



Chapman, Spira & Carson, LLC

Venture Capital

Chapman, Spira and Carson, LLC. is an early stage venture capital provider. The term venture capital means different things to different people. If you discussed a venture capital transaction with your conservative banker, he would probably understand the term to mean, providing working capital to an enterprise with proven management that had been successful for over century.

Your banker would require collateral encompassing assets and cash flow far exceeding logic to secure his position. To us, venture capital is early stage financing for an embryonic business with an untested product. What constitutes a business? Any enterprise entered into by an entrepreneur for the purpose of making a profit. What would we define as an early stage venture and why? This one is a little tougher to answer.

We believe that management's track record is the key to assessing the likelihood of a business' success. The fact that a person has been very successful in one type of business may or may not mean he will be successful in another. What was his role in his former business and what is his role in this one? Did he start it from scratch or was it already up and running? Was the product or service his idea or someone else's? The answers to these questions are critically important, but no matter how they are answered would not shut the door. The responses simply influence the terms on which the financing might be arranged. A person who has been successful in all his endeavors to date is likely to have a better chance at succeeding than the person who has tried many things and failed in all of them.

Management ability is more important than the underlying concept of the product or service. Therefore, we spend more time discussing this aspect of a potential client's business. We often ask why management that has a good record of accomplishment lacks enough capital on its own to provide financing to their new endeavor. We would hesitate to provide financing if this question is not adequately answered. There could be extenuating circumstances such as sickness, theft or innovation that outmoded the product. If the competing new technology had been fairly obvious, but overlooked by our suitor, we would worry about his strategic planning ability.

Two additional elements are also critical to the evaluation. Is this a person that has the will to stick to his guns and is hungry as hell? If the answer is yes, then we have the start of something interesting. How good is the idea? Having seen just about everything the human mind can think up over the years is good training for answering the question. An idea's relevance is fairly quantifiable unless you are thinking in terms of new medical, chemical or physical concepts. Again, this would not disqualify the concept, but it would make the process of due diligence much more involved.

If one of the later ideas were to be brought to us by someone that obviously did not have the necessary background in that field, we would probably discount any chances it may have. We have been blessed with a staff that covers most of the bases and is able to intelligently assess the value of most products and services.

If the concept sounds interesting enough and we don't have anyone on staff with the necessary qualifications to evaluate it, we bring in a consultant in that field. Finally, we ask whether the potential client understands that they are a fiduciary for people that have had enough confidence in them to fund their venture when all others would not. This is not an issue of loyalty; it is an issue of integrity. We are able to dedicate substantial resources to a promising project, but we are not interested in committing those resources to unscrupulous borrowers with no concept of their responsibility to the lender.

This brings up another problem that is one we face day in and day out: So this guy comes in and he has a device that will supply the globe with energy for the next millennium at no cost. He gives a small laboratory exhibition of his concept and we stand in awe of what has been accomplished. He now informs us that he is not going to share the secret of what he has done

with us, the patent office or even his mother. Thanks, but no thanks. We are willing to sign any reasonable non-disclosure agreement that he desires, but we are not going to deal with anyone that feels that his invention is more important than money. We know that our funds exist, but we must be sure that the concept is solid as well. Things that work well in a laboratory have only gone through the initial stage of an investigation. It is a long way from the lab to the production line. Although it is possible that we would take some interest in an intangible concept, we would like to see a prototype of any completely new product.

If it is a new business or an old business re-engineered, we would require an extensive business plan. We are well aware that projections are so much hog wash, but yet by intensively putting something to paper, evaluating the competition, enumerating the expenses, projecting the earnings and at the same time foretelling what the future will bear is an exercise that we believe would be helpful to anyone. Therefore, the energy product that will change the world might escape the intense scrutiny usually given to these types of things, but would still require substantial scientific backup, illustrating the theories involved in its creation.

How does this person get along with others? Not critical if we are not dealing with a neurotic person. Some people like to work alone while others enjoy the company of the cohorts. On the other hand, someone that does not like to be in the company of others or does not respect them is not a good candidate for being the chief executive officer of a thriving business. This trait is not a management strength. People skills are as important as scientific or mechanical skills; the inventor who understands this and will leave operations to a professional is someone whom we respect and are willing to deal with. With our cadre of management contacts, we are quite able to find someone qualified to run the show while our erstwhile prodigy confines himself to the laboratory and continues to turn out a never ending stream of unique products. For practical business purposes, this line must be drawn in steel and may not be crossed. Eventually the day will come when the underwriters will want to meet the creator of all of these wonders; at that time he must be willing to go through all of the proper motions to accomplish the financing, *prima donna's* don't get the job done. Money is not a particularly dear commodity on Wall Street and although it is still revered, it is available in bulk. Nobody wants to lose it but we are smart enough to know that something must be ventured in order to create the opportunity for gain.

There are few ideas of great merit with credible people behind them that cannot command almost unlimited money. Federal Express and Netscape are good examples of ideas that were so startling they found literally no trouble attracting as much capital as was logically required. On the other hand, these concepts were unique and these opportunities are few and far between. If the project passes muster, we set up a series of hurdles and work out a progress payment arrangement with management. They tell us what they are going to accomplish and what it is going to cost. We create hurdles or thresholds. As each hurdle or threshold is passed and the project throws off a profit, we proceed to the next stage of financing.

If the hurdle is missed, we bring together the team that is involved in the project, both from our side and theirs, and determine what went wrong. Was our timing just too optimistic or was management's assessment of the difficulty of clearing the hurdle wrong? If this happens consistently, then we are dealing with a group that has no foundation in reality and the project is undoubtedly doomed.

If it happens more than it should, we are probably dealing with management that needs guidance. Our business is that of investment banking, not that of shepherding companies through mazes.

If with all of our guidance, the rewards appear to be substantially less than estimated and our professionals spend too much time overseeing the project, it may be time to pull the plug. If everything is going like clockwork, schedules are met and the thing looks even better than we thought, we have died and gone to heaven. As long as everyone has their proverbial sleeves rolled up and is giving it their best, we will stick with their project to its fruition one way or the other. Of every ten deals that we finance, only one is a major success. Two will break about even and take an awful lot of our time, and the rest will fail. The winner will pay the bills for the next couple of years. It is a marvelously interesting business to be paid for sitting on the cutting edge of global technology and knowing that each day brings another potentially exciting project. We are always on the fifty-yard line and the home team always has the ball.

We welcome you, your ideas and your hang-ups. Most of them we can work out. This was only meant to describe what we think about when you walk in our door.