By Nick Wyman and Dane McDonald

**Executive Summary**

Angel investment plays a vital role in any startup ecosystem. With software technology companies costing less and less to start and venture capital firms shifting towards later stage investments, it is more crucial than ever to understand how early stage investors and entrepreneurs can come together to give a company the best chances for success. Despite its importance, however, there is limited understanding and agreement surrounding best practices for an angel investment strategy. On March 22nd, experts in early stage business creation, execution, incubation and investment met for Silicon Flatirons' Mile High Tech Entrepreneurship Conference: Angel Financing – Understanding the Early Outside Money In to discuss the current trends and future trajectory of angel investment.

Despite flawless 72 degree weather outside, the Wittemyer Courtroom was standing room only as a sell-out crowd came to learn the from some of the world's foremost authorities on angel investment. The format consisted of three keynote presentations and two panel discussions, tackling issues ranging from the global economic outlook to specific types of angel behavior. The following highlights some of the conference's key takeaways (a full video capture of the event can be found here).

**State of the Economy Keynote**

*Anthony Chan (Chief Economist for Private Banking at J.P. Morgan)*

Angel investors often directly invest their own money. This is in contrast to venture capitalists who invest money on behalf of a dedicated fund. This difference, notably, makes some angel investors more sensitive than VCs to current economic conditions. In his *State of the Economy* keynote**,** Anthony Chan addressed the macro economic environment. Chan's primary message was that of "cautious optimism" with respect to the global economic outlook. He pointed to the central bank's commitment to support growth and investment by way of low short term interest rates. Chan also highlighted recent trends in nationwide job creation and decreasing unemployment rates as an indication of an improving US economy. Outside the United States, Chan noted that Europe, Latin America and Asia were all showing signs of improvement and positive trends in their respective economies.

**Angel Investor Keynote**

*Jeff Clavier (Founder & Managing Partner at SoftTech VC)*

A conference highlight came from the keynote address by Jeff Clavier, whom Foundry Group's Jason Mendelson introduced as one of the original super angels. Clavier's keynote, "*So you want to be an angel*?" covered the promises and pitfalls of becoming an early stage investor. This post captures some of the key takeaways (his presentation deck can be found here).

Clavier started by encouraging attendees to pay attention to the following basic considerations before jumping into angel investing:

- You must be accredited
- You don't do it to make money
- You don't do it because it's cool
- You do it because supporting innovation and entrepreneurs is a passion

Still qualify? Great, but you're not nearly ready to start investing yet. Clavier recommends first doing your homework: attending conferences, speaking with experienced angels, reading lots of blogs, and getting up to speed on relevant books like Do More Faster.

Clavier recommends developing an investment thesis that will be the basis for your future deal sourcing and screening. Be careful to consider the sectors, types of startups, locations and company profiles that fit your experience and investment objectives. Take note that the vast majority of angel investments are within one day's travel. This is a perfectly reasonable limitation as coordination and communication become more difficult as distance increases.

Clavier suggests that investors next think about allocation. Typically, Clavier suggests creating an account with $100K to $1M to be invested in $10K to $25K slots over the next three years. Remember, this is an account full of money you may never see again so you have to take your time, diversify your risk and, above all, love the process.

The tricky part isn't just finding the best deals, it's getting a seat at the table. In order to attract good deals, you must understand and articulate your value as an investor. Figure out what, beyond capital, you bring to the equation. Hangout with entrepreneurs and build your reputation. Create a personal brand using tools like social media to connect with and support the overall ecosystem. Know what value you can add, and then offer to help and hustle your way into the best deals. Alternatively, if you are fortunate enough to befriend an experienced angel, ask to shadow their investments and learn from them with the aim of cultivating your own unique set of value propositions.

Deal sourcing not a problem? You'll still need to decide where to invest. This is where your carefully crafted investment thesis comes into play. "If you do random shit, it's shit," Clavier warns. Make sure to use your investment thesis as an absolute filter and unless you like the founders, are passionate about the product, and love the deal, don't invest.

Assuming that you still want to be an angel investor, that you've learned everything you can, met with everyone you can, allocated money to invest, weighed deals against your investment thesis, done your due diligence and finally found a deal that makes sense for you, it's then time to close.

Angel rounds will usually (hopefully) have a lead investor who handles the negotiation on terms/price, completes the lion's share of diligence, and, if applicable, joins the board. For your part, it's important that you understand the differences between an equity round and a convertible note. Additionally, be sure the deal terms are standard and won't scare away future investors, who may be crucial to the venture's ultimate success. (Clavier plugged seriesseed.com as a great resource for market term sheets.) The deal should be clean and done with reputable lawyers representing both sides. Clavier cautions that even the best of companies, when encumbered by poorly conceived investment terms, can be doomed to fail.

Congratulations, you're an investor! Now what? First and foremost, remember "it's not your company, it's theirs." You invested in the team and you have to let them steer the ship. Any information and reporting you expect should have been contracted beforehand (Clavier suggests a monthly email from the CEO that outlines progress and identifies the current challenges facing the company). Know where you can add value and let the founders, executives and other investors do the rest. Beyond assisting where appropriate, enjoy the ride. If you get worried, which is perfectly natural at times, compare notes with your lead or co-investors who have more experience dealing with similar situations.

There it is. Time to start from the beginning and repeat as necessary. Be sure to learn from your mistakes and those of the others who have come before you. Define and stick to your investment thesis, develop your value proposition as an investor and be a champion for yourself, your portfolio companies and the ecosystem as a whole. Help when you can and be a supporter from the sidelines when you can't. And don't forget, "If you don't love it, don't do it. Liking isn't enough."

**Panel Discussion 1**

*Jeff Clavier (Founder & Managing Partner at SoftTech VC), David Cohen (Founder and CEOat TechStars), Bret Fund (Assistant Professor, Management & Entrepreneurship, Leeds School of Business at University of Colorado), John Ives (Angel Investor), Erika Trautman (CEO at Flixmaster) Moderator: Jason Mendelson (Managing Director at Foundry Group)*

The panel began with a comment by Jason Mendelson, who asserted that in any discussion of angel financing, venture capital and the startup ecosystem, one cannot forget that entrepreneurs are, and always will be, king. It is therefore important to realize that for a VC and/or angel financing to succeed, a clear understanding of the entrepreneur's perspective must be grasped.

The panel agreed that angels must understand the high risks associated with early stage investments and should pay close attention to the following guidelines throughout their investing activities:

- Don't just invest in ideas, invest in teams
- Don't waste an entrepreneur's time
- Trust your instincts
- Understand investment terms and their implications on future rounds
- Know your role and value add as an investor

From the perspective of an entrepreneur seeking funding, the panel highlighted the following considerations:

- Always check references to learn about an investor and their reputation
- Always seek legal counsel when structuring financing rounds
- Never give away super pro rata rights to an investor

With respect to financing decisions, the panel noted that failure to adhere to the basic rules outlined above is a common and critical mistake made my many first time entrepreneurs and investors. It is crucial that entrepreneurs and angels carefully consider the future implications of ill-conceived terms and poorly chosen co-investors. As institutional investment is often the next step for angel backed companies, the panel noted that it is important to structure early rounds in such a way that VCs will not be dissuaded by cumbersome non-market terms.

**Academic Keynote**

*Jeff Sohl (Professor and Director, Center for Venture Research University of New Hampshire)*

Mr. Sohl brought with him a vast trove of data from the research department at the University of New Hampshire. This summary covers some of the main themes and, for additional information, his presentation deck can be found here).

According to Mr. Sohl's data, venture financing has increased significantly both in dollar amounts invested and total number of deals since the crash in 2008. There is, however, a funding gap forming between angels and VCs. Mr. Sohl suggests that this gap, formed from decreasing capital needs of software/IT startups and a trend of VCs investing in later rounds, is being bridged by angel groups and micro-VCs. He also noted that deceasing startup costs now make it possible for some software developers to go to market without requiring institutional investment. Mr. Sohl highlighted that significant value is often lost by venture backed entrepreneurs when exits are made via public markets. He believes that stocks are purposefully underpriced by venture capitalists to create a synthetic post IPO stock price up-swing aimed at making the VCs look good. A final note on the exit market ecosystem highlighted that the vast majority of liquidation events take the form of a merger and/or acquisition rather than a public equity offering.

**Panel Discussion 2**

*Jana Matthews (CEO at The Jana Matthews Group and Program Director for ANZ Innovyz START in Adelaide, AU), Nancy Pierce (President & Managing Director at KELD LLC), Nicole Skogg (CEO at Spyderlynk), Jeff Sohl (Professor and Director, Center for Venture Research at University of New Hampshire) Moderator: Brad Bernthal (Associate Professor of Law and Silicon Flatirons Entrepreneurship Initiative Director at University of Colorado)*

The second and final panel of the evening began with a discussion on the future of angel investing with regard to the size of financing rounds and future target markets. The panel agreed that the software and IT sectors, given their current rate of innovation and relatively inexpensive startup costs, will continue to garner active angel investment. Mr. Sohl expressed his belief that clean tech's reputation of producing low returns carries with it a possibility of decreasing capital investments, although the future isn't completely clear.

Further conversations centered on the current status of market conditions and valuations. There was consensus around the range of pre-money valuations for software technology companies being from $2-$5 Million, with greater management experience, traction and market opportunity informing decisions to accept higher valuations. Also, in terms of deal sourcing and funding, the panel agreed with Sohl's data, suggesting that about 15% of all companies seeking investment ultimately get funded. With respect to angel investment, the panel noted that in response to the angel paradox there has been a trend towards early angel investors seeking greater investor protections than has historically been the case.

The discussion then shifted focus to the international growth of startup incubators that are modeling themselves after Techstars. Unanimous agreement was expressed on the importance and value that such programs are creating. Australia was discussed in detail because of its forward thinking approach to developing an entrepreneurially friendly ecosystem. Specifically, Mrs. Skogg discussed her experiences launching Innovyze, a new incubator based in Adelaide AU. One important difference she observed between US and Australian investors is that the historic lack of entrepreneurial ventures in AU has resulted in a rather risk averse angel ecosystem. Despite this, systematic differences in Australia's banking system and trends in their overall economy make a compelling case for AU's potential as a startup haven.