to try to control things as much as possible.

- "You need to be selective about who you do deals with, since that will impact your firm's reputation and hence, your future."

Advice for a Spin-Off

Asked what they'd say to a successful younger colleague who's opting to spin off and create his or her own fund, the roundtable came up with some interesting answers.

- "I'd ask, 'Have you really thought through what you want to do? What size firm works for you? What kind of partners? What sort of progression? And what's your 10-year-plan for the new firm?'"
- "The first question that springs to mind is, 'Who do you want to hang out with every day?' That's important for individual satisfaction, but it also impacts reputation. In this business, you're known by the company you keep."
- "My message would be simple: 'Don't forget who brought you to the dance. And call me when you do your first great deal.'"

Appendix A

Panel Participants

Norm Fogelsong, Institutional Venture Partners

Diana Frazier, FLAG Capital Management (moderator)

Joe Horowitz, Jafco Ventures

Dick Kramlich, New Enterprise Associates

Bob Latta, Wilson Sonsini Goodrich & Rosati

Terry McGuire, Polaris Partners

Ray Rothrock, Venrock

Craig Taylor, Alloy Ventures