How to Fund Your Company

By Robert A. Adelson

Having an investor for your start-up company can provide you access to capital, business development and sales assistance, as well as organizational evolution. The expertise a seasoned investor brings can help a company go public quickly.

The ins and outs of finding an investor for your start-up can be challenging. With a good understanding of the differences between Angel investors (Angels) and Venture Capitalists (VCs), as well as the knowledge of what will most benefit your company, you can attain the capital needed to get your business moving.

You might wonder: Why do angels and VCs do it? Why give money away? Angels and VCs are what agents are to budding actors and writers. Investors plan to make a return. They look for businesses that can provide this by seeing who's best in the space, who can leverage an ending, and go public. There are also investors looking for physical returns: people who want to give back to the next generation of entrepreneurs, or stay involved without a full-time commitment, a kind of partial retirement. Angel investors are a diverse group of people, but they are all looking at what return your company will be able to achieve. Venture Capitalists are connected to a firm, and must keep their partners' interests in mind. VCs tend to have a pattern in the companies they have invested. When looking for a VC investor, familiarize yourself with their past investments by perusing the firm's website.

An entrepreneur must understand the roles and purposes of both Angels and venture capitalists.

Angel investors typically provide capital during the seed and start-up rounds of a company. Compared with the rounds a VC invests in, Angels support the majority of early stage deals. The majority of Angel Investors are U.S. millionaires. The investments from Angels can range $25,000 to $3,000,000. The number of angel groups has risen 300% in the last ten years and the groups are made up of previous and serial entrepreneurs. While it is true that Angels look for a return on their money, some are more concerned with non-financial returns. Some investors are looking for a way to be involved without working full-time, have a desire to give back, or want to be daring and challenged intellectually. Angel investors use their own money when investing; therefore, they must feel comfortable with a deal and often seek deals through connections and networking. An entrepreneur's job is to make a warm introduction.

The Angel's role transitions during the investment. First, there is a deal screening. The entrepreneur presents a 30-minute summary of the business plan and what kind of investment the company needs at an angel meeting. Next comes due diligence. This involves documents, references, interviews, and assessments of the entrepreneur. At this point there is no guarantee on investments. Having an experienced team and being able to convince the potential investor that people will buy the product will help secure an investor. After finding an investor, the angel's role changes. He/she will help the company navigate necessary changes, offers information whether the operating models are credible and compelling, and then after helps with recruiting financials.

As the start-up company, your job is to present a great team, a good business model, have a defined market and compelling technology. Instead of creating a product that does the same thing as another product already on the market, find a problem and solve it. Don't look for something to create, look for a problem to solve.

Venture Capitalists tend to become involved during the first through third rounds of financing, though some have begun investing during the seed and start-up rounds. The typical Venture Capitalist investment ranges from 1.5 to 20 million. The money given during a Series A round (the first round of Venture investing) is typically three times that of the investment in a seed round (the first round of investing from Angels).

VCs have raised money from pensions and other sources; they do not have personal risk with their capital. The VC Industry has taken a huge hit in recent years; there are less people involved with the market, making it difficult to raise capital. However, because of the Facebook effect, investors are looking for the next big thing, so some VCs will invest in the early stages of a company. There's also a dumbbell effect in investing, there is more funding available in the early stages and less later on—so companies need to be capital efficient. VC Firms will most likely have information about the companies they have invested in, know who you are asking for money before asking.

In finding the appropriate investor, an entrepreneur must customize the relationship between the investor and the company with the funding requirements and situation. A good investor will help the company in three ways: provide access to capital, encourage business development and sales, and by organizational evolution. The first is self-explanatory. Business development means being able to get people involved in the company who are going to risk their reputations. Will the investor help you network and provide access to his Rolodex of resources? Lastly, organizational evolution involves the changes a company makes during its lifetime—necessary transitional scaling, expansion, and the alignment of the company strategy with investor strategy.

Your board will need to change at some point. The CEO often shifts to the CTO, but many CEOs are wedded to their title. Realistically, as the company gets funding, the title changes, the founder will be miserable in the role that should be filled by CEO: the problem isn't a lack of commitment but a failure to shift to the next phase.

For the entrepreneur looking to receive capital: be prepared! Right now, the market wants internet-based, software companies and the investors in firms are under enormous pressure for a huge return in 3-7 years. Currently, people are not interested in making tangible products; almost all money is in Internet products and services. A good company will be multi-faceted with a well-thought business plan, yet able to pivot and adapt that plan. The Internet has not been exploited yet, now is the time to capitalize upon the open space.

The impressive entrepreneur is adaptable, listens to ideas, can navigate the twists, has a fierce drive to win, an ability to leave, and good judgment in hiring. He/She will be a dynamic person and demonstrate an ability to recruit good hires. Some investors will want to see a team—3 people teams are usually most appealing because of the way the weaknesses and strengths balance.

Look for an exit. Be flexible. Communicate.

About the author:

Robert A. Adelson is a corporate, tax and contracts attorney and partner, with over 30 years of experience at Engel & Schultz, LLP in Boston. Contact info: 617-951-9980 or radelson@engelschultz.com , and www.executiveemploymentattorney.com

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