



When do investors forgive entrepreneurs for lying?



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ABSTRACT

A growing literature suggests that some entrepreneurs lie to investors in order to improve the likelihood of acquiring resources needed for firm survival and growth. We propose a framework outlining the conditions that may enable an investor who has been told a lie by an entrepreneur to respond with forgiveness rather than by withdrawing from the relationship. Integrating the literatures on evolutionary psychology, forgiveness, and stakeholder theory we argue that investor's appraisals of expected relationship value and expected exploitation risk are the key antecedents to an investor's decision to forgive an entrepreneur's lie.

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1. Executive summary

Investors—defined as people who provide financial resources with an expectation of return on their investment—are critically important stakeholders for entrepreneurs whose most pressing task is to acquire resources needed for firm survival and growth. Accordingly, we would expect entrepreneurs to treat investors with respect and to provide an honest and accurate picture of the venture. However, in contrast to what we would expect, a growing literature suggests that entrepreneurs do not always share accurate representations of their venture. Put simply, some entrepreneurs present selected misinformation to prospective investors or deliberately use ambiguity to avoid disclosing aspects of a business that may create an unfavorable impression (Martens, Jennings, and Jennings, 2007).

This phenomenon of entrepreneurs deceiving their investors is evident in academic studies on the inaccurate stories and intentionally misleading information entrepreneurs provide (Lounsbury and Glynn, 2001; Rutherford et al., 2009) as well as practitioner reports (Kawasaki, 2008: 44) cataloging lies commonly told by entrepreneurs (e.g., “Our projections are conservative,” “No one else is doing what we are doing,” and “Hurry, because other venture capital firms are interested”). This line of research also coincides with emerging work noting the propensity of entrepreneurs to break rules, ignore guidelines, and pursue venture-related goals irrespective of moral virtue (for a review see Brenkert, 2009).

As an explanation, researchers note that these entrepreneurs may lie or engage in morally questionable behavior because they have not yet reached a point at which the firm is seen by potential investors as both understandable and permanent. Before reaching this point, investors are less likely to engage with the venture (Rutherford and Buller, 2007; Singh et al., 1986; Steverson et al., 2013; Zimmerman and Zeitz, 2002). This puts entrepreneurs in a quandary: lie to access the necessary resources or treat potential investors honestly and risk their refusal to invest.

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Stakeholder theory provides an argument that entrepreneurs could substantially benefit by establishing trusting and cooperative ties (Freeman, 1984). Firms that manage for stakeholders can create more value by getting their stakeholders to put forth greater effort and provide more nuanced information about their preferences (Harrison et al., 2010). In contrast, poor stakeholder treatment can destroy value and hurt the firm. For example, lying to an investor (a crucial stakeholder) can provoke moral outrage that results in retaliation, revenge, or avoidance. It follows that entrepreneurs who lie to investors should receive reduced value from the relationship and risk venture failure.

Interestingly, entrepreneurs who choose to lie may still build effective investor relationships (Rutherford et al., 2009) despite the violation of social norms (Steverson et al., 2013) and despite what stakeholder theory predicts (Freeman et al., 2010). This suggests that the entrepreneur–investor dyad is a context where the core propositions of stakeholder theory deserve closer scrutiny. The present conceptual contribution examines this topic and asks the question: Under what conditions will investors who could withdraw from the relationship, instead, choose to respond with forgiveness after suffering an entrepreneur's lie?

We submit that the present work is of interest to researchers and practitioners alike. From a theoretical perspective, we extend the logic of stakeholder theory by integrating the psychological conditions that facilitate forgiveness with specific types of organizational justice that may motivate investor behavior. From a practical perspective, this work outlines why entrepreneurs may lie as well as the processes through which forgiveness from investors for such a transgression may be achieved. Specifically, we note how, even after an investor learns of a lie, entrepreneurs can act to recover without suffering the expected negative effects. This research takes an important step towards a more complete understanding of the applicability of stakeholder theory in entrepreneurship as it relates to perceptions of justice and forgiveness.

2. Introduction

“An experienced VC fund manager I have known for years told me recently that if a person does not know how to seriously twist the truth from time to time, he (she) cannot be an entrepreneur”.

[Isenberg, 2010]

“In Silicon Valley, you can tell that a person is pitching because her lips are moving”.

[Kawasaki, 2008]

“Nearly every entrepreneur exaggerates his or her company's size to impress clients”.

[Fried, 2011]

The task of acquiring resources is one of the defining roles of an entrepreneur (Pollack et al., 2012). It is only through establishing relationships that the entrepreneur can entice investors—defined as people who provide financial resources with an expectation of return on their investment—to provide the resources that are needed for a venture's survival and growth (Nagy et al., 2012; Sapienza and Korsgaard, 1996). The primary way in which entrepreneurs entice investors to provide resources is a business pitch—a cohesive narrative woven together from written and verbally communicated information that helps an investor to understand the entrepreneur's business (Pollack et al., 2012). This entrepreneur–investor interaction helps clarify, in the mind of the investor, the viability of a venture.

Stakeholder theory suggests that the way to foster beneficial relationships is to establish trusting and cooperative ties. In turn, firms that deal with investors “on the basis of mutual trust and cooperation” gain a competitive advantage relative to firms that do not (Jones, 1995: 422). From this perspective we would expect entrepreneurs to act respectfully, honestly, and ethically when presenting written and verbally delivered information to investors. In contrast to what we expect, however, a growing literature points to a phenomenon in which some entrepreneurs deceive investors (e.g., Martens et al., 2007; Rutherford et al., 2009).

Entrepreneurs present selected information to prospective investors and sometimes deliberately use ambiguity to avoid disclosing aspects of a business that may create an unfavorable impression. For example, “...the narratives contained phrases suggesting that a firm was an established leader even though, in our opinion, insufficient factual information was presented to support such a claim” (Martens et al., 2007: 1111). Recent studies support the existence of this phenomenon: that some entrepreneurs lie to investors by sharing inaccurate stories and intentionally misleading information (e.g., Aerts and Cheng, 2012; Herzenstein et al., 2011; Lounsbury and Glynn, 2001). In describing the state of the practice, Guy Kawasaki cataloged the top eleven lies entrepreneurs tell investors—he notes that, “... just about every entrepreneur who pitches me tells at least four of these eleven lies” (Kawasaki, 2008: 44). Examples of lies Kawasaki (2008) describes are: “Our projections are conservative,” “No one else is doing what we are doing,” and “Hurry, because other venture capital firms are interested” (Sherman, 2012).

One motivation for such lies is clear—these entrepreneurs have not yet reached a point at which the firm begins authentically sending credible signals to prospective investors that the firm is acceptable, appropriate, and desirable (Rutherford and Buller, 2007; Singh et al., 1986). Accordingly, investors are less likely to engage with the venture (Zimmerman and Zeitz, 2002). To compensate, entrepreneurs may lie to prospective investors. For example:

“Some years ago I worked with an entrepreneur who was raising his first \$10 million of VC investment (“Series A”), without which the company could not proceed. One key element in the investment pitch was a strategic relationship with a multinational

customer. The day before finalizing the investment, the customer announced that they were backing out. I advised my friend to inform his investors, but he chose to let them know at the first board meeting after the money was in the bank. I don't know how he told them, but there was no apparent negative fallout".

[(Isenberg, 2010)]

An entrepreneur who willfully deceives investors violates social and moral norms of justice and earns a reputation for untrustworthy behavior (Freeman, 1984). For example, a firm that enrolls an investor with a lie risks initiating moral outrage and permanent damage to the ongoing relationship (Lewicki, 1983). From a stakeholder theory perspective, the standard predicted outcome is value destruction and, quite possibly, venture failure. However, even though stakeholder research provides strong support for this outcome (Freeman et al., 2010), it may be the case that deceitful entrepreneurs still manage to build an effective network of investor relationships (Rutherford et al., 2009). Thus, the entrepreneur–investor dyad is a context in which propositions at the core of stakeholder theory require refining.

The purpose of this paper is to examine the conditions under which entrepreneurs who are caught lying to an investor might still achieve a value-creating relationship. Though scholars have begun studying the unethical (and ethical) behavior of entrepreneurs (e.g., Babalola, 2009; Brenkert, 2009; Bucar et al., 2003; Fassin, 2005; Seglin, 1998), a large gap remains with regard to the consequences of unethical behavior (specifically lies). Thus, examining how investors may respond to such transgressions is a crucial, unexplored, area of work (e.g., Lounsbury and Glynn, 2001; Martens et al., 2007). We draw on an evolutionary psychology-based perspective of forgiveness and present a framework in which, in response to an entrepreneur's lie, an investor considers whether or not the relationship with the entrepreneur, ultimately, helps or threatens her goal achievement. Our overall model is depicted in Fig. 1. We examine two key antecedents to investor's forgiveness: (a) expected relationship value, and (b) expected exploitation risk.

We proceed as follows. First, we examine the literature related to interpersonal communication and lying, in general, as well as the specific phenomenon of lying in the entrepreneur–investor context. Then, we discuss stakeholder theory and responses to an entrepreneur's lie. Next, we integrate arguments from evolutionary psychology and stakeholder theory that explain the conditions under which an entrepreneur's lie may be forgiven. In closing, we discuss the implications for stakeholder theory and the entrepreneur–investor relationship as well as directions for future research.

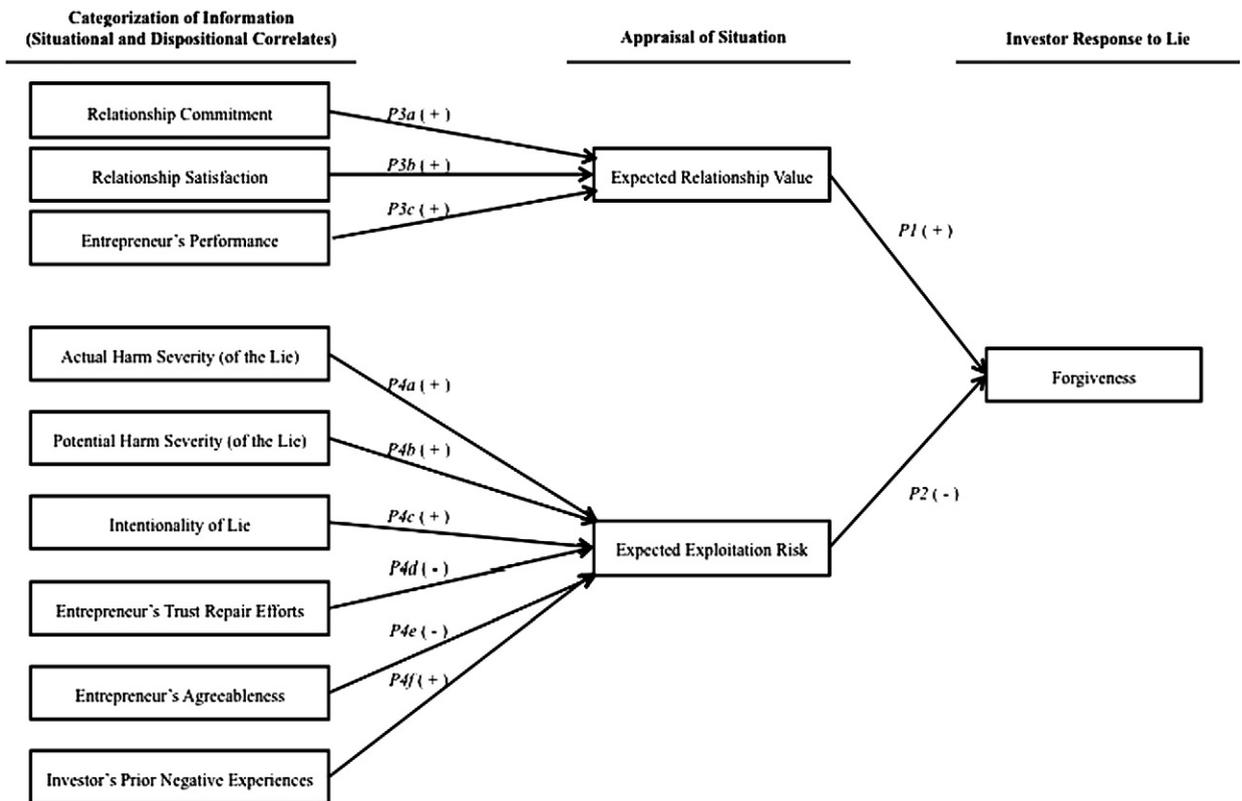


Fig. 1. The Categorization-Appraisal-Response (CAR) model illustrating the correlates of expected relationship value and expected exploitation risk and their subsequent relationships to investor forgiveness.

3. Theoretical background

“...Communicators frequently decide that honesty is not the best policy. Job applicants overstate their qualifications to make a favorable impression, spouses lie to minimize relational conflict, students claim purchased term papers as their own work, public officials conceal their true motives to representatives of foreign governments”.

[Buller and Burgoon, 1996: 203]

3.1. Interpersonal communication and deception

People lie to one another. The ability to lie and to tell when a lie may be warranted are core skills that humans acquire (Ford, 1995). Though estimates as to the percentage of conversations that include lies differ, from twenty-five percent (e.g., Buller and Burgoon, 1996) to sixty-percent (Turner et al., 1975), the consensus is clear: the truth is that people do lie to one another in a variety of contexts (Camden et al., 1984).

Lies are especially common in contexts where being viewed in a positive way is crucial to important outcomes—these are high-stake environments. For example, several studies indicate that people lie in job interviews and romantic relationships. Estimates as to the number of job candidates who lie range from twenty-eight to seventy-five percent (Levashina and Campion, 2007). It is not surprising that individuals lie here because there are important outcomes at stake: the applicant wants a job and is willing to manage the impression he or she makes on the interviewer (Stevens and Kristof, 1995; Weiss and Feldman, 2006). Similarly, in romantic relationships, another high-stake context, data show that almost all individuals (ninety-two percent) admit having lied (Cole, 2001), especially when trying to get a first date (Hall et al., 2010; Pontari and Schlenker, 2004; Rowatt et al., 1999). Some estimates suggest that people tell an average of one lie per day to romantic partners (DePaulo et al., 2004).

In this manuscript, we examine the nature of “interpersonal communication” between entrepreneurs and investors – the “dynamic exchange of messages between two (or more) people” (Buller and Burgoon, 1996: 205). We use lying and deception interchangeably to represent a “...message knowingly transmitted by a sender to foster a false belief or conclusion by the receiver” (Buller and Burgoon, 1996: 205). This conceptualization of lying and deception rules out the occasional mistake or unintended lie (Buller and Burgoon, 1996; Ekman, 1985). Drawing on these conceptualizations, in the following sections we examine the nature of the entrepreneur–investor dyad from an interpersonal communication perspective.

3.2. Lies in a broader theoretical context of social influence and impression management

An entrepreneur's temptation to tell a lie is rooted in a motivation to appear to conform to investor's expectations so they can gain access to financial resources needed for firm survival and growth. In short, entrepreneurs are attempting to positively influence the perceptions of the potential investor. Below, we situate the phenomenon of lying in the theoretical contexts of social influence (Cialdini, 2001a,b) and impression management (Bolino et al., 2008; Bozeman and Kacmar, 1997; Leary and Kowalski, 1990).

Consensus in the field of psychology holds that individuals care how others perceive them. Accordingly, each of us considers how we present ourselves to others because this impacts whether they do what we would like them to do (Cialdini, 2001b). The behavior we engage in when presenting ourselves to others is impression management. Impression management is effort by an individual “to create, maintain, protect, or otherwise alter an image held by a target audience” (Bolino et al., 2008: 1080). The earliest work on impression management was explored within a framework where individuals were characterized as actors who play a role (e.g., Goffman, 1959) in order to achieve specific goals such as “social and material outcomes, self-esteem maintenance, [and] identity development” (Leary and Kowalski, 1990: 38).

Recent research built on the actor–audience model (Goffman, 1959) to describe the entrepreneur–investor dyadic relationship (Nagy et al., 2012). Specifically, Nagy et al. (2012) experimentally induced the presentation an entrepreneur gave (via a video and a resume) to a potential investor. Results supported the premise that entrepreneurs who displayed enhanced credentials on their resume and who used impression management tactics (e.g., ingratiation, self-promotion, exemplification) would elicit greater perceptions of legitimacy from the audience (in this case cognitive legitimacy from potential investors).

Notably, Nagy et al. (2012) focused on the behaviors of ingratiation, self-promotion, and exemplification. These, however, are only three of 31 distinct impression management behaviors and tactics identified by Bolino et al. (2008). Within the Bolino et al. (2008) categorization, the behavior of lying would fall under a very extreme version of self-enhancement: making an entrepreneur's “best characteristics salient” even if sometimes fictitious (Bolino et al., 2008: 1082). Entrepreneurs who tell lies to intentionally deceive potential investors exceed the boundary of the domain of impression management and influence, however. In the following section, we review the literature related to lies in the entrepreneur–investor context.

3.3. Lies in the entrepreneur–investor context

Entrepreneurs seek resources they do not currently control in order to exploit a perceived market opportunity (Shane and Venkataraman, 2000). However, investors are only likely to achieve their goals by investing in firms that are legitimately

acceptable, appropriate, and desirable (Zimmerman and Zeitz, 2002). A characteristic of entrepreneurial firms, though, is that prospective investors have limited information upon which to make this determination. This makes the legitimacy of an entrepreneurial firm difficult to discern. This information asymmetry as well as the potential for moral hazard (i.e., entrepreneurs acting in their own best interests regardless of the outcome for investors) plagues entrepreneurs and limits the ability of potential investors to gauge the legitimacy of ventures (Chua et al., 2011; Elitzur and Gaviols, 2003; Sapienza and Korsgaard, 1996).

Researchers suggest there are three main categories of legitimacy: cognitive (i.e., tacit judgment about the nature of a business), regulatory (i.e., conformance to laws and rules), and normative (i.e., relative judgment about a business compared to peers and competitors) (e.g., Shepherd and Zacharakis, 2003; Suchman, 1995). Furthermore, legitimacy is a stakeholder driven process because entrepreneurs cannot *take* legitimacy; it must be granted by investors. From an investor's perspective, a venture may be granted legitimacy only when it is deemed understandable as well as permanent (i.e., not on the brink of failure) (Aldrich and Fiol, 1994).

This presents a paradoxical challenge for entrepreneurs: How can you signal to a prospective investor that you are valid and valuable if no other (or very few) investors have granted you legitimacy by engaging with your venture? In this situation, the fact that entrepreneurs may have private information that is difficult for desired investors to verify provides the opportunity, which some entrepreneurs take, to be deceptive. This raises the question: What happens when investors discover that an entrepreneur has lied to them? Below, we briefly review stakeholder theory and its use of justice norms to examine investor responses.

3.4. Stakeholder theory and investor responses to an entrepreneur's lies

Stakeholder theory, which explains how and why attending to stakeholders' interests improves the competitive performance of a firm, is built from an explicit recognition and inclusion of the moral and social norms of society (Freeman, 1984). While the theory offers guidance regarding which stakeholder relationships are most salient in value creation, it currently falls short in its explanation of "stakeholder engagement strategies" in various specific settings (Freeman et al., 2010: 287). For example, stakeholder theory, on its face, is currently unprepared to accommodate the phenomenon in which an investor forgives an entrepreneur for lying.

However, we find promise in recent stakeholder theory developments that build on the justice literature to explain the types of value stakeholders expect from a firm and how they respond to perceptions of fairness (e.g., Bosse et al., 2009; Harrison et al., 2010). Stakeholders assess value in distributional, procedural, and interactional terms. Distributional justice accounts for the perceived fairness of material value allocations such as money and time. Procedural justice is the perceived fairness of the decision-making process (Thibaut and Walker, 1975). A fair process is characterized by, among other things, the use of accurate information and the adherence to accepted standards of ethics or morality (Colquitt et al., 2001; Sapienza and Korsgaard, 1996). Interactional justice captures the stakeholder's perceptions of how she is treated interpersonally in terms of dignity and respect (Bies and Moag, 1986). Stakeholders continually update their perception of fairness by reassessing tradeoffs among the distributional, procedural, and interactional justice they receive (Colquitt et al., 2001).

When stakeholders perceive they are receiving fairness beyond their expectation, they positively reciprocate by putting forth greater than expected effort on behalf of the firm. The honesty and completeness of information a firm shares with stakeholders are critical to stakeholder perceptions of justice and to building trusting relationships (Strong et al., 2001). This trust facilitates the mutual sharing of nuanced private information about needs and demands that helps to reveal additional business opportunities (Harrison et al., 2010) such as investing additional funds when needed or introducing the entrepreneur to additional investors. Alternatively, stakeholders negatively reciprocate when they perceive that the firm is being unfair towards them. For example, an investor can negatively reciprocate by refusing to provide additional funding or refusing to provide a reference to other investors during additional rounds of financing.

Lying to stakeholders may violate all three types of justice and result in negative reciprocity that *diminishes* firm performance (Bosse et al., 2009). The investor's expectation for distributional justice is violated if the deceit does or will result in noticeably less material value for the investor. The lie can be perceived to violate procedural justice because it is intended to convey inaccurate information that influences the investor's decision-making process. Lying might also be perceived as a sign of disrespect, and therefore an interactional injustice, by some investors. Detecting that an ongoing relationship partner has lied can lead to moral outrage (Lewicki, 1983), destroy trust and cooperation (Shapiro and Bies, 1994), and irreversibly constrain future transactions (Bies and Tripp, 1995). The deceived party often senses an urge to punish the liar even if the lie did not result in a loss of value (Brandts and Charness, 2003).

Applying this framework, it is logical to predict that investors who find they have been lied to will typically seek justice through revenge—defined as seeking satisfaction by attempting to harm another (Govier, 2002)—and potentially withdrawing their support and resources. Losing a key investor relationship and suffering the resulting reputational damage could make it impossible to exploit an entrepreneur's perceived market opportunity. Thus, a key question is: Under what conditions can entrepreneurs who lie avoid this punishment from investors? In the next section we show how a framework of forgiveness addresses all three types of justice and, therefore, influences an investor's response toward the entrepreneur.

4. Investor's forgiveness: a Cognition-Appraisal-Response (CAR) model

"Revenge and forgiveness, we argue, have complementary biological functions: We posit that mechanisms for revenge are designed to deter harms, and that forgiveness mechanisms are designed to solve problems related to the preservation of valuable relationships despite the prior impositions of harm".

[McCullough, Kurzban, and Tabak, 2012: 2]

Our proposed model depicted in Fig. 1 acknowledges the correlates of both relationship value and exploitation risk and, ultimately, links the investor's appraisals of expected relationship value and expected exploitation risk with the decision to forgive. This suggests the presence of a multi-stage model. Within the forgiveness literature there is a lack of consensus as to the "stages" of forgiveness and whether it is a linear process or one with multiple feedback loops (e.g., relationship value and exploitation risk affect forgiveness which then, in turn, affects relationship value and exploitation risk; [Rusbult et al., 2005](#)). For the framework we propose, the extant literature on cognitive appraisal theory ([Lazarus, 1991](#); [Shweder, 1993](#)) is relevant.

Cognitive appraisal theory describes a multi-stage process where an individual categorizes her knowledge about an event, develops an appraisal of the situation (a primary appraisal of the relevance of the situation for her goals and a secondary appraisal of her ability to cope with the situation), and then acts in response ([Michl et al., 2009](#): 176). We have assimilated cognitive appraisal theory ([Lazarus, 1991](#)) with the current literature on forgiveness ([Fehr et al., 2010](#)) as both emphasize the importance of cognitions as well as emotions in predicting individuals' responses to events ([Fehr et al., 2010](#); [Lazarus, 2006](#); [Watson and Spence, 2007](#)). Across an array of research, data indicate that individuals' appraisals lead to subsequent behaviors. For example, cognitive appraisal theory has been used to explain consumer behavior (e.g., [Watson and Spence, 2007](#)), individuals' appraisals and responses to innovation ([Michl et al., 2009](#)) and individuals' appraisals of marketing decision options (e.g., [White et al., 2003](#)). The following sections provide further details on the multi-stage Categorization-Appraisal-Response (CAR) model we propose in Fig. 1.

4.1. Why are lies not always punished? Forgiveness, justice, and stakeholder theory

When an investor's sense of justice has suffered due to a lie, they are motivated to reestablish justice. Economic actors conceptualize two distinct ways to do this: through restorative justice or retributive justice ([Strelan et al., 2008](#)). The most direct form of punishing the transgressor and deterring future harm is through retributive justice such as terminating the relationship ([McCullough et al., 2010](#)). Evolutionary psychologists reason that this form of revenge became adaptive for humans as it ensured a decrease in the probability that a transgressor would repeat the undesirable actions in the future ([McCullough, 2008](#); [McCullough et al., 2012](#)). However, there are circumstances (i.e., when the costs of revenge are too high or undesirable) under which an individual may find it best to *forgive* a transgressor ([Aquino et al., 2003](#)).

Defined, forgiveness can be characterized as a decision to "release or forego bitterness and vengeance" ([Exline et al., 2003](#): 339). Forgiveness is a moral value that helps people move beyond feelings of revenge and hatred ([North, 1987](#)), and typically means there is a "willingness to consider engaging in future interactions" ([Bottom et al., 2002](#): 500). Through forgiveness (i.e., restorative justice), mutual cooperation can be reestablished after a lie ([Bottom et al., 2002](#)). Below we describe how the ultimate response to a violation of fairness depends on the investor's overall perception of fairness—either in excess or short of their expectation—for the relationship (e.g., [Gneezy, 2005](#)).

4.2. Conditions that facilitate forgiveness: Relationship value and exploitation risk

The forgiveness instinct is most likely to be activated when two psychological conditions are met: (a) high expected relationship value, and (b) low expected exploitation risk ([Burnette et al., 2012](#); [McCullough, 2008](#)). We argue that these two conditions are effective because they address the types of injustices stakeholders can perceive as a result of an entrepreneur's lie. As such, they provide granularity for a new stakeholder theory explanation of how investors respond to an entrepreneur's lie.

Our choice of theoretical lenses—evolutionary psychology and stakeholder theory—is uniquely appropriate for the entrepreneur–investor relationship phenomenon because it combines individual cognitive processes and venture-level considerations. This setting differs from the generalized psychological setting in several ways. For example, a significant portion of relationship value is arguably conceived of as financial value; the investor is constrained in her potential responses to the extent her investment capital is non-recoverable; and the investor's prior experiences with other entrepreneurs is likely to influence the appraisal of exploitation risk. The theory developed here is not applicable to other phenomena in which established firms, for example, intentionally mislead a stakeholder because the institutional or bureaucratic mechanisms at play in that setting differ from the dynamics of interpersonal relationships.

4.2.1. The relation between relationship value and forgiveness

The first psychological condition that makes forgiveness more likely than revenge is high expected relationship value ([Burnette et al., 2012](#)). The investor who, even after learning of an entrepreneur's lie, remains committed to her relationship with the entrepreneur, is still satisfied with the entrepreneur's overall behavior, and/or forecasts acceptable financial performance from her investment will make a positive appraisal of relationship value. This, overall, is an appraisal of the extent to which the relationship with the entrepreneur might still contribute to the investor's goal achievement.

As the relationship value assessment becomes more favorable, the investor believes she will be allocated more fairness (net of distributional, procedural, and interactional) if they continue engaging with the entrepreneur. After considering the costs they incurred as a result of the transgression, anticipating future rewards from the relationship helps them forgive. Thus, the higher the expected relationship value after discovering the transgression, all else equal, the more likely it is that the investor will choose to forgive the lie. For some investors, the opportunity might represent a prospect of great upside value creation through the successful exploitation of a market opportunity. In sum, we propose the following.

Proposition 1. *An investor who perceives greater expected relationship value in a relationship with an entrepreneur, all else equal, will be more likely to forgive that entrepreneur for a lie.*

4.2.2. The relation between exploitation risk and forgiveness

Low perceived exploitation risk is the second psychological condition that affects the likelihood a victim will forgive a transgressor (Burnette et al., 2012). The probability of forgiveness decreases when the investor perceives the entrepreneur is willing or able to harm them again in the future because such behavior will threaten the investor's goal achievement. The focus of this appraisal is on the risk of additional deceit and exploitation. Expectations of procedural justice include the use of accurate data and transparency in decision-making processes (Leventhal et al., 1980; Sapienza and Korsgaard, 1996). Both of these expectations are violated when the entrepreneur is caught in a lie. The discovered lie suggests that this entrepreneur might place less emphasis on truthfulness, generally, and therefore be prone to lie about other things or to other investors. Actual and potential harm severity, intentionality of the lie, entrepreneur's trust repair efforts, entrepreneur's agreeableness, and the investor's prior negative experiences all contribute to the appraisal of exploitation risk, which in turn affects the investor's decision to forgive. Our broad proposition here is as follows.

Proposition 2. *An investor who perceives greater exploitation risk in a relationship with an entrepreneur, all else equal, will be less likely to forgive that entrepreneur for a lie.*

In the following sections, we examine the conditions under which entrepreneurs who are caught in a lie can still achieve a favorable relationship with, or at least retain access to the resources of, the offended investor. Here, we integrate the literature focused on the correlates of expected relationship value and expected exploitation risk with research on organizational justice in a stakeholder context.

4.3. Relationship value and its correlates

Multiple factors affect a victim's appraisal of relationship value when considering forgiving a perpetrator. Drawing on evolutionary psychology (Burnette et al., 2012), forgiveness (Fehr and Gelfand, 2010), and stakeholder theory (Bosse et al., 2009) perspectives, we discuss three particularly relevant correlates: (a) relationship commitment, (b) relationship satisfaction, and (c) entrepreneur's performance.

In the interpersonal relationships literature, two of the most studied constructs are relationship commitment and satisfaction. Commitment predicts a host of pro-relationship behaviors including longevity (e.g., Fehr et al., 2010; Le and Agnew, 2003). In the specific context of transgressions and betrayals, commitment is linked to appraisals of the situation and the decision to remain involved (Finkel et al., 2002, 2007). This research suggests that greater commitment fosters a longer-term orientation that affects individuals' decision-making when responding to transgressions such as lies. In the context of investor relationships with entrepreneurs, some level of interpersonal involvement or expectation of continuity is common.

Regarding relationship satisfaction, the literature suggests that greater relationship satisfaction affects how victims perceive the responsibility of the transgression (e.g., Finkel et al., 2007): greater relationship satisfaction enables the victim to see "others' offenses as [...] understandable or unintentional" (Fehr et al., 2010: 901). From the stakeholder theory perspective, the investor's perceptions of relationship commitment and satisfaction may affect evaluations of procedural and interactional justice. Accordingly, we propose the following.

Proposition 3a. *Investors who are more committed to a relationship with an entrepreneur will appraise the expected value of that relationship more highly than those who are less committed.*

Proposition 3b. *Investors who are more satisfied with a relationship with an entrepreneur will appraise the expected value of that relationship more highly than those who are less satisfied.*

Our third correlate of relationship value is the entrepreneur's performance. From the investors' perspective, the entrepreneur's performance is the financial value of the venture as indicated by some combination of revenue growth, cash flow, and profitability. We suggest that actual as well as potential performance may affect the investor's appraisal of relationship value. Although, investors may find it particularly difficult to assess the potential performance of an entrepreneurial venture if the opportunity being pursued is characterized by uncertainty. An opportunity is uncertain, for example, if it is based on an innovation that is so unlike existing concepts that the set of possible future states is unknowable. However difficult it is, though, the investor will still attempt to assess the entrepreneur's performance and may rely on personal biases and heuristics to make up for a lack of objective performance data.

If the entrepreneur's business is performing as expected, or better than expected, an investor will reason that the relationship may hold greater value for them (McCullough, 2008). And, for example, if the investor has already received some return on her investment, this could serve to allay concerns about expected future value. Using the lens of stakeholder theory, this line of thinking is consistent with the investor expecting more distributive justice from the relationship in the future (Lazare, 2004). Accordingly, we propose the following.

Proposition 3c. *Investors who view an entrepreneur's performance more positively will appraise the expected value of that relationship more highly than those who view performance less positively.*

4.4. Exploitation risk and its correlates

The second psychological condition that makes forgiveness more likely than revenge is low exploitation risk (Burnette et al., 2012; McCullough, 2008). From the evolutionary psychology perspective, multiple factors affect a victim's appraisal of exploitation risk when considering forgiving a perpetrator (Burnette et al., 2012; Fehr et al., 2010). We discuss six particularly relevant correlates: (a) actual harm severity, (b) potential harm severity, (c) intentionality of lie, (d) entrepreneur's trust repair efforts, (e) entrepreneur's agreeableness, and (f) investor's prior negative experiences.

First and second, we examine the relations of actual and potential harm severity with exploitation risk. An important part of victims' evaluation process is assessing whether the perpetrator inflicted harm (Gordon et al., 2004). Perceptions of harm are often included in assessments of fairness. Lewicki (1983) explains that people separate their considerations of the impact a lie should have on their relationship with the other party and the material impacts of the lie. And, Sarasvathy (2001) argues that entrepreneurs and their stakeholders often incorporate the potential downside of their actions and limit their risk to affordable losses. Therefore, a lie might be forgiven by investors who recognize that the lie did not result in a material cost or opportunity cost. Thus, incurring an affordable loss as a result of the entrepreneur's lie might not be perceived as severe as a larger loss.

Overall, from this perspective, the pecuniary implications of a lie depend on the investor's view about the acceptability of the lie—and, this assessment of the actual as well as potential harm caused is related to her justice perceptions. For example, if the investor believes the entrepreneur did not inflict actual harm, the investor might conclude that the two parties' fairness norms are acceptably aligned. However, even if the investor perceives no actual harm, she may still perceive potential harm. This distinction focuses on objective and subjective transgression severity (Fincham et al., 2005)—and both factors play a role in victims' perceptions. Severity of harm, both actual and potential, may affect investor's evaluations of distributive fairness—the material rewards they invested and have at risk (with the possibility of returns on investment). In sum, we suggest that greater actual as well as perceived harm severity will be positively related to perceived exploitation risk.

Proposition 4a. *Investors who perceive greater actual harm severity of the lie will perceive higher exploitation risk in the relationship.*

Proposition 4b. *Investors who perceive greater potential harm severity of the lie will perceive higher exploitation risk in the relationship.*

Third, we examine the relation between the intentionality of a lie and exploitation risk. Multiple factors may weigh on an investor's evaluation of intentionality such as perceived choice and the nature of the lie. Regarding perceived choice, an investor may consider how much volition an entrepreneur had over the decision to lie. For instance, it is clear that new firms suffer from lack of legitimacy due to liabilities of newness and smallness (e.g., Singh et al., 1986). Thus, an investor may reason, if the entrepreneur had already been deemed legitimate by investors, she would not need to lie in order to attract additional investors. And, the very liabilities that plague the entrepreneurial venture might also represent a condition that provides a certain advantage in recovering a relationship. Investors might empathize with a lie because they acknowledge the challenges faced by entrepreneurs and attribute the lie to a desire to see the business succeed rather than to violate the investor's confidence.

From an empirical standpoint, a large body of research shows that economic actors care about others (e.g., Fehr and Gächter, 2000). Care and compassion can emerge for multiple reasons. For instance, studies about the conditions that support relationship recovery show actors with less power are consistently given more compassion and empathy (e.g., Koning et al., 2010). In a series of controlled bargaining experiments in which parties have differing amounts of bargaining power, parties with less power are forgiven their lies more readily than parties with more power (Koning et al., 2010). Relating this experimental finding to the lie phenomenon, perhaps it is the very nature of this setting that makes the deception excusable (i.e., the low power status of entrepreneurs seeking resources). An investor may infer that, in order to procure funds for the business, the entrepreneur had to (or was incented to) lie. This attribution would affect the investor's perceptions of intentionality.

This line of thinking is consistent with psychological research on the underdog effect. The underdog effect represents people's tendency to “support or root for an entity that is perceived as attempting to accomplish a difficult task, and that is not expected to succeed against an explicit or implicit advantaged opponent” (Kim et al., 2008: 2251). An individual's desire to root for and support an underdog has multiple psychological explanations (for a review see Kim et al., 2008). For instance, supporting an underdog enables individuals to promote uniqueness (Lynn and Snyder, 2002) as well as advocate for fairness and equity (Folger and Kass, 2000). In the case of entrepreneurs, data illustrate that about one-third of all new businesses close in the first two years and over half of new businesses close within four years (Headd, 2003; Knaup, 2005). As underdogs, entrepreneurs are indeed attempting to accomplish a difficult task while expectations for success are low. And, the perception of an entrepreneur as an underdog provides a plausible explanation for why lies might not always be punished as stakeholder theory predicts.

Regarding the nature of the lie, as it relates to intentionality, many issues could be considered. For example, an investor may consider whether the lie was related to an exaggeration or an effort to be deceptive. Entrepreneurs, especially those seeking funds, are prone to exaggeration (Kawasaki, 2008). An investor may consider whether it was a lie of omission (i.e., something left out) versus commission (i.e., something included that was untrue). Generally, “sins of commission” are seen as more serious than

“sins of omission” (Olekalns and Smith, 2009: 355) so an investor who was told something blatantly untrue may perceive heightened exploitation risk.

Overall, within the context of the entrepreneur–investor dyad, we suggest evaluations of intent provide cues about the degree of alignment in procedural fairness norms. Believing that the entrepreneur will act with procedural fairness in the future makes it more likely that the investor will see less exploitation risk. An investor is less likely to forgive when she believes the entrepreneur was acting maliciously. For investors who discover they have been told a lie, questions they may ask include: Why did this entrepreneur lie? What was this entrepreneur trying to achieve with this lie? How could this entrepreneur have accessed the resources she needs to exploit this opportunity if she had not lied to me?

These questions may enable the investor to take the perspective of the entrepreneur and make more accurate attributions, which could foster a decrease in perceived intentionality (Takaku, 2001). As a part of perspective-taking, investors also likely consider how the lie was discovered. Perceptions of benevolent intent, for example, could be influenced if the entrepreneur voluntarily disclosed the lie. In contrast, if the investor discovered the lie without the entrepreneur disclosing it, that may affect perceptions of malicious intent. Thus, efforts by the entrepreneur to explain her actions may affect the investor's evaluations of exploitation risk. Thus, we propose the following.

Proposition 4c. *Investors who perceive greater intentionality of the lie will perceive higher exploitation risk in the relationship.*

Fourth, we examine the relation between the entrepreneur's trust repair efforts and exploitation risk. The discovery of an entrepreneur's lie may affect the investor's perception of the entrepreneur's trustworthiness (e.g., Mayer et al., 1995). Perceived trust affects myriad outcomes at the individual and organizational levels (e.g., Colquitt and Rodell, 2011; Colquitt et al., 2007), and trust has been noted as a key to establishing cooperative relations between entrepreneur and investors (Maxwell and Lévesque, 2011; Shepherd and Zacharakis, 2001; Welter, 2012) as well as increased accessibility of finance and decreased risk management actions (e.g., collateral, guarantees; Howorth and Moro, 2006). Put simply, if the investor perceives that the entrepreneur adheres to a lower standard of truth-telling (i.e., decreased trustworthiness), she will expect additional procedural injustices in the future.

The trust repair literature provides insights into how an investor may evaluate exploitation risk (e.g., Gillespie and Dietz, 2009). From a trust repair perspective, we know that individuals evaluate the degree to which (a) a transgression occurred, (b) whether the transgression is attributable to the person or situation, and (c) whether the issue is fixable or fixed (Kim et al., 2009). For example, trust repair is more likely when there is an alignment of the victim's attributions (internal vs. external) and the type of violation (competence vs. integrity) (Kim et al., 2006; Tomlinson and Mayer, 2009). Attempts by an entrepreneur to repair trust with an investor will be most effective if aligned with the investor's perception of the transgression (e.g., Gillespie and Dietz, 2009; Kim et al., 2006, 2009; Poppo and Schepker, 2010).

Along these lines, an entrepreneur's apology may have an impact on (i.e., clarify) an investor's perceptions. Apologies may contain messages focused, for instance, on compensation and/or empathy in the wake of a transgression (Fehr and Gelfand, 2010). Apologies, therefore, provide a mechanism through which entrepreneurs can signal trustworthiness and facilitate forgiveness on the part of their stakeholders. Overall, the degree to which the entrepreneur engages in trust repair may play a role in the investor's evaluation of exploitation risk. Accordingly, we propose the following.

Proposition 4d. *Investors who perceive greater trust repair efforts on the part of the entrepreneur will perceive lower exploitation risk in the relationship.*

Fifth, we discuss the relation between entrepreneur's agreeableness and exploitation risk. Agreeableness is one of the ‘big five’ personality factors and captures the extent to which an individual is likely to cooperate versus disengage when faced with conflict. Fehr et al. (2010) report that agreeableness is the dispositional attribute that is most commonly linked to forgiveness. The amount of cooperation, care and empathy people show one another is a form of interactional fairness. Individuals tend to give respect and dignity to people who they like and find agreeable. Findings show that an offender's likableness affects forgiveness in the workplace (Bradfield and Aquino, 1999). And, victims of a transgression who viewed their transgressor as more agreeable had less stress measured by decreased cortisol response and greater self-reported forgiveness (McCullough and Tabak, 2011). Mapping this onto our context, when an investor determines that an entrepreneur is more agreeable they deem the entrepreneur as worthy of more interactional fairness. Thus, if an investor likes and finds an entrepreneur agreeable, this may compel the investor to favorably appraise the entrepreneur's exploitation risk.

Proposition 4e. *Investors who perceive greater agreeableness with the entrepreneur will perceive lower exploitation risk in the relationship.*

Sixth, we examine the relation between investor's prior negative investment experiences and exploitation risk. Recollections of prior transgressions, by the current perpetrator or another from the past, are negatively related to a victim's efforts at reconciliation (Rusbult et al., 2005). In short, if the investor has been hurt before by an entrepreneur's lie or has experienced a similar transgression, those feelings of betrayal will likely become salient and affect perceptions of exploitation risk. Victims who acknowledge past transgressions are less likely to engage with the perpetrator or expose themselves to exploitation risk in the future as the possibility of being hurt again becomes increasingly salient (Rusbult et al., 2005). Thus, we propose the following.

Proposition 4f. *Investors who have had prior negative experiences will perceive greater exploitation risk in the relationship.*

5. Discussion

The present conceptual contribution, developed above, examines the question: Under what conditions will investors who could withdraw from the relationship, instead, choose to respond with forgiveness after suffering an entrepreneur's lie? Overall, although stakeholder theory and entrepreneurial ethics explain why entrepreneurs benefit by being open and honest with their investors (Van de Ven et al., 2007), some entrepreneurs do the opposite when they lie to an investor (e.g., Brenkert, 2009; Rutherford et al., 2009). Interestingly, entrepreneurs who choose to lie may *still* build effective investor relationships (Rutherford et al., 2009), despite the violation of social norms (Steverson et al., 2013) and despite what stakeholder theory predicts (Freeman et al., 2010). Thus, we suggest that the entrepreneur–investor dyad is a context where the core propositions of stakeholder theory deserve closer scrutiny.

We put forward a theory-based model (Fig. 1) that outlines the conditions likely to affect an investor's decision to forgive an entrepreneur. The main conditions under which an investor is more likely to forgive an entrepreneur for lying are: (a) when the investor expects greater value from the relationship in the future (i.e., high expected relationship value), and (b) when the investor believes the entrepreneur is unwilling or unable to harm them again in the future (i.e., low expected exploitation risk). And, each of these conditions is further affected by correlates that either strengthen or weaken the investor's appraisal of the situation.

From a theoretical perspective, we extend the logic of stakeholder theory by linking the psychological conditions that facilitate forgiveness to specific types of justice that may motivate investor's behavior in the entrepreneur–stakeholder context. From a practical perspective, this work outlines why entrepreneurs may lie as well as the processes through which forgiveness from investors for such a transgression may be achieved. We note how, even after an investor learns of a lie, entrepreneurs can act to recover without suffering the expected negative effects. This research takes an important step towards a more complete understanding of the applicability of stakeholder theory in entrepreneurship as it relates to perceptions of justice and forgiveness.

5.1. Scholarly contribution

Contemporary research on the adaptations that comprise forgiveness systems has boiled down to a model in which appraisals of relationship value and exploitation risk are the key antecedents to the decision to continue cooperating after suffering a lie (Burnette et al., 2012). We apply this framework and leverage insights harvested from evolutionary psychology and forgiveness research to expand the explanatory power of stakeholder theory. Stakeholder theory draws focus on the specific relationship behaviors through which a venture creates value. And while the theory offers concise guidance regarding which stakeholder relationships are most salient in value creation, it currently falls short in its explanation of “stakeholder engagement strategies” in various specific settings (Freeman et al., 2010: 287). As explained above, stakeholder theory, on its face, is unprepared to accommodate the phenomenon in which an investor forgives an entrepreneur for lying.

These theoretical lenses—evolutionary psychology and stakeholder theory—are uniquely appropriate for the entrepreneur–investor relationship phenomenon because they combine individual cognitive processes and venture-level considerations. Throughout, we have integrated the psychology-based correlates and antecedents of forgiveness with the concept of moral norms of justice in stakeholder theory to develop a multi-stage model of investor's decisions to forgive an entrepreneur who has lied. This reasoning enables us to extend the logic of stakeholder theory and specify how, even after an investor learns of a lie, entrepreneurs can recover without suffering the expected effects of negative reciprocity. This work bolsters existing research advocating that a justice perspective can shed light on the intricacies of the entrepreneur–investor relationship (e.g., Sapienza and Korsgaard, 1996). In particular, our logic specifically uses a micro perspective from psychology to form stakeholder theory to the phenomenon of entrepreneurs who lie to their investors. This development provides researchers and practitioners a starting point from which considerations about future research and behavior, such as those offered in the next sections, can be explored.

5.2. Conceptually-focused suggestions for future research

Bridging the divide between the forgiveness literature, entrepreneurship literature, and stakeholder theory uncovers multiple areas for inquiry. Future research on entrepreneurial decision-making can further deepen our understanding of the unique conditions and strategies leveraged by entrepreneurs to overcome their relational challenges with investors. For instance, future studies designed to test the theory of effectuation can assess the differences in distributional justice expectations between arm's-length transaction parties and investors who are opportunity co-creation partners (Sarasvathy, 2001). In this context, research can also further examine the effect of assessments of intent on procedural fairness perceptions.

Future work is encouraged to explore the impacts of lies on other key stakeholders besides investors, such as customers, suppliers, and service-providers (e.g., accountants, lawyers, bankers, insurance professionals). Studies could merge the present work with the literature on interpersonal relationships to examine when, and how, apologies work in other specific entrepreneur–stakeholder settings. Apologies that contain messages focused on compensation and/or empathy in the wake of transgressions may provide a mechanism through which entrepreneurs can effectively facilitate forgiveness (e.g., demonstrating low exploitation risk, and high relationship value).

Along these lines, we recommend that future work examine different types of investment relationships. For example, a potentially relevant line of work could explore how different types of investors process the forgiveness decision. Although we suggest that all

investors would ultimately weigh relationship value and exploitation risk in their decisions, a family member versus a banker versus an angel investor versus a venture capitalist may emphasize one area over another. As one possibility, a family member may evaluate relationship value in different (e.g., non-financial and values-based) terms relative to a banker who may look at relationship value solely through a financial lens.

5.3. Empirically-focused suggestions for future research

The model developed in this paper might best be tested using structural equation modeling techniques following a careful primary data collection strategy involving the correlates and constructs of relationship value and exploitation risk and the outcome of forgiveness. An additional option is to explore the relative importance of each correlate in this process and their impacts on appraisals of relationship value and exploitation risk with a conjoint study. The data for such a study could be collected by presenting investors with various hypothetical decision scenarios containing various levels of each correlate and asking them to provide their appraisals as well as their willingness, on a Likert scale, to forgive the entrepreneur.

The above research avenues (both conceptual and empirical) are predicated on the accurate measurement of forgiveness. A vast literature in the interpersonal relationships domain has pioneered measurement techniques for forgiveness. Future research is encouraged to draw on this body of work (for reviews see [Worthington, 2006](#); and also [Hannon et al., 2010](#); [Molden and Finkel, 2010](#)). In particular, we suggest that future work follows the example of study two in [Molden and Finkel \(2010\)](#) which is a six month longitudinal investigation into how romantic partners forgive (or did not forgive) one another in terms of “initial” forgiveness as well as “delayed” forgiveness. In addition to these measures, one other option includes [Bradfield and Aquino \(1999\)](#) who developed a measure of revenge versus forgiveness in the workplace. For the specific measurement of relationship value and exploitation risk, we suggest the RVEX measure developed by [Burnette et al. \(2012\)](#). In short, the application of these methods and measures to the present context would make extensions of our work particularly effective and efficient.

One further opportunity is as follows. Our two focal constructs—relationship value and exploitation risk—affecting a victim's appraisal of the situation, may not act independently on the decision to forgive. The extant literature suggests that individually, as well as through their interaction, relationship value and exploitation risk predict forgiveness ([Burnette et al., 2012](#)). In particular, the optimal condition for forgiveness is one in which the victim perceives high relationship value and low exploitation risk ([Burnette et al., 2012](#))—and, data indicate that relationship value is a stronger predictor of forgiveness than exploitation risk. Applying this insight to our context of deciding when to forgive an entrepreneur's lie, we argue the effect of an investor's appraisal of high relationship value will be strengthened in situations where she also appraises a comparatively low exploitation risk. Thus, we encourage future work to explore the moderating role of exploitation risk on the relation between expected value and forgiveness.

5.4. Investor evaluations of lies

From a practitioner point of view (i.e., investors and entrepreneurs) the present work holds enormous value. The model developed above takes the perspective of an investor seeking to decide whether to forgive an entrepreneur for lying to her. In the development of the model, we already provided insights into how entrepreneurs can potentially repair relationship trust after getting caught lying. Moving on, here, we offer the following thoughts for investors about how to evaluate a relationship in the wake of a lie.

When an investor discovers a lie, she has the opportunity to evaluate characteristics of the offender (entrepreneur), the transgression itself, and clues to the future prospects for the relationship ([McCullough, 2008](#); [McCullough et al., 2010](#)). For instance, an investor may ask questions about the entrepreneur that help assess whether their moral norms of fairness are aligned despite the lie, the degree to which the entrepreneur is sincere, the degree to which the entrepreneur's intent was malicious, and whether the entrepreneur's alternatives to uttering this lie were prohibitively limited.

Looking at the transgression itself, investors can consider how much it has or will cost in material (distributional fairness) terms. They can also assess the non-material costs they have incurred in procedural and interactional fairness terms. For example, an investor may ask questions such as: If I were in this entrepreneur's position, how likely would I be to make a similar lie (procedural fairness)? To what degree did this transgression make me feel foolish (interactional fairness)?

The investor can take actions that directly adjust her own expected value in the relationship. If the investor believes she is putting greater effort into the relationship than her material value warrants, she can choose to negatively reciprocate by putting forth less effort or resources for the same output (e.g., [Fehr and Gächter, 2000](#)). One important caveat bears mention. In some cases, an investor may not be able to withdraw financial support (e.g., the money is already invested/spent). If, despite a rigorous due diligence process, an investor fails to discover a lie and decides to invest, it may be too late to recover all the financial assets after the lie becomes known. As this situation may substantially constrain an investor's options and decision-making discretion, we suggest this as a direction that future research can explore.

Overall, though, the investor's weighting of the three types of fairness will depend largely on the relationship she has with the entrepreneur. If the entrepreneur has discovered the opportunity and has engaged the investor in an arm's-length transaction (i.e., low relationship commitment) in order to exploit it, the investor is likely to place greatest emphasis on the distributive fairness she receives. The decision whether to abandon the entrepreneur hinges primarily on monetary value in this type of relationship. Procedural and interactional justice, while still important, will have comparatively less emphasis in motivating the investor's reciprocal response.

Alternatively, if the entrepreneur and investor are co-creating an opportunity through an effectual partnership (Sarasvathy, 2001), the investor will place greater emphasis on procedural and interactional justice and less emphasis on distributive justice. A cooperative scheme such as this creates an obligation (Mill, 1859) regarding how the parties will treat each other as the scheme unfolds. The investor's assessment of exploitation risk is comparatively more important in an effectual partnership. In particular, the degree to which the entrepreneur engages in trust repair may play a larger role in the investor's evaluation here. Especially in cooperative endeavors, trust between the entrepreneur and investor facilitates effective relationships (Howorth and Moro, 2006; Shepherd and Zacharakis, 2001).

Some of the following cues might help predict the probability of future transgressions from this entrepreneur: How sincere is the entrepreneur in her remorse? Since the lie, has something changed that will reduce the entrepreneur's motivation to lie again? What are the future opportunities for a mutually beneficial relationship with this entrepreneur?

In sum, these considerations affect the ultimate decision of an investor regarding how to respond. However, an important point needs to be emphasized. Above we noted that one potentially relevant line of research could explore how different types of investors process the forgiveness decision. This represents an important boundary condition of the present work. We focus, primarily, on envisioning the forgiveness process in more formal entrepreneur–investor relationships (e.g., angel investors, venture capitalists). However, these formal relationships, by number, represent a minority of the investments entrepreneurs acquire. It is much more likely that an entrepreneur will receive money from friends, family, crowdfunding, or a similar, more informal avenue, than from angel investors or venture capitalists. Accordingly, it is essential for future work, conceptual and empirical, to examine how (and if) the model we presented in the present work holds (or not) with regard to various investors.

6. Conclusion

This paper refines stakeholder theory for the specific situation in which an entrepreneur gets caught lying to an investor. Whereas stakeholder theory would normally predict negatively reciprocal behavior from the investor because lying is a violation of moral expectations, we explain how the appraisals of relationship value and exploitation risk influence decisions to forgive. One surprising conclusion of this work is that an entrepreneur's lie to an investor may initiate a multi-stage decision process that ultimately leads to forgiveness not retribution.

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