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EARLY STAGE INTERVIEW: ZIMMERMAN

Securing Venture Capital Requires Preparation

*Attorney **Edward M. Zimmerman** chairs the technology group at law firm Lowenstein Sandler in Roseland. He has extensive experience representing venture funds and technology-based firms in critical business transactions such as venture capital and private equity, mergers and acquisitions, going-private transactions, management buyouts and spinoff transactions. He spoke with **NJBIZ Staff Writer João-Pierre S. Ruth** about how growing companies should prepare themselves to approach the venture capital community for funding.*

NJBIZ: When does it make sense to seek out venture capitalists to reach the next stage of growth?

Zimmerman: It depends on what kind of company you are looking at. There are some companies that are just built for venture capital. For instance, if you are trying to start a drug discovery company, a semiconductor company or an Internet company, those are [businesses] that are really built to one day take venture capital and, in some cases, to take it from very early on. They are not going to survive without it.

If you're talking about a retail type of business, it's going to be a lot more extraordinary for them at an early stage to say, "I want venture capital" or "It's time to start considering venture capital." This is not to say retail doesn't, it's just a very different sector.

It only makes sense to look for venture capital if venture capital is going to be interested in you. If it is not, you are going to waste a lot of time and money. I think it's shifted a little bit, but the fundamental thing venture capital is looking for is a high-growth business with a differentiated product or service targeting a significant addressable market where it can create some real barriers for its existing or not-yet-born competitors.

NJBIZ: What elements within a company's structure and history make them more attractive to venture capitalists?

Zimmerman: The first question for me is always who's on the management team, how complete is the management team and what have they done? If you have a management team that has obtained third-party financing before venture, private equity or angel, the question is how did that relationship work out?

The venture capital community is a relatively small community and the first phone call that a potential financier is going to make is, "I see here you were backed by Charles River Ventures in your last company. Who can I call at Charles River?" If they call someone at Charles River and you don't get a great reference, that's an issue. You've got to go into your new venture and relationship with institutional financiers with the understanding that you're building a record and it can be a tremendous asset or significant impediment.

If you have entrepreneurs who haven't obtained that kind of financing before, you say, "What have they done?" Is the leadership team a team of people who previously led before or have they only followed before? Have they had responsibility for actually selling a product? Are they working in the same sector? Are they facing the same market? Is this a market where they really understand things? Or do I have a guy who was working in a lab in a pharmaceutical company who's now launching an Internet or social-networking business?

NJBIZ: What do venture capitalists bring to the table beyond the funding for the company?

Zimmerman: There are a couple of things VCs are supposed to bring to the table. One of them is business acumen and experience. Different VCs have very different backgrounds. These are people who are constantly looking at companies like yours and often constantly looking at companies in your sector. They understand the market, they understand the sales cycle for customers in that market often times they will know the senior decision makers at the potential customers. They can make introductions; they can make phone calls and find out what's really going on, what the hang-up is. They know other entrepreneurs who work in those arenas and can often bring in management talent to help round out the team. Often they will have a really good understanding of the technology and can be helpful in refocusing or realigning. Maybe sometimes they don't have this in-depth knowledge of the technology but have a really good understanding of how to motivate a sales force at a time when the company is being run by a technical guy. They really also help in terms of some core business decisions and strategy decisions. They provide significant resources whether it's connecting you with other CEOs in their portfolio to talk about some of the same issues. Just having someone who has, if you've run two companies, you've run two companies, chances are your VC has been on the board of a dozen companies or 20 companies and has seen some of the same issues come up 15 times, 20 times, and helping you through it with that kind of breadth and depth of experience can be extremely powerful.

NJBIZ: Is it important to have a clear exit strategy in place early on in the process?

Zimmerman: It's always important to think about it and map out the kinds of exit strategies you hope to have, but I think we've seen a number of companies with really nice exits where they absolutely did not have the exit strategy at the time the investment was made.

Sometimes you have to take that leap of faith on a technology that's been particularly disruptive that's facing a new market. And you have to figure out whether you think the management team and market opportunity is good enough, and realize you have some uncertainty around how the exit happens.

NJBIZ: What should companies look for in venture capitalists?

Zimmerman: I think you want to look at VCs who are willing to invest in companies at your stage of development, in your sector and in your geography. I was recently out in Silicon Valley talking to a senior partner of a venture fund and he was telling me he does maybe half his investments in San Francisco and the other half are in Silicon Valley. That's someone who doesn't have a whole lot of geographic diversity in his portfolio. If you've got a company in his sector in Texas, Alabama or New Jersey, that's not necessarily someone you're going to have a high degree of likelihood of getting money from.

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