



Visionaries

~ The YVCS Newsletter ~

UPCOMING EVENTS

NYC, Boston, Palo Alto, Singapore, HK

NEW YORK

- **Understanding Consumer Media**
 - **Panel Members include:**
Mitch Davis, CEO of Massive Incorporated, Jeremy Levine, Bessemer Venture Partners, Danny Schultz, Draper Fisher Jurvetson, Andrew Zalasin, RRE, Steve Brotman, Silicon Alley Venture Partners
 - **Oct. 6, 2005**
 - One Madison Avenue, 23rd street and Park Avenue, Auditorium
 - 6PM -8PM
 - \$20
 - Register at www.yvcs.org (events)

- **Transitioning to Private Equity, Hedge Funds or Real Estate**
 - **Panel members include:** The Blackstone Group, General Atlantic Partners, Morgan Stanley, Pzena Investment Management, SAC Capital Advisors, Soros Private Equity, Summit Partners, Thoma Cressa Partners, Tudor Investments
 - **Sept. 17, 2005**
 - The Harmonie Club, 4 East 60th street.
 - 10AM -1PM
 - W/ YVCS discount, \$99
 - Register at www.yvcs.com (events)

For info on our **BIOTECH EVENT** in **New York**, see page 2. Events in **BOSTON, PALO ALTO, SINGAPORE** or **HONG KONG** are coming soon. Visit www.yvcs.org for more info

Smile 'N Dial

A NEW VC APPROACH TO SOURCING DEALS

By: Paul J. Marino
Mathew Gulner
Patrick Michel

When was the last time you were excited to receive a telemarketer's call? Well for most of us, the answer is never. However some people, such as entrepreneurs seeking capital, will be very glad to receive the call. Why? Because some Venture Capital ("VC") firms have adopted a form of proactive deal sourcing known within the industry as "Smile N' Dial".

Venture capital firms have turned to proactive deal sourcing because of their desire to remove the reliance on external sources (e.g., business brokers, broker dealers, advisors, etc.) and more efficiently integrate the process from identification to investment. Using this technique, an associate in a venture capital firm is given the responsibility of identifying potential companies that fit the firm's investment criteria. While viewed with condescension in other businesses, some associates value the opportunity to connect with executives in this fashion. One Boston based VC associate stated "...calling is a great way to become knowledgeable on an industry and provide associates with exposure to companies".

Conversely, a recruiter with a private equity and venture capital search firm stated that "there is a degree of apprehension and anxiety involved with proactive deal sourcing (especially if it doesn't fit with the candidate's personality). Many Associate candidates view it as a sales role and may consider passing on a private equity opportunity, if the sourcing component represents a significant portion of their job (greater than 80%)." The recruiter also stated, "yet, it's important to realize that proactively sourcing new deals at any PE/VC fund is an important component of a firm's success, particularly in such a competitive deal environment. In addition, an Associate, successful in sourcing deals at their respective firm, is developing a transferable skill set that is highly-valued in Partner-track roles at PE/VC firms".

The process begins when the associate will then contact the company and attempt to have the startup present to the firm. This turns into a win-win situation for all: (i) the associates work on a deal from sourcing until investment; (ii) the venture firm is looking at companies which are much closer to their investment vision; and (iii) the company is presenting to a firm that has already expressed some interest. The Boston based VC associate continued with explaining how valuable it is to hone the skill-set of "being able to bring in deals like a partner". It goes with out saying that (obviously) venture firms do not invest in every company that gets past the "Smile N Dial" screening, but it would seem that receiving an invite to present would increase your probability of success.

~Continued on the Next Page~

UPCOMING EVENTS

New York – BIOTECH

- **What is Biotech and How Can You Make Money In It?**
 - Panel members being confirmed
 - **Mid-November Event**
 - Register at www.yvcs.org

Events in **BOSTON, PALO ALTO, SINGAPORE** or **HONG KONG** are coming soon. Visit www.yvcs.org for more info

The Write Time

EXPOSE YOURSELF

The Young Venture Capital Society is looking for **new contributors** to the newsletter and resources page on interesting and educational content. Topics we are focused on include:

- Angels and angel networks
- Biotech and life science primers
- Primers (Educational Intros to Sectors)
- Secondary investing
- Placement agents
- Raising capital in 2005
- Tech transfer investing
- And numerous other topics....

If you **interested in contributing** on these or other topics, please contact us at info@yvcs.org

Key Terms In This Issue

Powered by VC Experts

Accredited Investor - Defined by Rule 501 of Regulation D, an individual (i.e. non-corporate) "accredited investor" is a either a natural person who has individual net worth, or joint net worth with the person's spouse, that exceeds \$1 million at the time of the purchase OR a natural person with income exceeding \$200,000 in each of the two most recent years or joint income with a spouse exceeding \$300,000 for those years and a reasonable expectation of the same income level in the current year. For the complete definition of accredited investor, see the SEC website.

Private Placement Memorandum - Also known as an **Offering Memorandum**. A document that outlines the terms of securities to be offered in a private placement. Resembles a business plan in content and structure.

As one would assume, the reliance on this proactive deal sourcing technique varies among practitioners. The time allocation and job responsibilities of associates tasked with executing the technique varies from 100% sourcing/cold calling companies, to a mix of sourcing and deal work. Some of these practitioners include TA, Summit Partners, Battery Ventures, Insight Partners, Platinum Equity, Spectrum Equity, Pequot Ventures and Concert Capital Partners.

It may surprise some that so many "name brand" VC firms have adopted the proactive model but it should not, "As partners and other senior officers become increasingly tied up with portfolio companies or general operations of the firm" the recruiter stated, "they have less time to source new deals. As a result, they are looking to have junior professionals handle more of that function".

One final important aspect to note is that the variation in implementation of this technique directly impacts the daily life of associates and analysts. While some analysts and associates are working on deals brought in by them or others, and continuing to source new companies to bring and meet with, other analysts and associates at other firms are dedicating 100% of their time to cold calling companies and only working on deals that they bring in from their sourcing efforts.
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The Disclosure Syndrome

When Early Stage Companies Cut Corners Early On

By: Paul J. Marino
Patrick Michel

To most that operate within the early stage company space, the initial foray into the venture capital world is known as the "Friends and Family" round (obviously getting its name from the people who are most likely to invest in the nascent company). However, to the experienced venture capitalists and service providers, this early stage investment round presents a host of problems typified by the problems associated with inadequate investment disclosure documents. Simply put, it is in the earliest stages of the capital raising cycle that a company (due to lack of financial resources, know-how, etc.) neglects to provide investors with the necessary information to make an educated decision regarding the investment opportunity presented by the company and it is at this time that the company unwittingly takes on risks associated with neglecting to do the same.

In reality, the "friends and family" round (for the purposes of this article the "Friends and Family" round shall not include professional angel investors) is not very different from any other capital raise. The company, in need of capital, seeks investors who are willing to make an investment in exchange for an equity position in the company. What differentiates the friends and family round from the later rounds of investing is the sophistication of the investor (and quite often the company). Most unsophisticated investors do not turn over of the proverbial due diligence "rocks" of the potential investment and in the same vein most startup companies do not provide investors with the necessary documents to do so. The reason for the lack of disclosure documents and short cuts taken is because the friends and family round is generally a quick, get-it-done on a shoe-string budget where the company drafts one-page disclosure statement that is (usually) not in compliance with disclosure rules set forth by state and federal securities law.

While a discussion on how securities laws protect investors is far too complex for this article, the spirit behind the laws are to protect the investor by giving her as much information as possible in order to make an educated decision regarding the prospective investment. To achieve this objective, the security laws (both state and federal) force companies to disclose as much information about themselves as possible so to enable a reasonable investor to make an educated assessment about the investment risk associated with the company.



Book Review

Advanced Private Equity Term Sheets and Series A Documents

Joseph Bartlett, Ross Barrett and Michael Butler
ISBN: 1588521206
Published on November 1, 2003,
Published by Law Journal Press

Reviewed By: Paul J. Marino

Okay, you're probably thinking, "Why would a non-attorney (or even an attorney) read a treatise on private equity transactions?" Well for starters, if you have a desire to understand from top to bottom the terms of a private equity transaction and why each term/clause/section is negotiated in or out of a deal, then you should purchase this book. In short, it is an excellent desk companion for any private equity professional.

Advanced Private Equity Term Sheets and Series A documents ("APETS") includes negotiating tips, deal documents and real life scenarios that the authors have encountered during their deal experience (one of the co-author's has a deep reservoir of deal experience, Joseph Bartlett, see, YVCS December, 2004).

What You'll Learn:

- **Easy to Read:** The book does not read like stereo instructions. For instance, the authors did not start the opening chapter on liquidation preferences or full ratchet anti-dilution clauses but instead gave a brief but information introduction to venture capital (history, how it evolved, etc.).
- **Comprehensive Information:** Great overview of the journey from term sheet to definitive agreement and along the way take the time to discuss the intricacies of each transaction but never taking for granted that a reader may not be familiar with a particular nuance or facet of a private equity transaction.
- **Real Life Situations and Applicability:** Further to that point, as the authors take you through the evolution of a private equity transaction (e.g., from term sheet to definitive agreement), each chapter gives a synopsis of how that particular term and/or issue came about and how one should prepare to negotiate for or against it (obviously depending on what side of the transaction one is on: buy or sell side).

~Disclosure Syndrome Continued~

Ideally, the company would want to draft a private placement memorandum (the "PPM") or a document as close to a PPM as possible. It should contain, among other things, the business description, risk factors (i.e., you could and may lose all of your investment), terms of the offering, current financials, an affirmation by the investor that it is an accredited investor (as defined by Regulation D) and a snapshot of the management team. These documents should give the proposed investor enough knowledge about the company to make an educated and discernable decision as to whether it wishes to invest. A well prepared private placement will serve both the function of disclosing the risks and the potential investment upside. Unfortunately, however, what the investor usually receives is a business card and a one-page business plan that contains phrases such as "can't miss", "holy grail" and "ground breaking".

Undoubtedly, the decision to forego the proper disclosure documents by most early stage companies, especially companies with novice entrepreneurs at the helm, is more of an error of omission than an overt decision to defraud a proposed investor. Even where the investor does have considerable knowledge of what the proper disclosure documents should resemble, many an entrepreneurs will make self-serving justifications such as the shareholders of the company are better served by not spending money on consultants, accountants and lawyers since the company and investors are theoretically aligned in interest. While, this frugal approach might be well received by some like-minded shareholders most regulators would not be in agreement. In fact, if a regulator is alerted to the non-conforming offering (usually by a by a disgruntled investor, employee or both) the company and perhaps even the management, may wish that it had elected to spend the money to provide the proper documentation.

Even if all investors of the company are content with the company and its progress, the lack of proper documentation in the offering round may haunt the company in future offerings. For example, if the company is successful and elects to pursue professional investment, the professional investor is sure to discover that the company never complied with governmental regulations and could either walk from the deal or force the company to go back and recreate the transaction (which could prove problematic if the company has sputtered and the initial valuation was much higher than the current valuation). Nonetheless, it would be foolhardy for a professional investor to proceed with its investment if, as a result of an incomplete offering, the possibility existed that the company might have to defend itself against an investigation or lawsuit (a question for debate is whether this potential liability should be disclosed on the balance sheet).

So, what should a company do to avoid such a potentially disastrous situation? First, the management team should contact an attorney who is versed in this area and will help the management team and company navigate the potentially dangerous waters of seeking capital. For many startup companies, the fees involved in retaining experienced counsel are often too high and as a result the inexperienced management team will forego retaining experienced counsel. When in fact the fees associated with obtaining experienced counsel will undoubtedly be far less than the fees associated with defending a lawsuit brought by a disenchanted investor or the loss of a professional investor as a result of its unearthing of incomplete or non-existent disclosure documents from previous capital raises.

Second, after the company has interfaced with experienced counsel, it should, with the aid of counsel, begin to sculpt its offering documents including its business plan (an executive summary will do), offering memorandum, which should have a fairly straight forward risk factor section, description of the management team, an affirmation from the investor that it is an accredited investor and the stockholder or voting rights agreement.

- **Templates and Materials Provided:** The book comes with a CD Rom full of boiler plate deal documents that are useful to any professional either as a starting point for drafting or a baseline to compare documents against.

The Drawbacks:

- **It is a reference book:** While it is user friendly, it is closer to a Russian novel than it is to John Grisham—i.e., don't expect to bring it to the beach.

Final Thoughts

As stated, APETS is not an easy read but if you're interested in understanding the inner workings and machinations of a private equity transaction together with a better understanding of the terms most hotly negotiated and contested by private equity professionals then it is the book for you.



Below are some interesting and educational blogs and links to check out.

BLOGS

- VentureBlog – www.ventureblog.com
- Allen Morgan - <http://allensblog.typepad.com/>
- Steve Brotman - <http://brotman.blogs.com/vcball/>
- Steve Jurvetson -<http://jurvetson.blogspot.com/>
- Fred Wilson - <http://avc.blogs.com/>

LINKS

- VCfodder – www.vcfodder.com
- VC Experts – www.vcexperts.com
- SJ Mercury News - <http://www.siliconbeat.com/>



Third, the company should attempt to target investors who add intangible value as well as cash. The importance of having the right investors is paramount in any company but especially critical in a startup company where the investors may be the first introduction to professional management and assist the company in areas such as intellectual capital (big ideas), social capital (who you know), and management capital (the willingness to share management ideas, know-how).

Lastly, it is equally important that the company understand the expectations of the investor and if and when possible manage those expectations so as to avoid any over promising and under-delivering on potential returns (a classic startup company dilemma). Accordingly, it is as important to receive smart money as it is to receive money itself and as so the management team should use jurisprudence in deciding which investor will become a part of the company.

In conclusion, while obtaining capital may be the paramount activity of a startup company, the fact is that the management team should also be aware that every decision it makes regarding how it seeks investors and the information it presents to the same may impact both current and future events.

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Where Ideas Meet Funding

American Venture Network announces the acquisition of BusinessPlanPosting.com, expanding into the online investment market. American Venture Network, owner of American Venture Magazine, the leading publication solely dedicated to the emerging growth technology market and the entrepreneurial world, has announced its expansion into the online investment market with the acquisition of BusinessPlanPosting.com

"We are thrilled to have BusinessPlanPosting.com", says Timothy O'Malley, President of AVN and Publisher of the quarterly printed magazine." This deal is a natural bridge from being the premiere provider of venture capital news to bringing the players together to do business. We look forward to every deal".

This website stands as the best choice for entrepreneurs and start-ups to find a place to post their business plans and have access to a community of accredited investors. "We are passionate about creating a community where you can build long lasting partnerships to take your idea from the drawing board to the market place" explains O'Malley.

BusinessPlanPosting.com offers the opportunity to either post an executive plan or upload an entire business plan for viewing by investors. These investors can contact posters directly and make the deal happen.

This site not only provides a meeting point, but it also features a shopping section with the best "VC Tools" to help developing business strategies and careers, such as business planning software, venture capital directories, entrepreneurial guides, and much more.

With specific articles and news, multimedia gadgets (such as online video presentations, coming soon) BusinessPlanPosting.com is dedicated to make funding searches truly productive.

This incredible world, where exciting business ideas are coming into life, is reflected in BusinessPlanPosting.com.

New Info, Tools and Events from YVCS_E

Entrepreneur's Help Desk

- In the coming months, the Young Venture Capital Society will create a new platform where entrepreneurs can receive trustworthy answers from VCs.

YVCS – Entertainment Division (Film and Music)

- With an increasing number of film producers and related individuals contacting YVCS for funding sources, we are organizing the YVCS Entertainment division in Los Angeles and New York. This new group will organize events and create content to better tackle funding and all other issues occurring in the entertainment fields.

CFO Corner

- We are actively looking for CFOs of VC firms to talk about what they deal with and how other interested professionals can learn from their experiences.

 RRE Ventures


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PUBLIC RELATIONS



The 2005 Women's Technology Cluster Entrepreneur Venture Conference

Tuesday, November 1, 2005, at the Microsoft Silicon Valley Conference Center, Mt. View, CA.

The conference showcases high-caliber, women-led technology and life science companies to an audience of VCs, angel investors, and industry experts. Last year's conference, produced in conjunction with Springboard Enterprises, had over 400 attendees, 50 exhibitors, and 24 presenters – 1/3 received funding, and two companies received over \$5M in investments – a success measure unparalleled in the industry. In fact, it was at this conference that Hummer Winblad Venture Partners and portfolio company Palamida first met, leading to a \$5M investment together with Walden VC. It is because of this that we are pleased to participate in and endorse the 2005 Venture Conference.

Presented annually, the WTC venture conference offers a unique approach to the investor presentation. The Conference, coupled with an Entrepreneurial Immersion Program (EIP), is designed to prepare the Entrepreneur for the fundraising process and to help mitigate the inherent risks associated with equity investing. Through the EIP sessions, entrepreneurs engage industry experts and work side by side with seasoned CEOs and coaches. The EIP includes half-day sessions on topics such as Market Analysis, Business Plans, Financials and Term Sheet Negotiations.

When considering opportunities to meet quality entrepreneurs, we hope you will consider the value of attending the 2005 WTC Entrepreneur Venture Conference. We encourage you to register early.

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