

FutureValue

The Magazine of Oklahoma Deals and Dealmakers



Shaping Oklahoma's
Future Economy

Success Stories:
SemGroup, SolArc

Technology Yearbook

By William H. Payne

Angel Investor and
Entrepreneur-in-Residence
at Kauffman Foundation,
Kansas City



Angel Investing:

Enabling Entrepreneurial Growth

Funding high-growth entrepreneurs

Entrepreneurs have been starting new companies at a rate of 500,000 or more annually for many years. Most of these new businesses are sole proprietorships, startup companies in which the founder intends to work for him or herself and has no interest in employing others. These are lifestyle companies, in which the founder plans to substitute income earned by working for others with earnings generated by working for one's self. We suspect that 25 percent or fewer of startup companies are motivated by growth plans that can only be accomplished by employing others. It is important that we better understand these companies in the future because high-growth companies are creating over half of the net new jobs in this country.

Most of these growth entrepreneurs chose to grow their companies slowly; growth that they can sustain with internally generated cash. By seeking no outside capital (except for limited funds available from friends and family), these entrepreneurs can maintain 100 percent ownership of their ventures. Typically, two-thirds of the INC 500 and 80 percent of the Young Entrepreneurs Organization are entrepreneurs who have successfully built growth companies without soliciting outside investment capital.

About ten percent of startup entrepreneurs each year create business plans for companies that will scale rapidly enough to justify seeking outside equity capital. These entrepreneurs look for angel capital, in the range of \$250,000 to \$2,000,000, to finance their companies. Approximately 30,000 to 50,000 companies are funded with a total \$20 billion to \$30 billion annually by angel investors. Most of this investment is made in seed and startup companies or in subsequent funding rounds for these companies. This level of investment is the same order of magnitude as is made annually by venture capitalists (VCs) in this country, but not nearly as well publicized or understood as are VC investments.

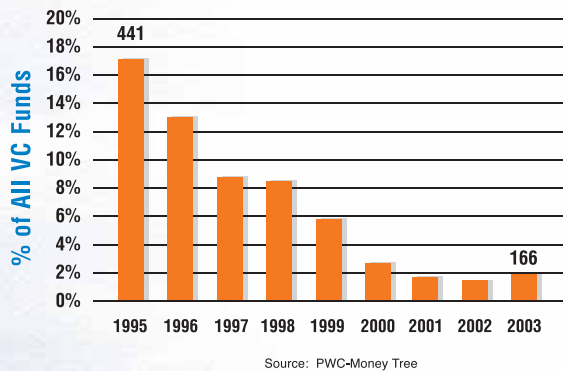
Angel investors focus on starting growth companies. VCs, on the other hand, have abandoned seed and startup companies, in favor of later stage investments. In 1995, about 20 percent of VC investments were directed towards seed/startup companies. Since that year, VC investment in seed/startup companies has steadily decreased through 2003, when less than two percent of VC monies were directed at seed and startup companies. Last year, VCs made 166 investments in seed/startup companies. Why? It is well-documented that VCs now invest much larger sums of money per round than a decade ago and, as can be inferred from the chart, in later-stage companies. With angels investing in as many as 50,000 companies per year and VCs investing in as few as 166 seed/startup companies per year, it is clear that the impact of angel investors on starting growth companies in the U.S. is huge.

Who are these angel investors?

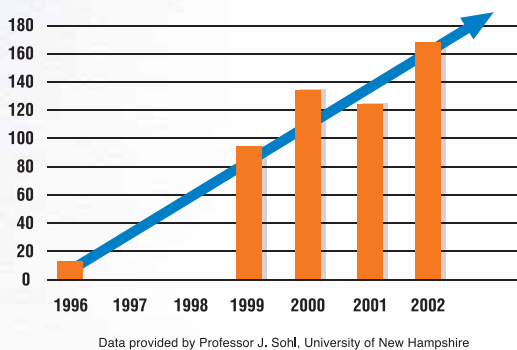
Angels are retired businesspersons and exited entrepreneurs with both the wealth sufficient to invest in startup companies and the skills, experiences and time required to coach and mentor entrepreneurs. Investing in new companies is an avocation for angel investors, who have little interest in full-time employment with or control of these ventures. Angel investors genuinely enjoy working with these entrepreneurs and in sharing their successes. As a group, 200,000 or so angels in this country invest about the same amount of money in new ventures each year as do VCs but invest in 50 to 100 times as many seed and startup companies per years as do VCs. We estimate that about 60 percent of these angel investments are in new companies and the remainder are follow-on rounds in companies funded earlier by these and other angels.

Angels have been actively investing in startup companies for decades — under the radar. Most angels are semi-retired with varied interests and activities. They have not publicized their angel investing activities, preferring instead to fund interesting deals vetted for them by trusted friends, service providers and other angels. Publicizing their angel interests and activities generates a multitude of interest from wannabe entrepreneurs. The angel's dilemma then is

VCs Abandoning Seed/Startup



Growth in Angel Organizations




reading business plans or spending the same time traveling, playing golf or other retirement activities. Angels traditionally have hidden from entrepreneurs to control their deal flow.

The world of angel investing began changing in the mid-90s. Since then, the number of angel organizations has grown from about ten to more than 200 in 2004. Angels have found that joining together with other angels reduces the workload of investing through a sharing the effort required, especially in screening deals and due diligence of candidate investment companies. New and inexperienced angels can plug into robust processes and standardized term sheets, well understood by members in the organization. All angel members bring vertical expertise to the group, which can be applied to studying a variety of deals. Most also find a camaraderie of like-minded, active, experienced businesspersons.

But, there is more. The unintended outcomes of the proliferation of angel groups has been substantial. Angel organizations publicize access to their organizations by entrepreneurs, often through their websites, which enhances deal flow. Angels are now easy to find in many communities. As importantly, because angels working together have become substantially more sophisticated and knowledgeable, most early stage VCs are quite willing to work and invest with members of angel groups.

Oklahoma Angels' Impact

Oklahoma angels have made a significant impact to the development of high growth entrepreneurial ventures in Oklahoma. History has shown that annually there exists an approximate \$25 million gap in risk capital for seed and early stage entrepreneurial ventures in Oklahoma. Traditionally seed and early stage capital must come from local "risk" sources as a catalyst for company growth. Once a company matures it can begin accessing venture capital from both within and outside its region or more traditional sources of capital such as banks. This seed and early stage gap is the most critical form of capital needed in the early development of a company's life cycle.

Since 1999 private Oklahoma angel investors have invested more than \$55 million in early stage advanced technology companies. The activity has changed from several years of angel "group" activity to more individual angel activity during the past two years. Access to angel investors is critical for entrepreneurs to be successful. Access to organized sources of angel capital causes efficiency in the entrepreneurial deal flow and ultimately the investment activity. The formation of the Angel Capital Association, funded in part by the Kauffman Foundation, is evidence of the growing number of organized angel groups in North America. Oklahoma's participation in the organized angel market can have a profound impact on the creation of new companies and ultimately act as a change agent for our state's future economy. 

**"SUCCESS IS NOT AN ACCIDENT,
BUT THE STRICTEST OF JUSTICE."**
— Alexander Smith

We congratulate our clients
on their recent successes in Oklahoma's highly competitive arena of science and technology.

- Ditch Witch**, 2004 Inductee into the Oklahoma Inventors Hall of Fame
- Ekids Technologies, Inc.**, Winner of the OCAST SBIR Phase II Award
- Nanobiomagnetics, Inc.**, Finalist in the Most Promising New Business competition

Their innovation, ingenuity and intelligent entrepreneurial spirit have been justly recognized.

McKinney & Stringer

OKLAHOMA CITY Corporate Tower 101 N. Robinson, Suite 1300, Oklahoma City, OK 73102 Tel (405) 239-6444
TULSA Mid Continent Tower 401 S. Boston, Suite 3100, Tulsa, OK 74103 Tel (918) 582-3176

Why are Angels Networking Nationwide?

Angel investing is a local phenomenon, with most angel investment made within 50 miles of the resident of the investor. For this reason, attempts at networking angels and entrepreneurs in national organizations have not been successful. With the proliferation of angel organizations, we have begun to observe a change. Angel groups in nearby proximity to one another are beginning to work together. Because of the local investing preferences of angel investors, the drivers for angel groups working together was not, at first, obvious. We are now discovering that neighboring angel organizations tend to work together to compare and exchange best practices of operations and to exchange views on trends in investing. Once familiar with one another, trust grows among members and they begin to show interest in each other's deals, especially when a neighboring group has an interesting deal within the specialty of individual angels. Adjacent angel groups often show deals to one another to help round out the funding of large rounds of investment in highly technical deals or those with narrow interest within any single group. In the past five years, some angel organizations in several regions of the country have begun to work with nearby angel groups, sharing resources and expertise and investing in one another's deals.

Trends – the Author's Opinion

Angel investors have made a substantial contribution to success of seed and startup growth companies in the past few decades. But, the best is yet to come. The Angel Capital Association will spawn a host of new angel organizations. New and existing angel organizations and the ACA will radically increase the knowledge of this source of capital for seed/start-up entrepreneurs. We will see the standardization of robust processes used by angel organizations and a substantial increase in the syndication of local deals. VCs have abandoned very early stage entrepreneurs and angels will fill the gap. Entrepreneurs will find it much easier to find investors through the proliferation of highly publicized angel organizations.

The author predicts that through outreach and education, the number of accredited investors who become sophisticated angel investors will increase rapidly in the next few years. As the number of angels and angel organizations increase and it becomes easier for qualified entrepreneurs to show quality deals to angel investors, investment in seed and startup companies will increase. The linking of neighboring angel organizations will increase the quality and quantity of syndications among angels and between angels and early stage VCs. The success of the Angel Capital Association will encourage the



“Entrepreneurs will find it much easier to find investors through the proliferation of highly publicized angel organizations.”

proliferation of angel organizations and neighboring angel organizations to work together. Research by Kauffman and ACA will lead to a better understanding of angel investing by practitioners and the public. It is, indeed, an exciting time to be an angel investor or a high-growth entrepreneur in need of seed or startup capital.

Davis, Tuttle Venture Partners

Providing Equity Capital for
Growth Companies in the Southwest

Barry M. Davis

H. Lee Frost

W. Michael Partain

William M. Wiles

Elmer Wilkening

320 South Boston, Suite 1000 ♦ Tulsa, Oklahoma 74103-3703

(918) 584-7272 ♦ Facsimile (918) 582-3404

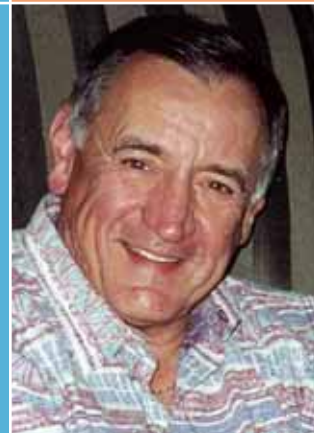
Philip A. Tuttle

Albert G. Laverty

8 Greenway Plaza, Suite 1320 ♦ Houston, Texas 77046

(713) 993-0440 ♦ Facsimile (713) 621-2297

William H. Payne



eXpertise

William Payne Since the early '80s, Payne has made angel investment in 25 early stage companies and served on the board of directors of about a dozen. In addition to his angel investing, since 1995 he has been an entrepreneur-in-residence with the Ewing Marion Kauffman Foundation. Payne serves on the Board of the Vegas Valley Angels and has recently served on the Board of the San Diego Tech Coast Angels. He has been very active in the Chairmen's RoundTable (a San Diego mentoring organization), the San Diego Social Venture Partners (a venture philanthropy) and the Aztec Venture Network (an angel fund).

Angel Capital Association


Early in 2002, the leaders of several large North American angel groups met in Boston to share best practices and discuss trends in early stage investing. These angel leaders solicited assistance from the Kauffman Foundation in Kansas City to provide a focal point for their fledgling activities. This first meeting led to several subsequent meetings and the formation of the Angel Capital Association in late 2003. The Kauffman Foundation has agreed to temporarily host this new organization for a few years until the ACA has demonstrated appropriate viability.

ACA founders have defined the membership as “open to groups of angel investors, located in North America, investing predominately in private equity through a member-directed investment process,” and have authorized their governing board to approve membership applications.

The founders of ACA have developed the following objectives for the organization:


- Support activities for the advancement of angel investing and angel investment groups, including
 - Define angel investing and angel investment organizations
 - Advocate angel investing with entrepreneurs and equity investors
 - Promote the establishment of angel organizations
- Support the common interest of groups engaged in angel investing, including education and public awareness with entrepreneurs and other stakeholders, including
 - Education programs (real and virtual) on working with angel investors
 - Educate public on integral part angel investors and angel organizations play in economic growth and vitality
- Support research on angel investing and angel investors, including
 - Define research objectives and guide structure
 - Develop a methodology for creating, maintaining and disseminating a robust database on angel investments
- Share best practices and other information with and among angel investment groups and angel investors in the furtherance of angel investing, including
 - Development of website for sharing information on public and “members-only” basis
 - National and regional meetings
 - Deal flow sharing

While organizing the four Angel Summits, which led to the founding of ACA and as a result of the national publicity that resulted from announcements of this new organizations, Kauffman has identified 200 angel organizations in North America which are likely candidates for membership in ACA. The organization has a goal of 60 new members by the end this year.




Encouraging Entrepreneurship and Economic Development in Oklahoma


Since 1987, the Oklahoma Venture Forum, with its mission of matching early-stage businesses seeking capital with prospective investors, both public and private, has been a catalyst in the growth of new and existing businesses in Oklahoma. This mission is accomplished through:



Networking – Assisting and matching early-stage businesses with private and institutional investors, and providing access to strategic partners, service providers and experienced business leaders.




Education – Teaching and informing entrepreneurs about the capital-raising and business development processes through speakers, seminars and special programs.



Recognition – Recognizing and honoring those who have taken great risks in starting new businesses in Oklahoma.

The Oklahoma Venture Forum meets on the second Wednesday of each month, except July and August, at 11:45 a.m. at the Beacon Club, located on the 24th floor of the Oklahoma Tower, 210 Park Avenue in downtown Oklahoma City. The fee for non-members and guests is \$25. Membership in the Oklahoma Venture Forum is \$350 annually. Visit our website at www.ovf.org for information on meetings and membership, as well as our Small Business Presenter Application for entrepreneurs interested in making a presentation to the membership. For more information, please contact Mindy Young, Executive Director, at ovf@cox.net or (405) 341-6545.



OKLAHOMA VENTURE FORUM

OVF PRESIDENT
G. Carl Gibson
Ekipis Technologies

OVF PRESIDENT-ELECT
Suzanne Symcox
First Fidelity Bank

OVF SECRETARY
Tom Blalock
Commercial Law Group

OVF TREASURER
Jeff Morton
Adesucia Corporation

OVF BOARD CHAIRMAN
Dale Hageman
Accord Human Resources

OVF PROGRAM CHAIRMAN
John Frick
Chisholm Private Capital Partners

OVF CHAIRMAN
Robert Rader
Capital West Securities

OVF CHAIRMAN
Monte Thacker
Bank of Oklahoma