



Guest Column

## Syndicates mean larger financings, better terms

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by [David Wolf](#)

Historically, angel investors were individuals who had made a lot of money from starting or selling a business and were looking to work with a budding entrepreneur to do it again. The angel investor contributed money and contacts, but often also worked on the business, arm-in-arm with management.

Starting in the 1990s, the angel investment climate underwent two parallel transitions. First, as their numbers grew, angels became less committed participants in a business and more dabblers who would throw \$50,000-\$100,000 into businesses they liked. Second, angel investors began to form groups in order to aggregate capital, take advantage of members' differing and complementary areas of expertise, and have a little fun at monthly meetings.

Angels are now a major force in new business funding, last year investing more than \$23 billion in nearly 50,000 ventures, according to the Center for Venture Research at the University of New Hampshire and the MIT Entrepreneurship Center. This investment total is more than the \$21.9 billion that venture capital firms invested, according to the MoneyTree survey by Pricewaterhouse Coopers, Thomson Venture Economics and the National Venture Capital Association.

Now, a third transition is taking place. Angel groups are not only getting more formalized in their own organizations, they are getting more formalized in how they work together to introduce one another to companies, share due diligence, and ultimately co-invest in deals on jointly negotiated terms.

This new concept of angel syndication, the topic at a recent meeting of the Angel Capital Association, a group of about 100 angel-investing groups in North America, portends some significant changes in the investment climate for entrepreneurs; some encouraging, some less so.

Simpler process

Entrepreneurs are often frustrated by the redundant processes of each angel group they meet. To the extent that angel groups can get together on investment criteria, due diligence and documentation, the entire fund-raising process can be significantly streamlined for the company. Fred Wainwright of Dartmouth's Tuck School of Business -- as well as both Granite State and North Country Angels -- says, "The key element underlying the concept of shared

due diligence among angel groups is trust. This will take some time to build, and the more transactions we do, the sooner we'll be able to reallocate our time more effectively to finding good companies and helping them grow."

#### Larger investments

Angel groups, acting alone, often invest \$250,000 to \$500,000 in young companies, but have been known to make investments in excess of \$1 million. As angel groups grow their internal capacity, as well as co-invest in deals, much larger investments are in the offing. According to James Geshwiler, managing director of Boston-based Common Angels and a founding member of ACA, "Most VCs have left the early-stage rounds, and certainly those below \$5 million. This capital gap is encouraging syndication among angel groups."

#### Follow-on funding

A criticism of angels has been that while they may make an initial investment more quickly and on more favorable terms than VCs, they can't be counted on for additional funding. This, too, is changing. Angels have begun to understand that, like VCs, they should keep capital in reserve for additional rounds and companies are beginning to bypass VCs for second or third rounds. In fact, through the first half of last year slightly more than half of all angel investments went to later-stage deals, according to a UNH study.

#### Tougher terms

On the down side for entrepreneurs, angel investors are also emulating VCs in terms of negotiating tactics. Although many angels will still take a simple convertible note in an early-stage investment, angels have become more aggressive on negotiating valuation and increasingly formal in deal structure. This not only adds time and cost to a transaction, but if the terms are too stringent, they can impair the company's ability to get follow-on financing from third parties.

Is angel syndication a lasting trend? Geshwiler says the trend is national and growing. How big will it get? Ask Geshwiler for an answer and he says, "We're starting to collect data. See me in six months."

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