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# Entrepreneurial Financing—Alternatives for Raising Capital


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# Entrepreneurial Financing—Alternatives for Raising Capital

## **Cover Page Footnote**

From the “Practitioner’s Corner”

## *From the Practitioner's Corner*

# Entrepreneurial Financing—Alternatives for Raising Capital

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**M**ost entrepreneurs are continually concerned about their finances. Their companies perhaps not yet profitable, they may have a fear of “running out of dry powder.” These entrepreneurs often have fallen in love with their company’s technologies, products, and potential markets, but they require more resources. Invariably these emerging ventures shroud their fear of the grueling capital raising marathon by presenting voluminous business plans to potential investors. They often flaunt their “optimized business models.” Investors, however, typically want to know why the potential investment is such a good deal. The entrepreneur often wants guidance regarding what to say to whom in a changing financing environment.

In this article, our “Practitioner’s Corner” associate editor Joe Levangie collaborates with a long-time colleague Paul Broude to address how businesses should “make their capital-raising initiatives happen.” Levangie, a venture advisor and entrepreneur, first worked with Broude, a business and securities attorney, in 1985 when they went to London to pursue financing for an American startup. They successfully survived all-night drafting sessions, late-night clubbing by the company founder, and even skeet shooting and barbecuing at the investment banker’s country house to achieve the first “Greenfield” flotation by an American company on the Unlisted Securities Market of the London Stock Exchange. To ascertain how the entrepreneur can determine what financing options exist in today’s investing climate, read on.

We start with a quiz:

January 26, 1983, a date that forever altered how startup companies went about the grueling process of raising capital. Was it:

- A. A spectacular rise or fall in the prices of NASDAQ stocks?
- B. A dramatic change in securities laws governing the sale of stock?
- C. A seismic shift in the Federal Reserve Board’s interest rate policy?

The answer is “D, None of the Above.” January 26, 1983, was the day Lotus Development Corporation released its first version of Lotus 1-2-3®, encouraging would-be entrepreneurs everywhere to create 50-page spreadsheets that fore-

cast the successful growth of their fledgling enterprises. The process of obfuscation was set in motion: too much data with too little meaning. Worse yet, entrepreneurs started to believe that these spreadsheets were the “truth!”

### Keeping It Simple

Fast-forward to 2006: The numbers still count, but today’s entrepreneurs need to have more—and less—than an extensive Excel® spreadsheet to raise capital. Across all types of financing—and we’ll examine current trends in various capital markets—businessowners seeking capital need to focus on three core questions that define the business opportunity.

1. What is the problem the entrepreneur is trying to solve?
2. What is the company’s solution to the problem?
3. Who is the buyer for the company’s product or service?

The concept of an “elevator pitch” is a bit of a cliché, but in reality it has become very difficult for companies to raise capital unless management can concisely identify—generally in five minutes or less—the market opportunity, its solution, and its customers. Most financing sources are less interested initially in seeing a 50-page business plan with full-blown financial projections than in a PowerPoint® slide deck that succinctly lays out why customers need the company’s new product.

The entrepreneur should try to think about these three core questions in their most basic terms—the more easily the product advantages can be explained to potential customers, the easier they will be to explain to investors, and the more likely it is that these money people will grasp the opportunity. Two Boston-area companies illustrate this KISS (Keep it simple, Sid) concept.

- Embo-Optics, LLC, based in Beverly, Massachusetts, has successfully raised startup capital from friends and family and angel investors. The company identified an easy-to-understand problem: Military personnel frequently need to give wounded soldiers intravenous drugs in the dark. Many battles take place at night and traditional lighting is either unavailable, or its use would give away the soldiers’ position to the enemy. Embo-Optics created the Pin-Lite™, a small, disposable, pinpoint light that clips onto a syringe and illuminates the patient’s vein to allow easy and safe insertion of an IV line in low-light conditions.

- Carbonite, Inc., based in Boston, Massachusetts, has raised money from friends and family, angel investors, and more recently, from a venture capital fund. Carbonite identified a problem faced by almost every home computer user—the loss of precious family photographs and other data when a computer crashes. Carbonite developed an on-line backup system that automatically backs up a user's computer to Carbonite's secure storage network without the need to copy photographs or files to CDs or other storage media. Carbonite software works in the background whenever the computer is on, and doesn't require any input from users after the initial setup.

### **“Further on Down the Road, You Will Accompany Me . . .”**

This Taj Mahal classic song could be an anthem for investors in today's venture climate. Most financing sources expect companies to be further down the road to profitability, or at least to products, than during the financing “boom times” of the past. Gone are the days when an internet (or other) start-up can raise money on a concept alone. Demo products are the rule; the easier the product is to “touch and feel,” the easier it is to raise money. As a result, founders are finding that they need to devote more time, and more of their own (or perhaps their family's) money to the initial stages of product development.

The ability of a financing source to observe a product prototype can be the difference between a new investor for the entrepreneur and a polite “no thank you.” Embo-Optics was able to provide prospective investors with sample Pin-Lite and other products, even though the production versions of the products would ultimately change somewhat. Similarly, Carbonite was able to provide potential investors with a trial version of the product to back up photographs on their home computers. The chance for investors to touch and feel a product, and see how it works, can be invaluable. In a classic case, when first getting started, snack food maker Smartfoods reportedly dropped off big bags of its popcorn at the homes of prospective investors with nothing more than a request to “try it and let us know what you think.” The result was a successful early stage financing for the company.

At a minimum, the entrepreneur should let investors see how the product would work. If there is no prototype, a website visualization can be a powerful tool. Drawings or pictures also are helpful. The better job the entrepreneur does to illustrate the product and its advantages to potential customers, the easier it is for investors to understand. Can the entrepreneur explain to his or her grandparents what the venture is all about? If investors don't appreciate how the product works and why customers will buy it, chances are

good that they won't invest. Most investors initially don't probe much, and if they don't understand the product or strategy, it becomes easy for them to simply say “no.”

### **Everything I Know about Starting a Business, I Learned from *Star Trek***

First-time business founders are usually “true believers”—and they need to be to have the determination, perseverance, and commitment to get a new company off the ground and a new product to market. But they are often driven by multiple motives, such as the psychic satisfaction of “building a better mousetrap,” solving a problem that has caused them personal hardship (not uncommon in startup medical device companies), creating an “alternate working environment” or “being their own boss.” Conversely, investors are single minded about a new investment opportunity: How will this business make me more money tomorrow than I am investing today?

Entrepreneurs need to recognize this dichotomy early on if they hope to have any chance to raise growth capital successfully. What does this mean in practical terms? Consider:

- *Star Trek* had “The Prime Directive”—*don't interfere in another world's business*. The entrepreneur needs to be equally single minded about the company's goal. The entrepreneur's Prime Directive: The first and only goal is to *make money*. Investors don't care that a new medical device will detect a particular disease sooner than current competing products if no insurance company will pay for the new test. Investors don't care that a company might be able to obtain patents in 35 countries to protect its technology if that technology can't be used in a product someone will buy. In a technology company, the goal is to turn science into money, not money into science. Every decision the entrepreneur makes should keep in mind the Prime Directive.
- The entrepreneur needs to be flexible about his or her role in the business. If the entrepreneur is primarily a “techie” who doesn't have prior experience managing a business, there must be acceptance that he or she might not be the CEO of the company forever. The skills needed to get a startup off the ground are very different from those needed to grow a profitable business or manage a more mature and more administratively complex company. Professional investors understand this and can help the company grow, and help founders adapt to changing roles. Entrepreneurs need to demonstrate the willingness to change their roles as the company grows—investors will generally turn down investment opportunities where ego-driven founders insist in advance on control of the company “no matter what,” since this demand can easily get in the way of the Prime Directive.

- The cash-starved company should also demonstrate flexibility when considering different forms of new investment. The company would be well advised to consider all reasonable funding sources and to try to avoid biased views. Even though, for example, it is true that Joe “Bananas” Bonanno, head of one of New York City’s five crime families, listed his occupation as “venture capitalist,” that alone does not mean that all VCs are bad people! Further, even if the company decides that it wants to avoid the entanglements of a VC investment, it might be beneficial to pitch the company’s story “off-Broadway” to some “friendly” VCs. They can be a great source of feedback to help the entrepreneur better focus his or her fundraising efforts.
- The entrepreneurial team shouldn’t think about the apocalypse. Too many founders spend time negotiating provisions of investment documents that are a lawyer’s parade of horrors—and which have little chance of ever impacting the company. For example, venture capitalists often include a registration rights provision for their shares that, taken at face value, would enable them to “force” the company to go public. The practical reality is that no company can effectively undertake a public offering without management’s cooperation, and underwriters are rarely willing to include many shares from existing shareholders in an IPO. Spending time and legal fees arguing about these types of provisions make the entrepreneur seem shortsighted, and can make investors question the founder’s priorities and business savvy.

### “Location, Location, Location!”

Entrepreneurs—particularly those starting their first business—too often focus on the wrong issues. Unlike the real estate truism regarding “location,” financing a startup is not all about “valuation, valuation, valuation.” Founders need to be realistic about valuation, particularly during the early rounds of financing with friends and family, angel investors, and venture capital firms. They also need to take the right steps—and align themselves with the right advisors—to enhance their chances of success. Some guidelines:

- First-time entrepreneurs should think long term about the financing needs and business opportunities the company will face. Founders who focus on control and dilution, rather than on owning a smaller piece of a growing, successful enterprise, will invariably choke off financing for their companies. Professional investors and experienced entrepreneurs recognize that rapid growth (needed to beat the inevitable competition) requires substantial resources and a talented team, both of which will leave the founder with a smaller—but probably more valuable—piece of the pie. A detailed discussion of

entrepreneurial control vs. value has previously been discussed in this Practitioner’s Corner column (Levangie 2005).

- First-time entrepreneurs should also think long term about their careers, and be prepared to give away more of their first startup—it’s the price of entry into the exclusive and rewarding club of serial entrepreneurs. Entrepreneurs should think about hitting a single with their first company, a double the next time, and home runs with subsequent businesses. Raising capital is exponentially easier for a seasoned, successful entrepreneur than for someone starting a first business.
- To borrow from George Orwell’s *Animal Farm*, “All dollars are equal, but some dollars are more equal than others.” Family and friends may get you to the stage where you can attract serious professional investors, and may be the first necessary step for many startups. But as choices develop, keep in mind the things your investors can provide, and look for the so-called “smart money.” Most venture capitalists, and many angel investors, can provide access to high-level contacts with potential customers, suppliers, joint venture partners, and future sources of financing. Their circle of business contacts can provide, for example, access to joint venture participants or Chinese manufacturing partners. Generally, Aunt Millie doesn’t offer the same entrée to those parties.
- Choose your advisors well. Experienced outside directors, lawyers, accountants, and other business advisors can provide introductions to potential financing sources, as well as intermediaries who raise capital for early-stage companies. The entrepreneur often needs advice in problem solving from those who have successfully confronted the same problems in the past. But beware of building an “artificial” board—having a “name director” who doesn’t attend meetings or provide real assistance won’t buy you much with financing sources, especially if he or she hasn’t invested a meaningful amount of money in the company. It’s far better to have committed directors who can provide real product, market, or industry experience, rather than a recognizable but inactive board member.

### How Much Is that Doggy in the Window?

The classic question every entrepreneur asks when starting to raise capital: “What’s my company worth?” To determine the answer, the entrepreneur could go back to that 50-page Excel spreadsheet, look at the projected revenues and EBITDA (earnings before interest, taxes, depreciation and amortization) in year 5, apply an assumed multiple to determine the value of the company at that time, and apply a discount that will yield the prospective investors’ hoped-for IRR (internal

rate of return). Why not? It's no less accurate than all of the assumptions made in the plan about manufacturing and selling costs, achievable market share, and a myriad of other items that go into preparing financial projections. Of course, the calculus becomes more complex when one considers that value/EBITDA multiples vary by market sector, as recent values demonstrate below (Capital Q 2006):

- Telecon services and equipment: 11.5 X
- Technology hardware and electronics: 13.5 X
- Software: 34.0 X
- Pharma and biotech: 5.6 X
- IT services: 8.5 X
- Internet software and services: 13.7 X
- Healthcare equipment and services: 13.1 X

The reality is that one might as well stick a finger in the wind, and see which way the breeze is blowing. Investors have a herd mentality that is hard to break. The best indication of value is probably the price at which other local startups and early-stage companies have raised capital, in most cases regardless of the industry they have targeted. In round numbers in the current venture market, the entrepreneur might think about premoney valuations of \$1.5 to \$2 million for friends and family financings, \$3 to \$5 million for angel rounds, and similar or modestly higher premoney valuations for seed round venture financings. Unscientific? Absolutely—but practical. There are, of course, variations based on specific circumstances; for example, a company started by a successful serial entrepreneur, or a company that has already brought products to market and eliminated technical risk, may command higher valuations.

The entrepreneur's friends and family may be willing to pay a higher price today (they may invest based more on emotion than financial analysis). But if the venture overprices this "friendly" investment, these friends and relatives are bound to be disappointed when the angel or venture capital investors in the next round insist on a lower valuation, and they perceive that they have already "lost money." If that happens, the entrepreneur's family will still be "family," but the entrepreneur's friends . . . ?

### **What's Happening Now?—Angels vs. VCs!**

In addition to some of the points discussed earlier, there are some discernable trends in today's market relating to angel investors, venture capitalists, commercial lending, public offerings, and other forms of entrepreneurial funding.

#### ***Angel Investors***

Angel investors are increasingly banding together in groups to evaluate potential investments. The advantage to startups is that it is easier than ever to meet a number of angel investors, who historically were hard to identify and contact. The disadvantage: Like venture capitalists, angels have devel-

oped a sense of safety in numbers—if one or two angels in a group pass on an investment, the rest may be inclined to do the same. Like VCs, angels prefer certain market sectors. Willis (2006) reports on a UNH study (Center for Venture Research, Whittemore School of Business and Economics), which analyzed how 126,000 angels invested \$11 billion in 26,000 ventures during the first half of 2005. The allocation of funds was distributed as follows:

- Health—20%
- Biotech—17.5%
- Software—17%
- IT services—13%
- Hardware—6%
- Semiconductors/networks—5%
- Financial services—4%

Angel investors are behaving like venture capitalists in other ways as well, particularly within groups. Angel groups do more extensive due diligence than in the past; valuations closely track comparable venture capital valuations (see above); and the group can offer help with industry and financing contacts, and in recruiting additional management. However, one study (VSS Project Angel Investors 2005) found that angels are still more likely to invest in first-time entrepreneurs than are venture capitalists.

An increasing number of angel investors and/or financial intermediaries (i.e., "finders") are putting together "one-off" investment vehicles to invest in a particular company. While this has the advantage to an entrepreneur of dealing directly with fewer investors, the structure tends to slow down later financing rounds as the early investors try to minimize dilution if they are not in a position to provide additional financing.

There are several networking groups for angel organizations. Entrepreneurs can access the Angel Capital Association ([www.angelcapitalassociation.org](http://www.angelcapitalassociation.org)), a nonprofit organization that publishes a directory of investor groups on a regional basis. Examples in the Boston area include Common Angels, which claims 34 IPOs in its portfolio, and Launchpad Venture Group, which invests \$100 to \$500 K in technology-driven startups.

#### ***Venture Capital***

On the face of it, venture capital funding seems to represent the most fruitful source of financing. After all, there are approximately 700 VC firms in the United States collectively managing about a quarter of a trillion dollars (Anthony 2006)! The problem these VC firms have managing so much money is that the risk-reward model is tempered by practical limitations of deal size vs. the number of deals that can be transacted. The attitude of VCs toward risk is becoming more conservative. The big New England VC firms (e.g., Highland Capital Partners, Greylock, Atlas, Polaris, Venrock, Advanced

Technology Ventures) are typically investing in bigger deals like Rib-X Pharmaceuticals (New Haven)—\$50 Million—and TagSys USA (Cambridge)—\$35 million (Calnan 2006). As a result, venture capital still remains a small minority of seed round financings, representing less than 4 percent of all seed financing in 2005, according to a PWC MoneyTree survey, as reported by Buckman (2006).

In 2005, aggregate investments by angels (\$23 billion) and venture capitalists (\$22 billion) were roughly equal, but angel dollars were spread over 49,500 earlier stage deals averaging around \$500,000 each, while VCs invested in just over 3,000 deals, most of them later stage investments averaging close to \$7 million each, as reported by the Angel Capital Educational Foundation (2006).

During 2005, New England companies raised approximately \$2.79 billion in 293 venture capital financings as reported by Venture One (2006). The last five years show a steady downward trend in the number of VC deals, and a leveling off of overall dollars invested after a steep decline from the highs of 2001:

- 2001 - # = 474 (\$5.05 billion)
- 2002 - # = 358 (\$3.02 billion)
- 2003 - # = 329 (\$3.03 billion)
- 2004 - # = 314 (\$2.81 billion)
- 2005 - # = 293 (\$2.79 billion)

The terms of VC deals have changed somewhat in recent times. Since transaction value has been trending upward, there has been a movement toward “milestone investing,” where funds are meted out based on the company’s attainment of agreed on milestones. VC syndicates have borrowed a poker term wherein venture capital financings have seen “pay-to-play” provisions, where investors lose certain rights if they do not participate in future rounds of financing, and creep into “up rounds,” where the value of the company is increasing. Historically, such provisions have applied only in “down rounds,” where the value of the company has fallen from the last financing. More overlays of complexity to give the entrepreneur a headache!

### ***Current “Hot Buttons”—A Green Example***

Anecdotal evidence suggests that “Renewable energy in ‘06 is the dot-com of ‘99,” with \$3 of investment funds chasing every \$1 of potentially viable opportunities. Included in the “green” case histories are:

- Konarka Technologies Inc. (Lowell, Massachusetts), with \$20 million from its recent round of VC funding, has developed carbon nano-tubes to capture solar energy to convert to electric power (Regan 2006).
- WindTechCo in Freetown, Massachusetts, is selling small windmills for homeowners’ backyards.
- The city of Burlington, Vermont, has completed the first hydrogen fuel station in New England, producing hydro-

gen from wind power and using the hydrogen to fuel hybrid vehicles.

- The Massachusetts Technology Collaborative has its Sustainable Energy Economic Development (SEED) initiative, and in 2006 made \$1.4 million in loan grants to Seahorse Power, maker of solar-powered trash compactors; Premium Power Corp, maker of fuel cells; Agrividia Inc, a biomass products company; and Stellaris, a developer of solar films.
- Other regional fuel cell companies attracting capital include Nuvera Fuel Cells (Billerica, Massachusetts), Acumentrics (Westwood, Massachusetts), and Fuel Cell Energy (Danbury, Connecticut).
- Boston-based RockPort Capital Partners raised in 2006 a \$261 million venture fund (Galante 2006) to invest in “clean energy” and environmentally friendly products, materials, and technologies.

Stay tuned to see if this latest of the venture market’s hot areas continues, even as oil and gas prices continue to fall.

### ***There Are Alternatives—You Can Take That to the Bank (or Not)***

The good news is there are more banks lending to young companies, as well as an increasing number of nonbank venture lenders who provide debt financing. Given the entry of new players into this market—both bank and nonbank—over the past several years, debt financing for growing businesses is somewhat more readily available than in the past. In addition, competition has, in many cases, brought down the premium above the prime rate charged to smaller customers, although most such loans still involve warrants to purchase the company’s stock, or other equity “kickers.”

The bad news is “smart money” still counts. Glen Mello, senior vice president and regional manager of Square One Bank, an active lender to startup companies, notes that most bank lenders will consider prerevenue and preprofitability loans only to companies that are backed by venture capitalists or other institutional investors. Those kinds of relationships are key to a bank’s decision to lend to early-stage companies. Nonetheless, entrepreneurs should plan ahead: When choosing a bank for a startup, the entrepreneur should pick one that will ultimately be a likely candidate to lend the company money as it grows, rather than the local branch of a savings bank that will never be a source of business financing. The sooner companies can develop relationships with a bank that can track their growth and progress, the more likely it is for that bank to become a source of financing (or source of leads to other investors) down the road.

### ***Cries for Liquidity: “How Do We Get Our Money Back?”—What Are the Options?***

The range of options for achieving liquidity for investors is

intriguingly broad and diverse; the choices perhaps difficult to make. A simplified decision tree for the entrepreneur to provide an exit position for the company's investors might include the following branches:

- Sell the company—a Merger & Acquisition (M&A) transaction.
- Pursue a conventional Initial Public Offering (IPO).
- Pursue an IPO on a overseas stock exchange.
- Execute an Alternate Public Offering (APO), or a variant thereof.

### ***Selling Out—New England M&A Activity***

Acquisitions have represented a frequent exit route for New England-based, venture-backed companies. According to the Venture One survey (2006), over the last five years, the region has experienced the following activity:

- 2001—48 M&A deals
- 2002—52 M&A deals
- 2003—39 M&A deals
- 2004—56 M&A deals
- 2005—64 M&A deals

The region produced two large M&A transactions involving Transform Pharmaceuticals and Imagitas—each for \$230 million. With its access to private and university R&D, the venture capital network, and the pool of technical and professional talent, New England remains a center of entrepreneurial activity. Accordingly, larger companies are typically drawn to the region seeking M&A transactions with smaller entrepreneurial companies.

### ***Rethinking the IPO Option***

IPO activity for emerging companies continues to be quiet, with only a relative handful of transactions in 2005 and 2006 compared to prior “boom” years. The market has been less receptive. Dozens of IPO offerings in 2006 [e.g., Alien Technology (bar code technology) and Go Daddy (Internet address registrar)] have been “yanked.” The companies themselves are also less receptive. Sarbanes-Oxley (SOX) and other corporate governance reforms have made IPOs less attractive as financing and exit vehicles for entrepreneurial companies.

The Venture One data reflects the reluctance to “go public.” The IPO activity for New England-based, venture-backed companies has been as follow:

- 2001—1 IPO
- 2002—0 IPOs
- 2003—3 IPOs
- 2004—7 IPOs
- 2005—8 IPOs

All the IPOs for 2004 and 2005 were in Massachusetts. The 7 IPOs in 2004 were all in life sciences; the 8 IPOs in 2005 involved technology and life science companies.

The reasons for low IPO activity seem clear. The relative burden on smaller companies of complying with SOX often outweighs the perceived benefit of being a public company. Since the enactment of the Sarbanes-Oxley Act, the average annual cost of compliance for companies with under \$1 billion in annual revenue has increased more than \$1.8 million to approximately \$2.9 million, representing a 174 percent overall increase (Foley and Lardner 2006). As a result, entrepreneurs and their venture capital backers are more often looking to a sale of the business as the preferred exit strategy.

### ***Going Overseas—the AIM Option***

Increasingly, smaller U.S. companies are considering an IPO on the Alternative Investment Market (AIM) of the London Stock Exchange, instead of a U.S. IPO. Two decades ago, the two coauthors were involved in a successful London USM (Unlisted Securities Market) IPO of a zero-stage Boston-area company. The USM has since 1995 become the AIM. Massachusetts companies such as online advertising broker, Burst Media, and e-commerce software vendor, Elcom International have opted for the AIM route.

Companies that list on a foreign market such as AIM generally escape the reach of Sarbanes-Oxley and other U.S. securities laws, subject to some exceptions (Broude 2006). However, most shares of AIM-traded companies are held by a limited number of institutional shareholders, with less activity from retail investors than U.S. markets. As a result, the AIM market does not necessarily provide the liquidity for shareholders that a U.S. listing provides. In many cases, an AIM IPO financing may be a form of “public” venture capital.

### ***Writing a “Blank Check”—the SPAC***

Despite the high costs of being a public company, some small and mid-size businesses continue to look at alternative ways to attract public investors and to provide subsequent liquidity for their early investors. Some raise capital by merging with a SPAC (Special Purpose Acquisition Company). A SPAC is a “blank check” company founded by a management team that usually consists of former CEOs, investment bankers, or fund managers. The SPAC has no initial business, instead it raises money in an IPO and then looks for a business to acquire. Some or all of the cash raised in the SPAC's IPO can then be used as growth capital for the combined companies. Over the last three years, more than 65 SPACs have completed IPOs, and more than two thirds of those are still looking for acquisition candidates. Currently, according to recent registration statements filed with the SEC, there are approximately 40 SPACs with a total of more than \$3.8 billion looking for companies to buy. Additional SPAC IPOs that are in process could double that amount.

There are a host of practical considerations about a transaction with a SPAC:



- Entrepreneurs can't have any discussions with a SPAC until it completes its IPO. SPACs must avoid such discussions so that they are not required to disclose information about a target acquisition in the prospectus for its IPO.
- The SPAC's shareholders must approve any acquisition, which tends to make transactions with SPACs take longer than other forms of financing. In addition, up to 20 percent of the SPAC's public shareholders can choose to vote against the deal and obtain a refund of their share of the proceeds of the SPAC's IPO, which makes the SPAC's capital structure somewhat uncertain until the deal is completed.
- A SPAC is essentially a shell with only part-time management looking to acquire a company. As a result, the entrepreneurial business acquired by a SPAC must be ready, as soon as the deal closes, to become an SEC-reporting company and comply with all of the SEC rules, including Sarbanes-Oxley.

### ***Playing the Old Shell Game—the APO***

In a variation on this alternate financing theme, some companies have completed an Alternative Public Offering (APO), which consists of a merger with a publicly traded shell company combined with a simultaneous PIPE (Private Investment in Public Equity) financing. A PIPE is a private placement by a public company (in this case, by a newly public

company). In an APO, unlike a SPAC, the publicly traded merger partner often has little or no cash, so the transaction makes sense only if it is combined with the PIPE financing. Some of these publicly traded shells are companies that failed in or sold their original businesses, while others are new entities that were specifically formed for the purpose of completing an APO transaction.

### ***Plus ça change, plus c'est la même chose***

French writer Alphonse Karr (Les Guêpes, Paris, January 31, 1849) had it right: The more things change, the more they remain the same. Raising capital for emerging companies continues to be a long, time-consuming process that strains an entrepreneur's ability to balance the competing needs to move the business ahead while wooing investors.

The relative availability of financing from various sources and for various industries changes from year to year, influenced by market trends, the current economic environment, stock market conditions, and other factors unrelated to any particular business. Outside directors and advisors can be helpful in identifying current trends in financing opportunities and making introductions to the right sources. The key for company founders is to stay focused on identifying and pursuing a real opportunity where they have the ability to seize market leadership. And, above all, remember the Prime Directive!

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Mr. Broude also has served as a representative to the U.S. Securities and Exchange Commission's Council on Capital Formation. He is a graduate of the Harvard Law School (J.D., cum laude, 1982) and Brandeis University (B.A. magna cum laude, 1979). He is a member of the American and Massachusetts Bar Associations and is admitted to practice in Massachusetts. Mr. Broude has twice been named a Massachusetts Super Lawyer.



**JOSEPH LEVANGIE** (joe.levangie@comcast.net) is a Boston area investor, advisor, and entrepreneur. Over the last quarter century, he has helped launch several dozen new business enterprises from first a large company platform, then from a not-for-profit incubator, and later as a venture advisor, as an independent entrepreneur, as an active investor and as a passive "angel." His companies have competed in a wide array of industries: financial services; renewable energy; uninterruptible power sources; biotech; computer hardware, flex circuits and software; medical lasers; electronic retail color-matching systems; radioactive medical implants; food technology; modular housing; semiconductor equipment; specialty materials; and waste tire recycling. The number of Mr. Levangie's ventures successfully completing an IPO has now reached double figures.

Mr. Levangie has served on the BODs of dozens of private and public companies, and has been a guest reviewer at Business Plan contests at MIT and Harvard Business School. He is an active alumnus of both institutions. He currently is vice chairman of Ardour Capital Investments, a New York City investment banking firm.