



# So, You Want to Start a Company?

*Some questions about raising your start-up's first capital.*

by  
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## *Every entrepreneur thinks their idea is great, but can they pass that crucial test ... raising capital?*

Starting in 1968 I have founded or co-founded fifteen companies. Some more successful than others. Since 1981 I have spent a great deal of time helping other entrepreneurs – probably over 100 – to pursue their dreams and start their own companies. I have ended up being on the board of directors of many of these.

Every entrepreneur thinks their idea is great. All the talk and media focus on start-ups in recent years has encouraged many to give it a shot, who otherwise might have been too timid to try. Regardless, many first-timers tend to focus on their product, service or business idea, and pay much less attention to some of the fundamentals that are common to launching any business – those that have nothing to do with the actual business idea itself.

One of those fundamentals that every freshman founder has to grapple with sooner or later, and one that generates the most frustration and wonder, is raising the initial capital that will be needed. Unless the founder is already wealthy or very well connected, this can create one of the biggest hurdles they will face in beginning their journey.

This is what I was faced with just this morning. A talented young woman named Megan has a good idea. She has already invested her own money in buying a great web domain and having a good storyboard for her proposed mobile app developed. She has discussed the concept with several colleagues and even some potential investors. Well, one of them has now asked her for some investment materials. Not full due diligence of course, but just the basics necessary to determine if he wants to take his investment discussion to the next level. This is when she called me.

Megan said, "Help! My potential investor said It would be interesting to know my cost base, development costs platform/app, full P&L forecast etc. What amount I'm raising, current cap table, pre-money valuation. Also, I need help making a data room – what's that?"

I responded, "It's all part of what I've been trying to tell you. No legitimate investor will give you money without your having done all the necessary preparation. Anyone who tells you 'sure, I'll invest' is either bs'ing you, or they have just not asked you for this kind of information – yet. If you approach an investor and they do not at some point ask the following questions, they are not likely to be real investors who will actually write you a check:"

1. What is the business?
2. How does it make money?
3. How will I make money from it - what is your exit strategy, or is your goal to simply have a profitable business that distributes earnings to the investors?
4. Who are the people involved, and what is their experience, skills, knowledge?
5. How much money are you raising?
6. What are the terms - common equity, preferred equity, loan/note, convertible note, SAFE, conversion discount, conversion cap, interest, etc.?
7. What is the pre-money valuation?

8. What are the uses of funds?
9. I'd like to see your business plan, including financial projections, and your cap table.
10. What type of entity is it - C corp, LLC, Sub S, partnership, B corp, etc.; and what state is it incorporated in?

Items #'s 1-2-3-4 would be in your **business plan** (#9).

Don't miss the importance of the 'team'. The ability to recruit others to help you is a key indicator of a successful entrepreneur. Convincing someone else of your vision and motivating them to participate with little or no pay, is one of the most critical factors for success. The range of skills and depth of experience of the team as a whole is a key criterion for experienced investors.

A full P&L forecast (a profit and loss forecast is another way of saying **financial projections**, including all expected expenses, revenues, profits/losses, capital infusion, etc. Usually an investor will be satisfied with one year monthly from the time the capital is raised, and two more years quarterly. Few still expect five years. The 'cap table' is **capitalization table/schedule**, which is a chart showing who currently owns the company.

They want to know how much money you are raising and the valuation so they can gauge if it's a good investment, and how much of the company they might own, for their money.

For example: If you feel the company might be worth \$1,000,000 at the stage you are at, then the pre-money valuation (before the new money comes in) is \$1,000,000. Will the investor agree with you that the work you have done so far, including the money and time you have invested, is worth \$1M as it stands right now?

Then if your goal is to raise \$250,000, That would mean that your post-money valuation (after the new money comes in) would be \$1,250,000. If the investor put in \$100,000 (and you raised the total of \$250,000) his share would equal 8% of the company.

$\$1,000,000 + \$250,000 = \$1,250,000$ .  $\$100,000/1,250,000 = 0.08$  (8% if you raised the entire \$250k). In the future, your post-money valuation of \$1,250,000, would be the starting point for the pre-money for your next funding round – plus and additional value that you may have created by using the \$250K to further enhance the company value.

An entrepreneur cannot afford to take shortcuts with this. All you will do is alienate legitimate investors and turn them off. Not doing homework, and not preparing properly for raising capital, is a primary cause of ending up making very bad deals and even losing control of their own company at some point.

At that point, Megan responded impatiently, "I don't know how to do any of that. Can I provide you the info and you can put it into the correct layout?"

I like to feel that I am educating people when we have these types of discussions, not just advising them with the answers. My response was therefore, "Correct layout for what? There are several documents listed or other information implied here?"

Just for a start, a serious prospective investor will likely want to see the following – in the order you would create, not necessarily the order they would be requested in:

1. Certificate of Incorporation
2. Bylaws
3. Organizational Consent
4. Foreign business filing/approval - depending on state of incorporation

5. Business Plan (detailed description of the business, and answers to my original questions 1-4)
6. Capitalization schedule/table
7. Detailed financial projections (P&L, use of funds, expenses, revenues, investment capital, etc. - 3 years)
8. One-page investor summary (short overview of #'s 5,6,7)
9. Investor PowerPoint slide deck (includes slides addressing valuation, use of funds and limited projections)
10. Investor term sheet
11. Investment documents (stock purchase agreement, shareholder's agreement, promissory note (regular or convertible), SAFE agreement, etc.
12. SEC Regulation D (Reg D) filing (often skipped in friends & family rounds – but still best-practice).
13. A functioning and informative website is very desirable before raising capital.
14. Qualified advisors, in the form of a board of directors or advisory board, although not critical, can be very helpful.

So, my basic advice to entrepreneurs is to get your thoughts down on paper – the best way you can. Start addressing all the above in as much detail as you can. Then you can start refining it using either a trusted advisor or Internet searches to learn the most favored varieties of the documents and formats that you will need. As a first-timer you will probably not raise capital without doing the work. Just having a story board of your mobile app, or even a prototype, proof-of-concept, or working mobile app, or great sample marketing materials, or a mock-up of your new product design, will not be enough. Investors will only give their money to the person they believe can start a real company and then lead/run it.

While many seasoned folks like me are usually willing to help and mentor, we need to be sold on the vision and convinced that you can do the work and go the course. To start with, our contribution is education, not work, at least until we see your work product, determination, hunger to learn, and relentless drive to succeed. *Good luck.*