Approaching the venture capitalist

By Bartlett M. Sheinberg

This article is intended to provide information for those who are considering approaching a venture capital company (VCC) for funding. Three areas will be discussed: (1) preparation for the meeting (2) making the presentation, and (3) considerations for negotiation strategies. This article is written as a guide for those with little or no experience in investment and financial markets. Specific information regarding financial, legal, accounting, and technical information should be obtained from the best experts the engineer/scientist (ES) can afford.

A number of assumptions were made in preparing this article. Despite a lack of investment experience, the ES in search of venture funds should have a well defined project in mind and have or be close to having a working prototype. Without a working prototype, it can be extremely difficult to raise funds, even for the most talented and highly qualified person. The ES also should have performed extensive research to determine the product market size and have a realistic estimate of the production costs and selling price.

Furthermore, it is assumed that all products that could be remotely identified as being competitive have been analyzed in terms of their respective strengths and weaknesses. Finally, the ES must have objectively determined that the product is superior to any on the market and that the potential users of the product agree with this assessment. It would be of great help if companies which could benefit from this product would be willing to place written orders, contingent upon the product delivering as promised.

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Putting the business plan on paper

At this junction, the ES should begin preparation for dealing with venture capital companies (VCCs). One way to organize one's thoughts, directions, and goals is to prepare a comprehensive strategic business plan. There are numerous references that review in detail the content of business plans, how to analyze their contents and how to evaluate risk.[1-4] Basically, the plan should contain a clear, concise, and crisp overview of the project so that anyone who reads the overview will be able to understand the company's product and financial objectives. The plan should contain at least three separate headings—operational, financial, and technical—followed by a discussion of how these three areas are interrelated and how they each can beneficially or adversely affect the other two. This allows the ES to identify problems before they arise and prepare remedies. For an investor reading the plan, this early identification of problems and proposal of solu-

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All critical factors in the company's operations, i.e., cash flow, manpower/materials resources etc., should be fully explained, perhaps as an addendum to the actual plan. The capability to operate even in the worst of possible conditions will generate confidence that the project has a better than average probability to succeed.

It could take from three months to two years to complete such a plan. Although the ES is probably impatient about getting the business going, he should not forget that it is this plan by which most people will judge whether or not they see a profitable and stable venture worthy of their funds. After the plan has been written, edited, and discussed with professionals (i.e., attorneys, CPAs, close personal friends with expertise in the area, advisors from the Small Business Administration) the ES should now have a firm grasp of the business, including its strengths and weaknesses.

Start with a long list of contacts

With the plan complete or near completion, the ES should begin compiling a list of potential investors. This includes asking all friends, relatives, and professional acquaintances (without jeopardizing his current position) for personal contacts and for introductions to investors. A long list of contacts is suggested because the usual probability of success is about one or two percent. A number of excellent books list VCCs by geographic area, funding interests, and current portfolios.[1,2]

There are various philosophies about contacting VCCs. The ES should follow whatever route feels most comfortable. Writing an introductory letter, then following up with a phone call is one approach. On the other hand, for someone who is comfortable talking to strangers, cold calling and writing a letter after the conversation can be just as productive. The important thing to keep in mind is to find the people with authority to fund the project. One can expend an immense amount of time talking with people who can be of little practical help. Persistence is essential—the process of getting through to the right people can take weeks or months.

When the ES does get through to the investor, he must have a clear idea of what is to be accomplished in terms of the style of presentation and the topics for discussion at the first meeting. The initial screening may only involve the ES sending the investor a copy of the business plan. After review, should the investor express an interest, he will arrange a meeting. However, the approach likely to provide the best results is to ask the investor for 15 or 20 minutes of his time for a personal "pitch," leaving a copy of the business plan for further study. This places a face with the plan as well as a high degree of enthusiasm about the project. If the ES cannot be totally involved in the project, then he is not ready to ask for funds.

Presentation: anytime, anywhere

The ES should be willing to meet the investor anywhere at any time. The initial meeting and presentation is just as likely to happen at the airport as in an office. The ES should be prepared to deliver his presentation under circumstances which are not conducive to high and prolonged levels of concentration (i.e., airports, taxicabs, hotel lobbies, etc.) In no more than 15 to 20 minutes, he must sum up the important points and explain what this project can do for the investor (i.e., financial gain, etc.) The presentation must not be dependent upon audio-visual materials but rather depend upon a thorough knowledge of the operations. Moreover, it should be delivered with enthusiasm—this is not the time to be reserved. While delivering the presentation, the ES can provide the investor with a brief outline, but must concentrate on eye contact during the presentation. If the investor is interested, he will ask for a copy of the business plan. At that time, the ES should ask when they can set the next meeting. The reply could range from "Don't call me, I'll call you" to "Call my secretary to set an appointment." Expect the former. Then allow a reasonable time for the in-

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vestor(s) to read the report and follow up with a phone call about 10 working days later. Offer to supply any additional information or to answer any questions. One must be persistent but in a subtle and unobtrusive manner.

The ES should approach the second meeting as one of information gathering and should not make any binding agreements, no matter how tempting, until he has the advice of an attorney and accountant. What is important here is a free dialogue between the parties to establish a productive working relationship. At this meeting, the ES should be prepared to ask the investor a number of questions, including: How much money the investor can contribute, and, if he can not finance the total operation, can he act as a lead investor for others? What is the length of time the investor wants to stay involved in the business? One or two years; five or ten years? If the ES should need additional rounds of financing, would the investor be able to follow through? Can the investor lend any management expertise to the company? Does he prefer to be involved only in financial matters or can the ES tap his expertise and experience in other areas, i.e., marketing, the development of a customer base, etc.? What is the investor's philosophy concerning buyouts, mergers, acquisitions, going public? What role does the investor want or demand on the board of directors?

To compromise or not to compromise . . .

The ES must decide what he can and cannot live with before he asks the questions, then both parties can compromise. The ES must not be hesitant about getting up from the bargaining table and saying that he cannot live with the terms. In that way, both parties walk away on good terms. The alternative can be total disaster, for no deal is infinitely better than a bad deal.

The ES should be prepared to discuss what he can contribute and the terms he feels will be acceptable. It is important that he give careful consideration to his talents and where they can best serve the company. The investor is likely to ask: In what position does the ES see himself? This role could include being the CEO or being the technical director with a board seat and ownership in the company. The key question in the investor's mind will be what kind of experience the ES has in running or operating a business on a day-to-day basis and his talents in business and people management. At some point in the discussion, the ES should bring up the question of compensation packages that could be arranged if there was to be a merger, acquisition, etc., and what his rights and privileges would be.

The art of negotiating is knowing beforehand what can and cannot be compromised. Making a list of these items can be very helpful and stabilizing, especially if the discussion becomes very emotional. The ES must always keep his perspective and be flexible enough to listen to other proposals. One can always think about a deal overnight or over a weekend. When the pressure is on to find money, perspective and timing can often be lost. The ES cannot afford for this to happen.

One must be confident and enthusiastic about the project, understand where the stumbling blocks are likely to be, know where to go for help, and be ready to listen with an open mind. The process is successful only when everyone wins. With some common sense, a lot of stamina, a few lucky breaks, and an immense amount of dedication and hard work, one can be successful both as an entrepreneur and in achieving one's financial goals.

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