



Angel Investment Clubs Summary

By Seth Temko

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Angel investors are typically individuals that invest money in start up or small company growth investment opportunities. Often times these early stakeholders invest in ideas in the concept phase, well before there is a “company”. Typically funds are invested in exchange for equity in the business or idea. In most cases, angel investors have little or no day-to-day management, nor do they necessarily participate at a board level.

Angel investors who choose to make regular investments into these early stage companies need to be prepared to spend a fair amount of time creating, vetting and managing “deal flow”. Deal flow is an industry term often time used when referring to a pipeline of potential investments. More often than not, an entire raft of companies needs to be vetted to find the few companies that will be deemed worthy of an investment.

Traditional Angel Investor Clubs

Angel Investor Clubs are affiliates of angels that work together, and sometimes with other similar clubs, in an organized fashion to find worthwhile investments, which meet the financial risk objectives of the club’s charters. There are no set models for how a club functions. Minimally the participants of the clubs have regular meetings and at least loosely defined investment criteria.

- Structured clubs – with executive director, breakfast meetings, presentations and lead due diligence person.
- Unstructured clubs – no staff, opportunity sharing.
- Kieretsu – very large networks.
- Sidecar funds – Common Angels, NY Angels.

The most highly effective Angel Investor Clubs are operated if not as businesses, like business. There are application processes by which investors join the clubs. Staffs and committees with business and investment backgrounds work with the clubs. In these cases there are established rules and procedures both for companies seeking funding, and investors who wish to participate. Investors may pay annual fees or dues to participate in the club. Prospect companies, who wish to be considered by the club, go through a vetting process in which they fill out applications, which follow pre-defined and standardized description and presentation formats. Standardization allows potential investors/club members to quickly assess and evaluate a candidate company's position and attractiveness as quickly as possible. Additionally, standardization helps members consistently benchmark their evaluations against the club’s pre-defined investment objectives, minimizing emotional reactions to particular presentations. Companies seeking investments many times pay a presentation fee (typically \$3,000 - \$5,000). The fee offsets the cost to administer and vet the companies and also weeds out “conceptual” or poorly founded businesses from strong candidates for investment. Typically there are regular investment presentation sessions in which companies have 20 minutes to present (in a defined structured format), 10 minutes to answer questions, followed by a coffee or cocktail mixer where they can then mingle with investors and answer more individual and specific

questions. The presentation sessions are usually not more than 2 to 3 hours. There is longer half day or full day presentations formats but those are usually only held once or twice a year. At the end of presentation sessions, investors submit a list of companies they are interested in learning more about, and a diligence committee member or club administrator makes contacts available to the presenting companies to discuss next steps.

Some clubs create standard investment documents that investors have access to, but largely, individual investors work with the prospect companies directly because often companies seeking investment will have their own offering documents and investment contracts.

Clubs truly are designed for the investment members and have several committees that define the club's goals, approve companies for presentation opportunities and create funding rules. Goals can include investing in certain types of companies (i.e. high tech, biomedical), regional location of companies (i.e. local) and existing businesses (i.e. those seeking growth capital). Criteria for presentation can include companies with certain management talent present, unique product opportunities, those companies that already have products and are seeking capital to go to market, etc.

Example Keiretsu Forum Presentation Agenda:

Summary of the Presenting Companies

RedShift Networks - Amitava Mukherjee, CEO

RedShift is an Innovative Enterprise Unified Communications Security company. We provide a new level of enhanced and proactive security for next generation Unified Communications Networks.

Kingstone Media Group - Art Ayris, CEO

Kingstone produces and sells comics, graphic novels, books, and films for both the faith market and crossover general market.

MNM Partners - Mark Putney, Managing Member

MNM Partners LLC is a Tenant in Common (TIC) Sponsor investing in commercial property only in Northern California.

Green House Data - Shawn Mills, President

Green House Data is a 100% wind powered data center facility that offers colocation and managed hosting services without a premium 'green' price tag.

Billing Revolution - Andy Kleitsch CEO

Billing revolution partners with global brands to process credit card transactions on mobile phones.

Aug 29 – Keiretsu Forum Silicon Valley

7:30am-11:30am; Fenwick & West, 801 California St., Mountain View

Guest Speaker: Rob Rueckert - Director, Intel Capital (*Focus Areas: Business Internet/Web 2.0*)

Rob joined Intel Capital in 2002. Prior to Intel Capital, Rob spent 10 years in the software industry. He spent 5 years as a senior engineer / CTO with a few start up companies and an additional 5 years as a senior software consultant with Arthur Andersen. Rob is board observer for Iovation, InSync Software and Arch Rock. Rob led the assembly of SuiteTwo, the Intel enterprise collaboration suite that includes NewsGator, SixApart, SocialText, SpikeSource, Visible Path and SimpleFeed. In his role in Portfolio Management, Rob managed over 8 IPOs and 30 exits, including LANDesk, MusicMatch, Groove, Zone Labs and TimesTen amongst others. Rob has a BS in Information Systems from Brigham Young University and a MBA from the University of Chicago.

Current Economic Climate Opportunities

Most angel investment clubs seek to invest in early stage companies but in the current economic climate there is a tremendous opportunity for angel investors to participate in later follow-on investment rounds associated with more mature companies.

Structured Debt

The recent banking meltdown and regulatory changes have dramatically changed the way more traditional lenders, such as banks, can do business and who they can do business with. Banks have been forced to dramatically reduce their risk exposure on traditional business loans and lines of credit, which presents an opportunity for early investors.

An interesting opportunity may exist for a club to include in its deal flow criteria, businesses that may be seeking to include debt, in addition to equity, as part of an overall capitalization strategy. There are several advantages to these types of investments for the prospect company as well as the investor:

For Investors

- Debt can be securitized by all of the assets of the company including inventory and A/R.
- Debt typically provides a guaranteed rate of return.
- If the business plan does not go as initially planned and the business gets in trouble, lenders take a liquidation priority over equity holders.
- Debt can be structured in convertible instruments that allow investors to “wait and see” and convert debt to equity upon certain milestones or “events”.
- Loans typically have performance covenants, which can provide additional protection to investors

For Companies

- The cost of debt in early stage companies is often much less than the cost of equity
- A revolving loan that is based on a percentage of Inventory and/or A/R, a company can better plan its working capital and associated costs based

on its sales forecasts. Often the only financing a company in the sales mode needs is to finance finished goods or cover for the time that it takes customers to pay for those goods. In the case of “cash and carry” businesses, the capital requirement may only be needed to finance inventory.

- A convertible note structure can postpone the need to establish a value on the business until there is an event. This allows a company to potentially sell less equity, although it can work both ways.

Acceleration Partners

For those angel investors with rich management backgrounds and the ability and desire to work closely with startup or “turn around” companies, opportunities to become acceleration partners may be attractive. Acceleration partners actively work with and participate in startups or troubled companies less to provide financial capital, but more to help structure and often times restructure companies so that they may be more attractive to investors.

Many companies naively believe that their only issues are capital and that infusion of capital will solve everything, “If I only had a million dollars I could...” syndrome. A significant challenge, which most startups and early stage companies struggle to see, is how to become more attractive to investors. They might lack management talent, have operational issues or inefficiencies, be poorly structured financially, etc. In many cases, “a million dollar” investment alone would only provide companies the ability to do more of what they are doing (potentially wrong) for longer.. There is a great need and opportunity for talented managers to “jump into the trenches” with these companies and tackle the greatest issues that have caused a company to plateau or decline in business growth. In these situations, acceleration partners gain a vested equity position and may garner some minor financial compensation for their participation. These partners typically are involved through the “turn around” and subsequent financial round of investment. At that point, the company should have sufficient financial resources to bring in full-time management talent to take over the acceleration partner’s role.

Additional Resources

“Best Practices Guide for Angel Groups and Investors” from the National Angel Organization of Canada can be found here:

http://www.angelinvestor.ca/Best_Practices.asp

For more about acceleration partners:

<http://www.firstascentventures.com/blog/?p=26>

Kieretsu Forum (one of the largest groups of its kind):

<http://www.keiretsuforum.com/frontend/index.aspx>

About the Author – Seth Temko

Seth Temko comes from a long background of creating new technology products in new markets opportunities at several startup companies over the last decade with such titles as Founder, CTO, Vice President of Product Management, Director of Product Strategy and Consultant. His roles have included technology management, marketing strategy, business development, operations management, product management and Ecommerce initiatives for several companies including Monster.com, Covad Communications, Tesla Capital, Hartford Computer Group, NEC-Mitsubish Displays, Vital Link Business Systems, Capton, KindMark, Virtual Relocation.com, Sessions and PEACE of MIND Technologies. He has been part of startup teams that have raised millions in VC funding, sold to a large public company, restarted companies based on "fire sale" of assets and out of court work outs and done "boot strap" startups.

His strategic thinking combined with practical execution strategies has made him highly effective in working with start up and early growth companies. He is able to "fill the gaps" on management teams from business strategy initiation through business inflection growth points. Seth holds a B.S. in News Editorial from the University of Illinois, Champaign-Urbana and a MBA from Aurora University.

Seth was born and raised in Chicago. He has been married to his wife of 14 years Wendy. They met in high school. He has worked and lived in Aurora, IL for four years. They are blessed with two healthy sons and currently live in the Chicago suburb of Prospect Heights, IL.

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