

# How a Distillery Founder and His Investor Went Off the Rails

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In 2013, Chip Tate was on the verge of taking Balcones Distilling to the next level. Since 2008, he had been building his Waco, Texas-based craft whiskey business literally with his own hands, designing and welding equipment himself and researching the best distilling techniques in Scotland. After gaining a cult following and winning several international competitions, Tate was anointed by whiskey industry writers as “the Steve Jobs of Craft Whiskey.”

But the acclaim hid a big problem: Balcones was running out of money. It couldn't keep up with demand. It needed an investor to expand capacity, and quickly. Tate found one, but their relationship would soon fall apart. The unraveling, detailed in extensive litigation, in-depth interviews with the founder and the investor, and diverse media reports, provides numerous lessons for founders and investors looking for happier endings.

Tate sought a partnership with an angel investment group that shared his passion for the business and could help Balcones scale up profitably to meet demand. He agreed to an equity investment from Oklahoma-based Greg Allen of PE Investors II. The agreement gave each of them equal decision-making power. Allen became board chair and assumed responsibility for financial issues and business oversight. Tate remained CEO and head distiller, and he was charged with running the business, process and product innovation, and expansion.

It took only 18 months for the partnership that Chip Tate hoped would be a marriage made in heaven to explode. Tate exited the business that he had worked so hard to build, after a bitter rivalry with Allen that included a court case, reputational damage, and even alleged death

threats. The surprising root cause of all this trouble: their shared decision-making power, which set the stage for destructive turf wars.

Balcones remains in business today. But our extensive research into the Balcones case provides a cautionary tale and actionable advice for every founder and investor who join forces to try to turn a promising business concept into a winner. It vividly illustrates that the party investing most of the cash doesn't always hold most of the cards, but that much can be done on both sides to forestall a bitter dispute over a startup's direction.

## A Perennial Battle

Battles between visionary entrepreneurs and their investors are common and can be epic, as the stories of Steve Jobs (Apple), Travis Kalanick (Uber), and Adam Neumann (WeWork) show.

To scale their ventures, founders give up decision-making control to access investor cash, advice, connections, and other resources. Indeed, investors receive dominant equity interests, board chairs, board membership majorities, and decision-making authority. Research tells us that, despite collaborative and constructive starts to these relationships, conflicts arise from arguments over goals, responsibilities, and performance issues, culminating in investor calls for founders to step down from leadership roles and even to leave their organizations.

The impact on founders can be profound, causing psychological and emotional distress at the prospect of being disconnected from their creations. Most founders fight back: They struggle to regain control from investors



and forestall further erosion of their influence. According to Noam Wasserman's article in *Harvard Business Review* (2008), his research found that four of every five founders (80%) resisted investor pressure to give up their CEO positions (<https://hbr.org/2008/02/the-founders-dilemma>). However, as the founder of Balcones Distillers discovered, such battles can come at a big cost: Fights in the court system, distractions for employees, and other impediments threaten to reduce business success.

The academic literature and conventional wisdom assume that investor control leaves founders powerless to resist their will, suggesting that founder resistance amounts to "tilting at windmills." Yet, according to [Wasserman's piece in the Wall Street Journal](https://www.wsj.com/articles/how-an-entrepreneur-s-passion-can-destroy-a-startup-1408912044) (<https://www.wsj.com/articles/how-an-entrepreneur-s-passion-can-destroy-a-startup-1408912044>) (2014), about one of every two founders (48%)—among more than 16,000 founders studied in his academic career—had *not* stepped down as their organization's chief executive by the third round of outside funding—a later-stage milestone in venture development. By the time of IPO, a milestone that most startups do not reach, Wasserman (2008) reports that one of four founders (25%) had not stepped down.

The disconnect between beliefs and statistics raised various questions for us. We wondered, how do relationships that begin collaboratively and consensually transform into bitter struggles over venture control? Are these struggles simply about founder resistance to giving up leadership positions, or are the motives more complicated? And, if investors hold and exercise complete control, how do founders hold their ground during these struggles? The fact that 25-50% of founders do not succumb to the fate assumed to await them, being ousted by more powerful investors, highlighted the need for further investigation and understanding.

We conducted an exploratory qualitative study to learn more about consequential instances of founder-investor rivalry, those where either founder or investor could emerge victorious.

Our in-depth, longitudinal study, which is published in *Journal of Business Venturing*, explored how such rivalry can arise, unfold, and conclude. [Balcones was an ideal case to study](https://familybusiness.org/content/for-new-research-ideal-case-to-study). ([https://familybusiness.org/content/for-new-research-](https://familybusiness.org/content/for-new-research-ideal-case-to-study)

insights-study-one-family-in-depth) Tate and Allen, who's angel investment group received the controlling equity interest, initially worked together collaboratively before their relationship descended into rivalry over control of the distillery. Moreover, despite not being a majority owner, Tate successfully retained his position as Balcones' CEO until deciding to leave of his own volition. To understand what happened at Balcones, we analyzed nine in-depth interviews with Tate, Allen, and others; more than 1,000 pages of legal documents and their attendant private emails, social media posts, board meeting minutes and other exhibits; and dozens of news articles about the battle for Balcones.

We saw their doomed-from-the-start partnership progressed from harmony to discord in three overlapping phases (credit to the rock band Green Day): "Welcome to Paradise," "Boulevard of Broken Dreams" and "Good Riddance." Moreover, within each phase, we identified triggers that undermined the partnership and led to its acrimonious conclusion.

## Phase 1: Welcome to Paradise

When the partnership launched in 2013, Tate and Allen started out with good-faith intentions and a shared vision. Both sides were excited for the company's next stage and genuinely respected each other.

The collaborative start shaped the investment deal, including how they would share the post-deal work of running the company. But in very little time, key stressors disturbed the carefully crafted equilibrium between the two men and sparked a rivalry that quickly degenerated into private warfare.

The initial stressor came with a disagreement over the cost to expand Balcones. Tate, who had been given free rein by Allen to plan for an expansion of the distillery, chose a historic building that needed an expensive cooling system for distilling operations to run year-round. Tate favored running the plant only during the cool season in Texas, which would eliminate the need for the cooling system and keep the expansion budget in check. But the board, dominated by Allen's appointees, overruled him to focus on maximizing return on investment.

However, when the costs of the cooling system grew larger than what Tate had estimated, Allen blamed Tate and questioned his management skills.

## Phase 2: Boulevard of Broken Dreams

The disagreement over the cooling system is what we call a “homeostasis-disrupting event” – something that provides the first dent in the harmonious relationship between entrepreneur and investor and ushers in this second, more disillusioned phase.

In this chapter of the partnership’s decline, both sides focused more on their personal interests and less on their shared vision for the company. This focus shift contributed to profound misunderstandings. Efforts intended to salvage their relationship were increasingly seen and dealt with as personal threats, damaging their bond through attempts to preserve it.

One hallmark of this phase is called “compliance tension.” It means one party starts feeling the other is not meeting the original expectation. Allen began to doubt Tate’s competence as a CEO and as leader of the expansion project. Engineers and contractors allegedly complained about Tate’s project management acumen. As Allen and the board intervened to keep the expansion project on track, Tate felt Allen was threatening his turf.

Both sides at this point engaged in “role jockeying” – i.e., actions to exert influence over each other’s agreed-upon roles. Allen watched over Tate’s expansion activities more closely and hired other executives to help guide the project. He was less than glowing in Tate’s performance review and proposed that Tate step down as CEO to focus on distilling and brand building. Allen also proposed an internal financing round to raise more money, which Tate saw as an attempt to weaken him.

Tate, in turn, pushed back by refusing to step down and arguing for alternatives to the financing plan. He then skipped board meetings, depriving the board of his vote so that financing plan could not move forward. He accused Allen of taking over the firm’s social media accounts to discredit him.

And in a sign of how nasty things had gotten, Allen accused Tate of making death threats against him and other members of Balcones’ leadership team. Tate denied the allegations, and after a summary judgment in his favor, both sides dropped their legal claims against one another.

## Phase 3: Good Riddance

In this phase, what had been a private battle between entrepreneur and investor began to spread to other stakeholders, as both sides jockeyed for their hearts and minds. The trigger was when the board suspended Tate and had police officers escort him off the property.

At this point, the rivalry spilled into the public domain. The mudslinging began. Tate was accused of coming to the Balcones facility without prior notice, failing to forward emails from third parties to the company, initiating contact with competing distilleries, and using Balcones’ credit card. These transgressions constituted a **threshold-exceeding event**—in this case, actions that exceeded the boundaries (or limits) of the board’s desire and capacity to continue the working relationship.

Allen and the board sought an injunction against Tate in district court to gain sole control over Balcones’ affairs. Both sides crafted petitions accusing the other side of undermining the company, covertly pointing the media to the petitions. Doing so courted support from other stakeholders, including employees and customers. Allen won the hearts and minds of employees while Tate won support from customers, who even created a GoFundMe campaign for him and other industry experts.

Eventually the court sided with Tate, allowing him to return to his business. But by that time, both Tate and Allen were weary of their battle and the partnership. Following mediation, despite securing court support for his agreed-upon roles at Balcones, Tate voluntarily left the business he had worked so hard to build.

## Lessons for Founders and Investors

Drawing from our findings, we believe entrepreneurs and investors have much to learn to avoid such rivalries at their companies. Five are foremost:

### Think Twice About Sharing Control

It sounds great in theory, but relationships where entrepreneurs and investors share control of venture affairs may not create the lasting paradise they intend. For instance, Tate’s and Allen’s decision to divide control evenly into complementary roles, although seemingly noble, may have created favorable conditions for rivalry to erupt, spread and conclude as it did.

## Don't Assume Cash is King

Bringing money to the table and receiving a dominant ownership interest did not give PE Investors complete influence over Tate or mitigate his influence over them. Other resources, such as technical know-how and professional reputation, positioned Tate to retain extensive influence over his venture's affairs after the investment was made.

## Be Clear on Expectations

Founders and investors must *precisely* communicate how they perceive their own and their counterpart's roles, the scope of their decision-making authority, and what they will add to the venture—before finalizing agreements. The Tate-Allen partnership might have unfolded very differently if both sides had concentrated on their shared vision, subverted their self-interest to collective goals, and resisted the primal urge to fixate on their differences. Showing empathy for your counterpart's perspectives and expectations, and communicating openly and honestly as relationships evolve, may prevent battles over venture control from arising or escalating.

## Legal Agreements Are Not Enough

Tate and Allen formalized their desired roles and rights in an operating agreement. The process of revising the operating agreement was amicable and thoughtful. But in the end, it was not nearly enough to save their relationship when things went south. While their agreement gave Tate veto power over board decisions, it still didn't prevent the board from suspending him, slapping him with an injunction or even forcibly removing him from the premises—particularly in the shorter term.

Fighting back cost Tate his money, emotional well-being, and reputation with co-workers – and he still left the company. The same reasoning applied to Allen and the board: The operating agreement did not protect them from the consequences of Tate's actions. The takeaway: Preventing founder/investor relationships from descending into rivalry, or mitigating rivalry that occurs, requires much more than a good contract. Thinking through how power is shared in advance, and being clear with one another about role expectations, is also vital.

## Protect Other Stakeholders

As rivalry escalates and concludes, stakeholders such as employees, suppliers, and customers will feel the

impact and eventually take a side. Being mindful of their interests, building and maintaining relationships with them, and protecting them from collateral damage can win their good will at a time when it's needed and help you keep the venture. At Balcones, it was the investor, not the entrepreneur, who won the minds and hearts of venture employees, leading them to support Allen's bid to control Balcones. Had Tate done the same, he very well could have regained control of Balcones and watched Allen depart for greener pastures.

As the Balcones Distilling story illustrates, even the most equitable arrangements for shared power are no guarantee of a harmonious partnership involving founders and their investors. Clearer definitions of duties, with no ambiguities over who has the final say, in the long run will protect both parties, even if one side ultimately has a greater share of the power.

## Explore the Research

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