The Ten Steps To Raising Money from Angel Investors

By David S. Rose

NY Business Expo 2012 is bringing together thousands of dynamic startups and small businesses from the tri-state area. Some will be showcasing their products and services on the show floor, many more will have the opportunity to interact with experienced mentors in the Startup Central area. In both areas and throughout the show, New York's early stage business angel investors and venture capitalists will be out in force, all looking for 'the next big thing' into which to invest.

Raising equity funding from outside investors is competitive. Very, very competitive. In fact, only in one out of every 40 companies seeking angel funding manages to get the brass ring (the odds for venture capital funding are even tougher.) To give your venture the best possible chance of raising money from these early stage funders, and to stand out among the thousands of great startups and small businesses in New York, you need to be at the top of your game. Here is a step-by-step guide to raising seed capital to accelerate your venture:

1. **Understand your business.** It sounds obvious, but the majority of entrepreneurs who pitch me have obviously never thought through many of the major issues surrounding their companies. You should know EVERYTHING about your business, product, customers and competition. You should know every metric regarding customer acquisition, conversion and retention. You should have a crystal clear understanding of your business model and your financials. And all of this should be at the tips of your fingers so you can instantly answer any questions you are asked about it.

2. **Understand what investors are looking for**, what they usually invest in, and why. There is a vast gulf between a 'cool product' and an 'investable company,' and if you don't understand the difference, you will be doomed before you start. There are many good books on this subject, and you owe it to yourself to read at least one of them before you begin talking to angels. A good beginning would be Bill Payne's *The Definitive Guide to Raising Money from Angels*, available as a free download from http://gust.com/definitiveguide/.

3. ONLY after you've completed #1 and #2 will you then be ready for capital to be applied to your venture. And that **capital is going to come from...YOU**. That's right, you should not even consider trying to raise money from anyone else until you have reached deep into your own pocket. This is the case for two reasons: first, because the bare fact is that investors simply do not fund ideas. The expectation is that in an era of increasing technology and decreasing costs, you will be bringing them an operating company with at least some traction. Looked at from their perspective, given two teams equal in entrepreneur, market, business model and potential, why should they invest in one that exists only on paper, when the other has reduced its risk and improved its viability by actually getting started? The second reason is that investors want to know that YOU believe in your own startup...and the best way for you to demonstrate that is to show that you have personally put your own money where your mouth is. Keep in mind that any cash you put in will remain in the company as Founders' Equity, and will only come back

to you on a successful exit in which your investors make money.

> [3a. Although it is not required *per se*, and therefore is not being given its own discrete step here, in the real world most startups at this point **turn to friends and family for additional capital**, in the form of equity or loans, to help get the company to a stage at which it is legitimately investable by third parties. The important thing to note about this is that the money should either go into the company directly as a convertible note without a cap, or (depending on the personal relationships involved) as a personal loan to the entrepreneur, which he or she in turn invests as equity into the company, but will be responsible for repaying even if things don't work out.]

4. With #1 - #3 under your belt, you should start **preparing the components you will use to support your pitch to outside investors**. These range from outbound materials, such as pitch emails and funding applications, to presentations of your venture in different forms for different purposes, to detailed back-up information that you will be asked to supply during due diligence. (See the sidebar for a comprehensive list of things you should have.) All of these pieces should be neatly gathered into a confidential investor relations site, such as one that you can create at no cost with Gust.com.

5. Now, and only now, are you prepared to **start fundraising**. This phase is a combination of (to mix several metaphors) Weapons of Mass Destruction…and sniper fire. Start by letting absolutely everyone know that you've got a great startup looking for early investors. And I mean <u>everyone</u>. I have been led to deals by my barber, my interns, my mother and my high school classmates. If you hide your light under a bushel, investors simply will not come looking for you proactively. At the other end, do your homework to really understand which investors would be the most productive for you to approach. Some only invest in their home city, others only invest $5,000, still others only invest in biotech, for example. Blindly sending your business plan to every single angel and VC in the world will have zero effect, and simply clogs the system while annoying everyone.

6. Seriously consider **applying for funding from your local angel investment group**. There are many hundreds of these across the country and around the world, and virtually all of them accept applications over the transom. You can find a comprehensive list at gust.com/find-investors. The largest group in New York is New York Angels (newyorkangels.com), with other local groups including Golden Seeds, Archangel Fund, Keiretsu Forum, NY Life Science Angels and Tevel Angel Network. If you are invited to come in and pitch, even for a preliminary screening, you will have the opportunity to present your business to experienced investors. This will give you both presentation experience and usually solid feedback on your plan. And if you do get funded, the group can be extremely helpful in getting other investors to join in with additional funds.

7. Another avenue that is increasingly a good idea is to consider applying to one of the new breed of **accelerators**. While yCombinator in Silicon Valley is the best known, there are dozens of others; local, national and international, many specializing in specific areas (including fashion, food, finance, gaming, etc.) Here in New York some of the leading

accelerators are TechStars, ERA Accelerator, DreamIT Ventures, LaunchPad and NYCSeed. Accelerators typically provide several months of intensive mentoring, at the end of which they host a Demo Day to introducing all their graduating companies to a large number of local angel investors.

8. Your goal in all this is to try to **find a lead investor**. This person will be critical in rounding up other investors, drafting a term sheet, and generally getting the deal done. He or she will be your primary champion, and often mentor. Doing a deal with a lead investor is three to five times easier than trying to pull everything together by yourself. Among other things, your lead can vouch for you with other investors in their circle, or who follow them on online financing platforms, which can be a good way to finish up a round (via "social proof") once your leads are in place.

9. Before you start negotiating a term sheet with any potential investor, make sure that you **GET A LAWYER**, specifically, a lawyer with experience directly in the early stage financing world. This will NOT be your family lawyer, or the one who helped you beat that traffic ticket. There are excellent venture lawyers in every major city, with enough to form a flash mob here in New York.

10. Finally, from the minute you begin engaging with an investor, it is critical to **COMMUNICATE** early and often. Keep them up to date while circling your round, thank them as soon as it closes, and provide ALL your angels with either quarterly (at a minimum) or monthly (ideal) reports on how the company is doing. In my experience there is a astounding correlation between frequent, thorough communication and successful follow-on funding.

David S. Rose is a serial entrepreneur and active angel investor, described by *Forbes* magazine as “New York’s Archangel”, and by *Red Herring* as “patriarch of Silicon Alley.” As an entrepreneur he has founded half a dozen companies, and as a ‘super angel’ technology investor, has funded over 80 others. He is the founder and CEO of Gust, the entrepreneurial finance industry's infrastructure platform; founder and Chairman Emeritus of New York Angels; Managing Principal of Rose Tech Ventures; a partner in True Global Ventures (an international super-angel venture capital fund) and Founding Track Chair for Finance, Entrepreneurship and Economics at Singularity University in Silicon Valley.

Your Investor Pitch Toolbox

If you meet a VC for 30 seconds in an elevator, you certainly aren't going hand her a 30 page business plan. Although it sounds like overkill (because you won't need all of these for every VC), a well-prepared entrepreneur will have all of the following, to be used at the appropriate times:

Written

- A one sentence (or sentence fragment) tag line

- A professional business card
- A one or two paragraph email introduction to the business
- A 'one-pager' overview
- A 2-3 page executive summary
- a slide deck specifically designed to be handed out
- A thoughtful, comprehensive business plan: either (a) a traditional 10-20 page written plan, or (b) a carefully prepared and annotated 'business model canvas'
- A finished (or prototype) marketing brochure

Live
- A one sentence description
- A 30 second elevator pitch
- A 5 minute 'quick pitch'
- A 15-20 minute angel/VC PowerPoint/Keynote pitch
- A sub-15 minute foolproof product/site demonstration

Online
- A functional public web site
- A short video pitch
- A dedicated, controlled access, investor-relations profile on a site like Gust.com

If you have all the above, you'll be fully prepared for any sequence of events as you interact with prospective investors.

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