intelligent.ly presents

Get Funded

Expert Advice From People Who Know

It's All About the Benjamins

When it comes to funding startups, Silicon Valley Bank (SVB) has seen the good, the bad, and the ugly.

This eBook will give you foundational of knowledge and first-hand insight about how and when to take advantage of some of the most important and popular funding mechanisms.

“With every round of financing you raise, think about what you are going to achieve, and what options you’ll open for your company.”

– Dan Allred, SVB Financial

Expert Advice

The information in this eBook was first presented live to startup founders and team members at Intelligent.ly – a learning campus in Boston.

SVB's Dan Allred and Smith Anderson took students on a back-stage tour of the otherwise exclusive and intimidating funding machine, offering insight into how and when to use different types of financing at different inflection points in the growth of a startup.

Dan Allred
Silicon Valley Bank

Smith Anderson
Silicon Valley Bank

People Who Know

Three of Boston's all-star startup CEOs weighed in on their own funding journey and lessons learned:

Aman Advani
Co-Founder & CEO
Ministry of Supply

Brent Grinna
Founder & CEO
Evertrue

Jason Jacobs
Co-Founder & CEO
RunKeeper

Bootstrapping

Crowdfunding

Equity

Debt

Get Funded

Bootstrapping

“Think about whether you really need funding to get where you’re going.”

– Aman Advani, Ministry of Supply

Bootstrapping

"Bootstrapping" was a term first popularized in the early nineteenth century; it referred to taking on an absurdly impossible task. Today the term has been appropriated by a class of ambitious entrepreneurs and startup aficionados.

The premise is simple: you're bootstrapping when you found and build a company from personal finances or from your company's initial revenue – in either case, you're starting with a small amount of capital.

As a founder, bootstrapping allows you to maintain personal control over all decisions, without consulting other investors. However, this form of financing may involve unnecessary personal risk. Additionally, it may ultimately jeopardize the success of your young enterprise; too small an initial investment may handicap your company by not allowing it to grow at a reasonable rate.

Bottom Line

- Requires a relatively small amount of initial funding
- Useful for startups and companies of all sizes
- Can involve significant personal risk

Tips & Techniques

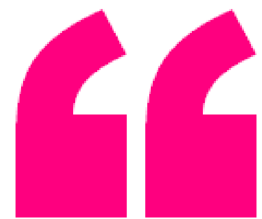
Self-financing: Many founders reach into their own pockets when bootstrapping. Tread carefully here. Working without pay (and asking others to do the same) is one thing. But taking out new mortgages or using personal credit can have long term consequences. It's not uncommon to hear founders (typically the successful ones) joke about the fact that, for example, American Express has banned them for life after a bumpy start on their first business.

Vendor financing: If you're lucky and strategic, you can launch your company by leveraging your payables and asking vendors for trade credit. For example, small retailers are sometimes able to fill their shelves and actually sell their current season's merchandise before ever needing to pay the vendor.

Customer financing: Customer financing is sometimes described as "selling ahead of your product." The idea is to pull your revenue forward by collecting pre-payments. This strategy can work particularly well for ventures that are service-based or that involve significant amounts of new R&D and ongoing consultation with the client.

"Moonlighters working for equity became my founding team. It was about finding people who had a mentality that was aligned with mine."

– Jason Jacobs, RunKeeper



Crowdfunding

"In the end, it's about users.
Consider swapping out some meetings with
investors for meetings with customers."

– Brent Grinna, Evertrue

Crowdfunding

Seek out and leverage small contributions from many. Think Girl Scout cookies.

This is a particularly good funding mechanism for:

- Consumer facing projects
- Micro-market products
- Market “unknown” products
- One-off garage projects
- Hardware with production or prototype costs
- Artistic or philanthropic projects

Before embarking on a crowdfunding campaign, remember that this funding mechanism will put you and your company very much in the public eye. You can have no secretes and you can tell no lies (no matter how white). Putting everything on the table is essential for winning support from individual backers, but it also shows your competition your entire hand.

Bottom Line

- Best for novel retail products or philanthropic projects
- Large companies have trouble crowdfunding
- Complex or B2B products are also hard to crowdfund

- **Instant access to cash, risk free:** When launching a crowdfunding campaign, you have to set a funding goal or minimum threshold amount. Once that threshold is crossed, you enjoy instant access to the cash. On the other hand, if your funding goal isn't met or the project fails, you have almost no liability to your backers as you're not promising repayment.
- **Proving your market in advance:** Assess customer demand and market viability *before* having to make expensive strategy or production decisions. Knowing how many and what types of people are interested in your product, and knowing how much they're willing to pay, allows you to move forward with confidence once you're up and running.
- **Perfecting your story & inspiring brand advocates:** Successful crowdfunding campaigns all share one thing: compelling and well-crafted stories. Remember, your nascent venture is a veritable needle in haystack, vying for attention and support from potential funders. It'll be obvious if your story isn't getting traction, and you'll have plenty of opportunity to tweak it and try again. Once you've perfected your pitch, your supporters will amplify your success by re-marketing your story for you. If you do it right, you can create a customer-base that is literally sitting on the edge of their seats waiting to buy.

Crowdfunding

This Forbes article provides a good overview of crowdfunding platforms.
And of course we have our own list of buzz-worthy sites:

Pledgie (2006)
Sellaband (2006)
IndieGoGo (2008)
GiveForward (2008)
Kickstarter (2009)
RocketHub (2009)
Fundly (2009)
GoFundMe (2010)
Appsplit (2010)
Microventures (2010)
Fundageek (2011)
Dragon Innovation (2013)

Crowdfunding

Tips & Techniques

Donation crowdfunding. "Investors" pledge support in return for products, perks or rewards, but no equity.

Investment crowdfunding. Many "investors" purchase small amounts of equity. Policy makers have been talking about making regulatory changes to the tax and reporting obligations in these cases (see JOBS Act, July 2013), so be sure to talk with a lawyer and an accountant before heading down this path.

Friends and family rounds are sometimes lumped into the crowdfunding category and can be either "donation" or "investment" based. To first time founders, this can seem like an easy route, but can ultimately carry some heavy consequences.

"The single biggest myth we love to dispel about Kickstarter is that there's anything organic about it. It's tremendously high risk from a time perspective."

– Aman Advani, Ministry of Supply

Equity

"It's not about convincing non-believers, it's about finding believers."

– Jason Jacobs, RunKeeper

Equity

If you're looking for large amounts of capital, or are dreaming of scaling a bigger company faster, equity investors may be able to help. But know that with the sale of stock, you're not just getting into bed with your investor(s) – you're not just agreeing to share control of your company – you're agreeing to get married.

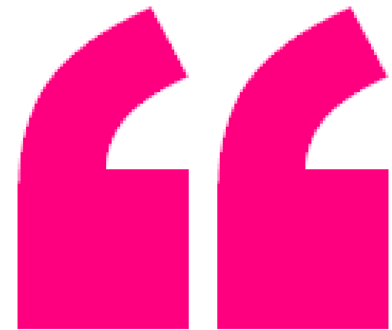
You're committing to work together. A lot. Every day. Until you secure an exit – be it acquisition or an IPO – equity investors will be looking for a timely exit.

Bottom Line

- Helps startups scale faster with access to larger amounts of capital
- Best when founders also envision exiting through acquisition or an IPO
- Don't expect to be able to negotiate terms

“Raising venture capital isn’t success.
It’s when you return many multiples to your investors – that’s success.”

– Brent Grinna, Evertrue



Angel Investors

Angel Investors are high net worth individuals who trade seed funding for equity. Angels typically invest $100k to $2mm per project and time their investments to help early-stag companies (often just as startups are graduating from an incubator/accelerator program). Since early stage investments are considered high risk, Angels typically end up with a 25% to 50% ownership stake.

Partnering with an Angel who shares the same vision as the founding team can bring huge strategic insights, as often they've been involved in similar companies before. Alternatively, other Angels prefer a more hands-off approach, especially when they don't have industry specific experience. Before teaming up with an Angel, decide if your venture would be better served by "smart (involved) money" or "dumb (arms-length) money;" there are advantages to both.

Angel Groups, Angel Clubs & Super Angel Groups

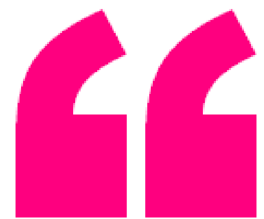
These are all collections of Angles that invest as a group. Each has its own profile in terms of how involved the investors will be in ongoing company strategy and management.

Venture Capital Firms

Venture Capital Firms invest on behalf of their own group of private and institutional investors. Typically they invest between $1mm and $20mm per project and expect a successful exit within 7 to 10 years. Since they can provide essential cash and connections to help a startup grow quickly, VC dollars are in high demand and short supply. If they're willing to invest, VC's generally negotiate for a significant portion (20% to 40%) of your company as preferred stock; this increases their potential profit and limits their potential risk. It's also common for them to require the formation of a board and request a seat at the table. (By the time a VC-backed startup is ready for an IPO, founders are lucky to retain 5% to 7% ownership.)

"The smartest people in the world, great investors … they're in Boston. It's a great place to start a company."

– Brent Grinna, Evertrue



Fine Print

Don't expect to be able to negotiate terms. Trying might cost you the deal.

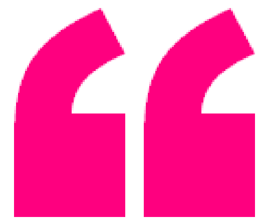
Common vs Preferred stock. Unlike common stock, preferred stock comes with special provisions that limit shareholder/investor risk; these often include terms to guarantee a fixed dividend and protect the investor if the venture folds.

Convertible Debt and Warrants. Sometimes investors (especially Angles) structure investments as "convertible debt" and issue "warrants" rather than sock. These warrants allow investors to convert their loan into stock, usually preferred stock, at some point in the future. They may also save a bit of money because issuing debt comes with cheaper transaction and legal fees.

Redemption & Registration rights. A redemption right gives investors an "out," allowing them to force your company to repurchase their shares. A registration right effectively allows investors holding restricted stock to demand that the you register their shares with the Security and Exchange Commission, effectively making their stock available for sale to the public.

"We've closed big deals over a beer, and tiny deals over many months of negotiation. It varies."

– Aman Advani, Ministry of Supply



Tips & Techniques

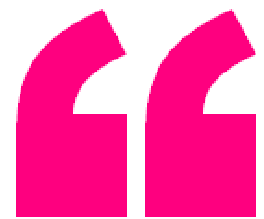
Before getting in bed with investors, take the time to understand their motivations and expectations.

Reporting. How often do the investors want updates on your progress and how much detail are they interested in?

Board of Directors. Do they want to lead or sit on your Board? How involved do they like to be in day to day operations?

"Look at your peers and find out who invested in them to begin building relationships with investors."

– Aman Advani, Ministry of Supply



Debt

"It's about traction and sales. Those are the guys getting funded right now."

– Smith Anderson, Silicon Valley Bank

Lenders can be great bedfellows for startups and founding teams. By taking out a business loan or other type of venture debt ($1mm to $100mm), you can access needed capital to drive growth without losing control of your company. The catch is that you need to demonstrate your ability to pay back what you borrow.

Banks issue loans and also accept deposits. They earn their keep from the interest on loans but also from the management fees associated with keeping an account.

Finance Companies and **Debt Funds** are corporations and limited partnerships (respectively) that don't accept deposits, but do offer interest bearing loans.

Bottom Line

- Debt gives you immediate access to capital, often without losing any stake in your company
- An option for those envisioning long-term ownership of their "life-style" startup or small business

Tips & Techniques

Proof of Revenue. Most lenders require proof of current revenue as part of their underwriting process, thus debt financing is often best suited for startups that have already built sales momentum.

Venture Debt (pre-revenue). Some lenders will work with startups at earlier stages, approving so called "venture debt." Since these loans are approved based on expected rather than existing revenue, they are thought to be higher risk and thus come with a higher price tag. Unlike traditional loans which include repayment with interest, venture debt also requires the creation of **warrants** and/or entitlements for company stock (typically preferred stock) at a fixed price. Structuring debt agreements this way is perfect for earlier stage startups with little or no revenue.

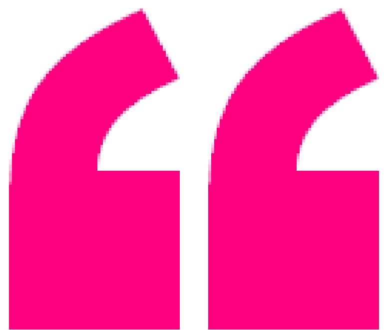
When to borrow. The most common reasons for borrowing are when a company wants access to either working capital, growth capital, or acquisition capital.

Who to borrow from. Research lenders to compare fees and rates. They vary.

"Meet as many people as you can."

– Smith Anderson, Silicon Valley Bank

Get Funded



"Put a stake in the ground and get started."

– Jason Jacobs, RunKeeper

It's not uncommon for a company to employ a range of different funding mechanisms at different points in its growth – starting out bootstrapped, before seeking crowdfunding, and then moving to VC backing and a portfolio of bank loans to help finance strategic acquisitions.

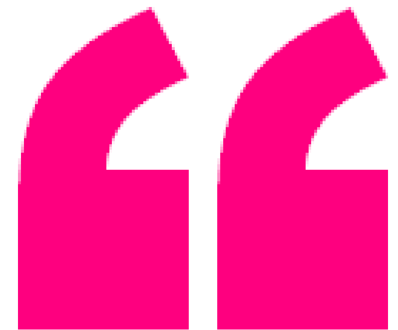
To evaluate which option(s) are best for you, talk to folks who have done it before. Appeal to your network and listen to their stories.

Bottom Line

- Funding decisions should hinge on your long term vision for your company.
- If your goal is to run a small to mid-sized life-style business, you may be best served without outside investment; relying on revenue and debt instead.
- If you're hungry for something bigger and can envision an exit via acquisition or IPO, you'll likely want to go after Angel or VC support.

"If you ask for money, you get advice.
If you ask for advice, you get money.
Have conversations and build relationships."

– Dan Allred, Silicon Valley Bank



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