WHY COMPANIES HAVE TROUBLE RAISING MONEY

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For the most part companies have always approached investors with the dreams of high profits, shared glory, and a piece of the American dream of ownership. Even today, those of us old enough to remember the "wonder" (sic) days of the 1980 limited partnerships, still find amusement at seeing copies of old offering documents that promised instant wealth in oil and gas exploration, motion picture production, real estate development and other exciting new ventures. Never mind the rolling-break-even accounting that ultimately led to everyone receiving profits but those who put up the money, or the lack of distributions because the general partners sold out long before their time. All that seemed to matter was you helped create that wonderful piece of Americana you are now all enjoying.

Well, it's obvious that those days are long gone.

It’s a hard pill to swallow, but most investments are simply not attractive to investors anymore. And why? In general terms it can be summed up with a single statement. Those before you forgot the single most important factor in raising money - "*The investor comes first.*" They gave new meaning to the word pillage. Believing that it was normal to use investor capital for side deals, or to build their individual wealth, company executives seldom produced the kind of profits promised.

So, the question becomes, how do I, seeking investor capital, overcome this apparent lack of investor interest? Well, here are a few suggestions:

1. Have the Right Attitude

Many in corporate management have a natural disdain for investors. They see them as individuals who fail to understand their company and the process of creativity necessary to get a new venture off the ground. It is the arrogance to assume that the only one who can understand a project or new business venture is the Chief Executive Officer of the company seeking capital. Everyone else is somehow less in the chain.

Further, many start up company executives do not look at the investors as partners, but as a necessary evil. They need the funds provided by investors, but don't want all that goes along with using other people's money - that is - accountability. I can't begin to tell you how often I've heard project management say, "Just get me the money and get out of my way. I know

how to make this company successful, I've done it before, and I'll do it again," or " What I don't need is some amateur constantly looking over my shoulder telling me how to run a successful company." What these individuals don't understand is that many investors possess as much creativity and understanding of business in their field of endeavor. You might consider the fact that the investor has obviously achieved enough success in life to be able to make an investment into your company in the first place. Remember, they are not the one asking you for money, you're asking them.

Don't assume the investors are stupid. Be prepared to answer questions honestly. Even though the investor may not talk in the industry jargon, or understand certain nuances, basically all businesses operate the same. While a good business executive can improve the odds with his or her experience, he or she should be able to convey the principles of a business plan in a clear and logical manner.

Lastly, most investor problems can be overcome with a simple principle. Treat investors as you would like to be treated. The old "Golden Rule" is called "Golden" for a reason. If you're not prepared to consider the investors needs, you have no business asking for their money.

2. Provide Accurate Disclosure about Yourself

I once read a business plan where a corporate officer's background was listed in the following manner. (Obviously, the names have been changed)

> *Mr. Jones, age 34, completed his formal education at the University of Illinois in 1979, in which he majored in economic finance. In 1980 he entered the military and oversaw his division's mechanical operations. As a decorated war hero in Vietnam, he received a Purple Heart and was discharged with full honors in 1982. Recruited by Network Cable Television Inc. in 1983, he began his professional career as a technical consultant working closely with the Belize government in the creation of a new communications network. In 1987 he left his position to begin his tenure with North American Manufacturing as the company's chief assistant financial officer where he remains today. Mr. Jones will bring his full skills to bear under the leadership of Mr. Robbins, the company's Chief Executive Officer.*

Yup, you guessed it. The reality is not quite as this bio would lead us to believe. Mr. Jones did attend the University of Illinois, but not the main campus in Urbana, Ill., but the extension at Navy Pier in Chicago (before it closed and became a tourist attraction. He also flunked out after the first semester and was then drafted. He did get a Purple Heart when an errant rocket fragment accidentally ripped into a bunker in which he was hiding, but the wound was minor. He actually never fought in a battle, or even carried a gun. His job was a jeep mechanic. When he was discharged from the military he went to work as a laborer, digging ditches for a cable construction company in Belize Central America. His only contact with the Belize government was as a runner between the company's site and the local government office that required weekly reports of construction progress. And finally, his new job with North American Manufacturing came about because he happened to marry the boss’s daughter.

While not the norm, this type of deception occasionally occurs. Taking credit for important posts, stating famous associations, and building career skills on paper do creep into disclosure documents. In addition, the deceptions don't end there. Take a look at the average financial projections. How can any company that has never been in existence project how well a project will do? Without knowing the details of a project's budget, or other unknown costs, much less the public's acceptance of a project's product or service, most figures have little basis in reality. Even when companies or individuals have a substantial track record, it is practically impossible to pinpoint future revenues or profits. It's all a big guessing game - unfortunately, with the investor's dollars. A little aside, during the height of the dot-com boom, some companies even offered investors a "pro forma price earnings ratio." Think about this. An estimate of fictitious future earnings based on a fictitious future price.

Over the years I have heard every conceivable method of running a company. From those who believe that one must spend the highest dollars to be competitive, to those who believe that spending as little as possible will work. Each company executive or project manager has his or her slant on what it takes to be successful. Obviously, a previous track record can help determine the risk, but few are willing to inform the investors of the real risks involved.

If you want to go out and raise money, tell the investor the truth. Investing into new project is risky. It's a gamble. Even with 144+'s highly mitigated risk "Preservation of Principal" programs there is always some risk. In addition, a project probably won't be successful unless there is enough money to cover unknown contingencies. Tell the investor how you intend to alleviate these risks, what you will do if things don't go right, and what will happen if you can't be successful. The important thing to understand is that by being up-front, investors will recognize that you are indeed a good "businessman," and will likely handle their money as though it were your own.

In addition, there is nothing wrong with stating you don't have all the answers. It goes back to a principle I learned a long time ago. If you want to judge a company, judge the person in charge. The company will always be a reflection of his or her character. I keep waiting for that one project executive who is willing to tell the investor that indeed, in such and such date, he or she failed miserably because he or she didn't know what he or she was doing. As least I would trust the rest of their statements. I would assume that this executive learned from the past and is less likely to make mistakes again. I would also assume that if the executive managed to get to where he or she is today, despite previous failures, there is a good chance he or she has learned how to overcome adversity and will be successful in the future.

3. Adhere to Sound Business Principles

What are the sound business principles that are attractive to investors? Consider the following:

- Until you have achieved profitability, keep your salary low. You do not deserve a high salary simply because you have been paid a great deal by some other company. Salaries should be based upon current and future performance, not the past.
- Don't attempt to leverage investor cash by borrowing. Borrowing costs money and puts the company at risk.

- Keep a cash reserve. Don't spend every available dollar trying to make something work.
- Don't be greedy. Attempt to do back-end deals or co-ventured projects until you have achieved profitability. It is better to share risk than die from it.
- Control costs. Fancy offices, expensive travel, lavish lifestyles can all be accepted once investors have been paid back and the company is making solid profits. Remember, every dollar spent on style, cuts substance. Try keeping money in the project rather than in your back pocket.
- Plan long term, not just short term. Staying power and a long-term reputation are more important than any quick deal.
- Diversify. Don't put all your eggs in one basket. If you have $20 million available for a project, consider ways of making the project work for only $10 million, and use the rest for other products, services, or joint ventured deals. This may mean that you have to give up some control, but at least there is a plan in case things don't go well.
- Create accurate accounting. False assets, overstated revenues, and deceptive balance sheets all come back to haunt a company. They tend to lead to lawsuits or worse.
- Align with solid companies. Avoid the temptation to enter into deals with companies that are shaky. Even though you may be able to cut a better deal with such organizations, you will pay for it in the end. Never be in a position where another company's failure puts your company at risk.

4. Prepare Paperwork for Those you are Approaching, not Yourself.

One of the most glaring mistakes made by those seeking capital centers upon the type of documentation presented to investors. For example, a standard business plan is perfect for a bank, or a single investor, but may be wasted on an underwriter, venture capitalist, or group of investors (i.e. through a private placement/ limited partnership).

Consider the conventional wisdom surrounding a business plan. Most professionals will tell you that a business plan should be brief, with only limited details concerning operations. The main focus should be on the financials and how you intend to pay the money back (an "exit" plan). The idea is that a banker or a wealthy private investor doesn't have time to review bloated documents. They will try to get a quick overview, and then see if you have sufficient collateral, income, or backing to "guarantee" or “assure” the repayment of funds. Their concerns will center upon such items as: (a) how much control you are willing to give up, (b) how viable is your "exit" plan, and (c) how well planned is your financial strategy for building profits. Quite frankly, most private investors and bankers don't trust anything else. If you have the means to pay the money back through collateral, and they can lock it up, you will get the money. In their eyes, a bad deal with good collateral is better than a good deal with bad collateral.

However, when you are approaching underwriters, venture capitalists, or multiple investors, much more is typically required. Did you ever wonder why the Securities and Exchange Commission requires that a disclosure statement (sometimes called a prospectus for an IPO or Offering Memorandum for a limited partnership) is in the form that it is? The main reason is to attempt to standardize not only language, but content as well. Financial professionals understand this and are most comfortable looking at an industry format.

Need proof? Take a standard offering memorandum for a limited partnership and attempt to create content about your business for all the headings. Fill in details regarding "Risk Factors", "Application of Proceeds", "Allocation of Income", "Financing Transactions", "Discussion and Analysis of Financial Condition", "Conflicts of Interest", etc. See how far you can get. When completed, take this document to one of your buddies, and watch the reaction. Your friend will probably fall asleep before completing the report. Now take the same report to your local broker and watch what happens. The broker will get excited. The reason is quite simple. The broker is used to seeing business discussed in the formal context of a Memorandum or Prospectus, and he or she will be impressed that you, the project manager, know something about how the financing process works.

5. Don't Submit Your Capitalization Plan to Everyone at Once

Another big mistake is to prepare a plan, and then attempt to pass it out to as many potential investors as possible. You will find that each investor will see something different in your plan. Some will like a certain section, others will criticize it. Therefore, don't put your plan into a final format and submit it across the board. Do it first as a draft, (sometimes referred to as a Discussion Memorandum) and even then, only submit it to one potential investor at a time. Try to get opinions before you commit to a final course of action. By doing so you will get sufficient feedback, learn what is wrong, and be able to make improvements prior to your next presentation or a final effort.

Also, don't assume that because you know someone in the financial business that you can just give your plan to her or him and "explain" missing details. Your plan, if submitted to any professional, will get reviewed by others. And, there is no guarantee that the person you submitted the plan to will be able or willing to convey your words to another. Assume that perfect strangers will be looking at it, and they will be your harshest critic.

Lastly, don't submit your plan to professional organizations such as underwriters or venture capitalists first. Even if the firm likes what they see, it is likely that they will pass it on to others within the firm for a second opinion, or to others outside the firm who may be called on to reduce the risk through syndication. If your plan is turned down by the first firm, you may not be able to come back with a revision, even by going to another firm. Wall Street is a small place, and most of the firms have connections with each other. The word can get out quite quickly. Therefore, begin submitting your plan with those who are not so important, and attempt to improve the presentation before approaching the big boys. You'll be glad you did.

6. Focus Your Approach on the Negative, Not the Positive

There are two areas where an optimist can hurt you - (a) creating plans to build a nuclear power plant under budget, and (b) the development of the typical start up project sold to potential investors. Both tend to compromise safety in the excitement to meet a goal, and both can have serious ramifications to everyone involved. If you want a valuable tip, worry more about what can go wrong, than what can go right. Plan for the worst, and the positive will take care of itself. This applies toward developing your financial strategy, preparing your business plan, and developing the approach to investors. This mental exercise also allows you to keep everything in perspective and reduce the tendency to be influenced by negative emotions such as greed, apprehension and fear.

7. Be Careful Not to Build On a False Premise

I was once asked to evaluate a merger between a new start-up film production company, and a publicly traded distribution company (OTC) that had fallen on hard times. The advocate of this merger attempted to show, even though the two potential candidates were without any financial substance, that once the merger took place, the "wave of excitement" concerning new management, new plans, and new focus, would create a dramatic change of investor attitude, which in turn would push the price of the public company's stock higher. With the higher valuation, it would then be easier to secure a new round of secondary financing, and eventually enable the merged company to form "solid" alliances and develop new growth opportunities. My answer was as follows:

"Let's see if I got this right. (a) We merge two companies, one that is in debt with no discernable revenues, a shaky track record, and tarnished image, and the second with no track record, big ideas, and no money, (b) we go to new investors with a plan based upon meaningless statements of "undervalued assets" and "off-balance-sheet financing", (c) using investor funds, we pay the enormous legal fees related to the merger, disclosure statements to the SEC, and new offering expenses, (d) we announce the merger in the press in order to get everyone interested so we can artificially prop the price of the stock up, (e) we "ride the wave of excitement" by coming out with a new financing plan, and finally, (f) we somehow come out of this unscathed with no problems such as investor lawsuits, investigations for stock manipulation, improper use of market personnel, and making misleading statements on disclosure statements".

In short, everything was based upon management believing that investors would perceive these two companies as being stronger together than as separate entities, and that no one would really notice the weaknesses. The problem, of course, is what if the author of this plan was wrong on his premise? Be careful of this type of buildup when approaching investors. There is an expression that applies: "Sometimes you can see the stars and still not see the light". Make your plan realistic, based upon substance.

8. Consider More Than One Approach When Raising Capital

Few seem to understand that it is almost as easy to create a financial package for a Private Placement Offering as it is for an Initial Public Offering. Much of the same information is used, and the format, while different, has some similarities. Therefore, when approaching the process of raising capital for a project, consider planning multiple approaches. Since you never know who you may come across, be prepared. IPO's, Private Placements, Cooperative Contracts, Private Equity Offerings, Limited, Partnerships, Limited Liability Corporations, and other forms of financing can all be considered. Be flexible in your plans.

9. Develop a Diversified Team for Management

Control is a key element to many project developers. Few like the idea of giving up control, and most would prefer management or advisors who think along similar same lines, with the same goals, and agenda. While this is fine, sometimes it is taken too far. A good management team is not a social club made up of individuals who have fun, swap war stories, and share common expertise. The best teams are diverse, both in experiences and areas of professionalism. Consider aligning with individuals who have both parallel and contrasting experience. Look for management personnel who cover company weaknesses, either in areas of focus, or in personality. Build directorships or an advisory board that investors might recognize, who possess the talent to advise. In short, don't assume that you can do everything alone, and don't make the mistake of ignoring personnel who may not have experience in your field, but are solid in their understanding of business principles.

10. Consider Forming Strategic Alliances

Investors look at not only your past background and track record, but also judge your capabilities by your associations. There is the old story about JP Morgan being approached by a young man who was convinced that he had a business idea JP would be willing to consider as an investment. When Morgan turned him down, he was devastated, but continued to beg JP to listen. Finally, Morgan told him to show up at the steps of the New York Stock Exchange the next morning. When he showed up, Morgan told the young man to accompany him on the exchange floor. Thinking that he was going to be introduced to other investors he was again disappointed that JP not only didn't introduce him to anyone but didn't even talk to him about his idea. After spending an hour walking around conducting his normal business, JP left, got into his car and said nothing more to the young man.

Thinking the whole episode was a waste of time, the young man returned to his office deeply disappointed. Much to his surprise the phone was ringing off the hook with calls from interested individuals wondering why the young man had been granted an audience with JP Morgan, and what was of such interest to JP Morgan that JP would bring him personally to the NY Stock Exchange floor? He subsequently found all the investor dollars he was hoping to find when he first approached JP.

While you may envision yourself head of a mega-organization some day, it is very difficult to know or control all areas of a project. Consider forming strategic alliances with others who may possess greater experience, have a stronger financial background and reputation, or offer a potential alliance that covers an important segment of your business.

CONCLUSION

So, there you have it; a basic primer for successfully locating and approaching new project financing. Perhaps the next time you decide to attend the local trade show or eclectic party and there is the Wall Street guy dressed in the Brooks Brothers suit that looks horribly out of place, and terribly alone, consider what I've said. This time, be really creative and approach him with your idea with the level of sophistication that makes you stand out from the norm - as a professional who understands the valuable relationship between creating a project and financing a project. Welcome him with open arms and remember - he represents those individuals who have always been gutsy enough to put up the money that have the potential to make your dreams come true.