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Venture Capital Due Diligence: Issues & Processes

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in Finance and Entrepreneurship with Honors

April 2006

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Executive Summary

This paper discusses the areas and methods by which venture capitalists need to concentrate their efforts when assessing the attractiveness of an investment. The information is additionally valuable for entrepreneurs seeking funding to expand their businesses and academics researching the topic.

A series of books, trade journals, articles and interviews were referenced in an effort to present a thorough and unbiased investigation of the topic. The research is significant given that private equity has remained an understudied area in comparison to larger public equity markets. Additionally, the traditionally shorter periods of operating history of private companies add a layer of difficulty to predicting future performance not present in public equities.

First, the characteristics of the high-growth businesses best suited for venture capital funding are discussed. The structures present in the industry and its boom and bust cycle over the past ten years are covered. Finally the fact and fiction in pervasive rumors about venture capital, such as a funding bias towards high-tech startup companies and the general difficulty of getting funded are discussed.

The second section covers the recent trends towards international venture capital investments and lower levels of investment liquidation through initial public offerings, primarily in favor of mergers and acquisitions.

The next section covers the best practices in screening prospective investments. The value of referrals, especially from a VC's trusted inner-circle, is explained. Additionally, screening companies based on desired industries, geographic locations, and growth stages are discussed. Finally, eliminating prospective investments based on business plan quality, the quality of other investors and the reputation of business associates is covered.

Next, the process of assessing the management team, considered the most critical aspect of an investment by many VCs, is discussed. Suggested questions for references are presented along with methods to conduct interviews and assess management team member's integrity and ethics. Making use of trusted sources and psychological tests to determine the completeness of the executive team and their level of preparedness are covered. Finally, recommendations for assessing the commitment and value of board members are discussed briefly.

The section on assessing the business includes research on how to determine the strength and fit of an entrepreneur's product or service with a market need. The market represents the other aspect of due diligence that some VCs argue is more important than the management team. Lastly, methods for assessing the operational performance of the business are covered.

The next section of the paper covers major issues in finalizing an investment. The key legal issues and primary method for valuing a firm are discussed.

Lastly, the summary and conclusion restates the main points of the paper and recommends VCs begin to adapt their due diligence process to accommodate increasing levels of international investments and exits through methods other than US public equity markets.

Table of Contents

Introduction.....	1
Intended Audience	1
Purpose.....	2
Importance of Due Diligence in Venture Capital.....	3
Topics Covered and Methodology	5
Conclusions and Recommendations.....	7
Venture Capital.....	8
Background Information	8
<i>The Select Few</i>	8
<i>Fund Structure</i>	10
<i>Fund Investors</i>	12
<i>The Deal</i>	12
<i>Size of Industry</i>	14
Primary Firms	15
<i>Draper Fisher Jurvetson</i>	15
<i>New Enterprise Associates</i>	16
<i>US Venture Partners</i>	16
<i>Venrock Associates</i>	17
<i>Sequoia Capital</i>	17
<i>Polaris Venture Partners</i>	18
<i>Kleiner Perkins Caufield & Byers</i>	18
Venture Capital Myths	19
<i>Startups Only Need Apply</i>	19
<i>High-Tech Only</i>	20
<i>VC Funding is Impossible</i>	21
<i>Struggling for Control</i>	22
Venture Capital Industry Trends.....	24
Initial Public Offerings Fall Out of Favor.....	24
Venture Capital Globalization.....	26
Initial Screening of Opportunities	28
The Referral Game.....	28
<i>Inner Circle</i>	29
<i>Professional Contacts</i>	29
Strategic Fit.....	30
<i>Industry</i>	30

<i>Location</i>	31
<i>Stage</i>	32
<i>Business Plan Quality</i>	32
<i>Other Investors</i>	33
<i>Reputation of Business Associates</i>	34
Assessing Management	35
Checking References.....	35
Interviews.....	36
Assessing Integrity & Ethics	39
Psychological Tests.....	40
Trusted Sources.....	42
Management Preparedness.....	43
Completeness of Team.....	45
Assessing the Board of Directors	46
Assessing the Board of Advisors	47
Assessing the Business	48
Market Investigation	48
Offering Fit and Future	51
Operational Performance	52
The Deal	57
Legal Issues.....	57
Valuation.....	59
Summary and Conclusions	62
Works Cited and Referenced	69
Appendices	73
Appendix A: Myers Briggs Type Indicator.....	73
Appendix B: Adjective List	74
Appendix C: TL Ventures Due Diligence Checklist.....	75

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Introduction

Intended Audience

In 2000, \$105 billion was invested by US venture capitalists. By 2005 this number had dropped almost 85% to just \$16 billion. (MoneyTree, 2005(B)) A bubbling stock market in combination with poor research led venture capitalists to make many investments that were unwise, eventually leading to plummeting portfolio valuations. This paper focuses on what venture capitalists need to include in their due diligence process, and the methods by which due diligence should be conducted. The specific area covered by this paper is due diligence for expansionary funding, as opposed to startup or turnaround financing, although in some areas the processes are similar. Startup due diligence heavily weights different areas because companies have no operating history; the investment is made almost entirely based on company founders and the market. Alternatively, turnaround financing relies very heavily on the operating history of a company because operations will likely need to be significantly changed.

This paper should be especially interesting to venture capitalists (VCs), however, VCs are not the only party that can benefit. The paper is additionally intended to be a resource for academics seeking to gain an understanding of the venture capital industry, both on a broad scale and how it should function at the firm level. The facts and processes included will serve as a starting point for further research on the intricacies of a properly functioning due diligence process. Finally, this information should be helpful to those seeking venture capital funding. An understanding of what and how venture capitalists approach the

evaluation of a funding opportunity will allow the company's officers to view their position through the eyes of a VC.

Purpose

This research is necessary because of the increased complexity existent in private versus public equity investments. While the Securities and Exchange Commission (SEC) highly regulates companies that trade on public exchanges, their approach to private equity is much more "laissez faire". The SEC does not require the amount of financial disclosure mandated of public firms in the private arena because it is entirely populated by "sophisticated investors." Primarily funded by pension funds, endowments and insurance companies, venture capital firms are allowed to invest in higher risk and therefore higher return companies than in public markets.

The higher risk is partially caused by less operating history than exists in public companies. This increased operating risk requires special consideration when making financial projections critical to earning a sufficient rate of return on an investment. In addition to financial projections, management teams have often spent much less time in their posts. Venture capitalists must take special care to thoroughly evaluate executives individually, their fit with their functional role and fit with the rest of the top management team. Finally, products and markets served by rapidly expanding companies tend to be immature and take unexpected turns without warning. All underlying assumptions are generally not as secure as in public companies, requiring rare foresight into the future of developing markets.

In addition to operational risks, venture capitalists must also combat certain market risks. Typically these risks are the liquidity event, where the VC converts its equity into cash, and improper valuation. The risk of incorrect valuation is increased in private equity markets due to the small number of participants that value the companies. The efficient market hypothesis stands up well in public markets because many analysts valuing the same companies keep information asymmetries to a minimum. Conversely, private companies are known for much larger information asymmetries, creating much larger levels of risk in valuations. Additionally, the smaller size of private markets can create liquidity problems. The gold standard in expansionary funding is to take a company through a successful initial public offering (IPO), however, this does not always happen. If caught in private equity markets the number of market participants is much smaller and required investments are much larger, making it harder for a VC to convert its ownership into a cash gain.

Unlike public equity markets which have become increasingly dependant on approaches such as complex simultaneous equations, private equity markets simply do not have the data to build meaningful models. Much interpretation is left to VCs in evaluating deals. The venture capital process is more art than science.

Importance of Due Diligence in Venture Capital

This paper focuses on due diligence in venture capital not as a discrete step in the funding of a business, but rather as a continuous process determining the attractiveness of a venture investment. As an integral aspect of all stages in

the funding process, due diligence establishes the values and risk levels for the market space and management team. These and other issues investigated in a VC's due diligence then determine the valuation an entrepreneur gets for his or her business.

Robert Simon, director of Alta Partners states that “we construct our own model on revenues because usually they're [entrepreneurs] wildly optimistic.” (Roberts, 2004) The due diligence conducted on a company allows for these financial projections. It also allows for an understanding of the level of risk a company brings with its projected financial rewards. While some startups have large projected revenues, they typically also have high levels of risk, raising the risk premium VCs use when discounting cash flows to determine valuations.

However, even though thorough due diligence is beneficial in determining investment attractiveness, it must have an end. An obsession with developing detailed projections for every last item will lead to “analysis paralysis” and add little to the decision making process. The 80/20 rule generally works quite well. As Russell Siegelman of Kleiner Perkins Cauffield & Byers puts it, “the due diligence will only take you so far, and then you have to use judgment based on experience.” (Roberts, 2004)

A reasonable and well thought out due diligence process allows venture capitalists to invest in only the best and most promising businesses. The process sparks many conversations about the ways customer needs should be met, and the ability of businesses to provide products and services in these ways. The due diligence process improves allocative efficiency through better, more informed

investments while the contact between innovative professionals creates an open dialog prompting even more innovation.

Topics Covered and Methodology

The first section of this research paper will introduce the reader to the venture capital industry. It will cover the types of businesses best suited for venture capital financing as well as alternate funding sources. The section will also cover the structure of the market along with a short history and current trends. Finally, the largest and most prestigious VC firms will be mentioned along with a short discussion of their investment strategies and successful portfolio companies.

The second section of the paper will shed light on some of the more common myths associated with venture capital funding. Comments such as “Those VCs don’t care about us, they just care about their return,” or “It’s impossible to get a venture capitalist on the phone,” are common among disgruntled entrepreneurs but are certainly not always true. This section will discuss the truth in statements such as these, but explain why a well educated entrepreneur or VC can avoid many of these negative feelings.

Next, research on the due diligence process venture capitalists use will be presented. The first sub-section will cover how VCs screen hundreds or even thousands of business plans a year. The train of thought a VC goes through, or at least needs to go through, will be discussed. The process of screening business plans is very subjective for most VCs, however, common themes will be presented.

The following sub-section will discuss what venture capitalists nearly unanimously call the most important aspect of funding a venture – management. In real estate the common phrase is location, location, location, in the venture capital industry it is management, management, management. The section will look into the methods venture capitalists use as well as how to evaluate executive's experience and fit with the rest of the team. It will also cover how venture capitalists assess boards of directors and advisors, both being a significant influence on the management team.

Next, methods for dissecting and evaluating the business opportunity and concept will be covered. This sub-section will cover areas such as assessing the market space and customers, as well as financial projections. It will cover the strategy and difficult intangible aspects like the momentum of the firm. Special consideration will be made to the underlying assumptions of the business. Top-level management teams that pay close attention to their assumptions many believe have a better chance of success than a less careful team with a much stronger initial concept.

Finally, a brief discussion of how VCs assess the legal matters relating to a deal will be presented. This sub-section will not be a full discussion of term sheets, nor will it cover the ensuing legal documents. Rather, it will present the key legal issues VCs worry about and how they gauge their importance on the rest of the deal.

Conclusions and Recommendations

The last section of the paper will present a review of current practices and recommendations on modifications to the due diligence process that will aid in more thorough decision making. Consideration will be given to how current trends will also require continued process adjustments over the next few years.

Venture Capital

Background Information

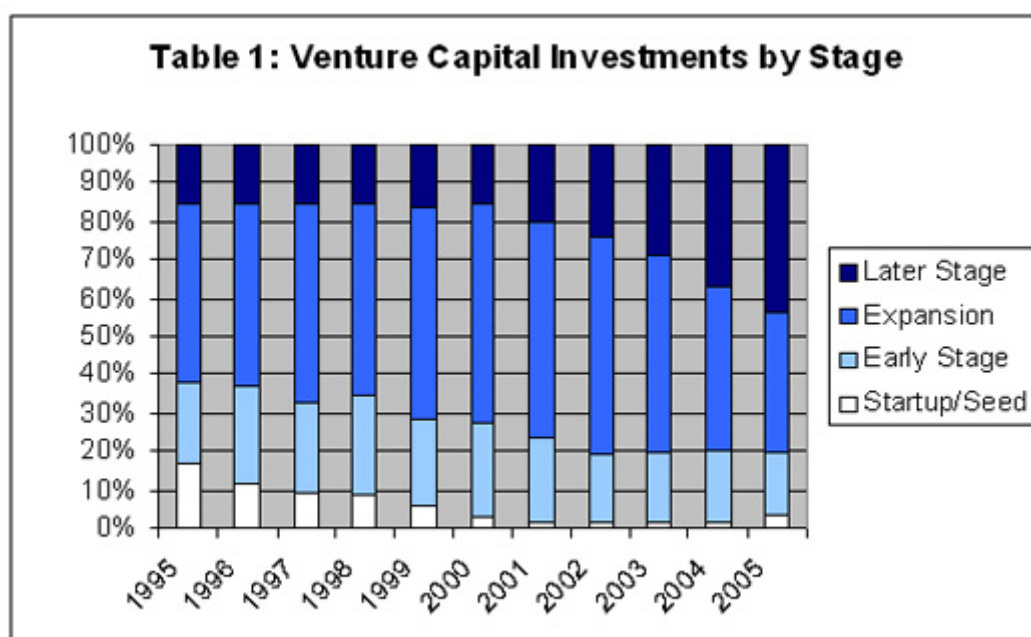
Venture capital firms invest money from a small number of investors into private companies that have the potential for large growth. VCs and their investors benefit when the equity they receive from their investment increases in value. VCs typically work with their portfolio companies for many years ensuring their companies succeed and everyone wins. The National Venture Capital Association (NVCA) describes VC's general activities as:

- Financing new and rapidly growing companies
- Purchasing equity securities
- Assisting in the development of new products or services
- Adding value to the company through active participation
- Taking higher risks with the expectation of higher rewards
- Having a long-term orientation

The Select Few

Venture Capital funding is intended for a select group of businesses. VCs look for companies with, “very high growth prospects and a high probability of exit through sale of the company or initial public offering.” (Vinturella, p. 189, 2004) Typically, venture capitalists are expected to produce a 25-35% annual return for investors. (Zider, 1998) In fact, according to Venture Economics' US Private Equity Performance Index the net return for VC funds in the ten years preceding September 30th, 2005 was 26.5%. (Mendell, 2006(A)) This high return

expectation in combination with the traditionally low success rates among new businesses means that VCs must look for companies that will be worth many times their initial investment when they are harvested. “By one estimate, 6.8 percent of the portfolio companies of venture capital funds account for 50 percent of the returns, whereas 34.5 percent of the portfolio company investments result in partial or total losses.” (Smith, p. 490, 2004) This criterion eliminates a great deal of businesses that may have excellent prospects, but will likely not grow at a fast enough rate.



Source: MoneyTree Report. PricewaterhouseCoopers & National Venture Capital Association. 18 Feb. 2006 <<http://www.pwcmoneytree.com>>

Additionally, most venture capital firms look for some level of current ongoing operations. The general rule is that friends and family or angel investors provide the capital at the very beginning of starting a business and venture capitalists enter into the picture slightly later. However, there are some VCs that concentrate on the seed or startup phase. Table 1 shows VC investments by stage according to data in the MoneyTree Report by PricewaterhouseCoopers and the

National Venture Capital Association. Recently, later stage and expansionary funding have become relatively more popular, representing 80% of the total.

Fund Structure

Venture Capitalists invest the money from a fund which they raise through outside investors. The fund will typically have a term of 10 years but include the possibility of an extension for a year or two if investors stand to gain a significant return by keeping the fund in operation for the extra time period. It is during the first 2-3 years after the fund's creation that the VCs scour the markets for the most promising companies to invest in. After the portfolio companies are selected the venture capitalists spend the next 5-7 years meeting fairly frequently with the companies to ensure that they are growing as expected and to offer help in many areas. The last 2-3 years are spent harvesting the VC's investments through mergers/acquisitions or an initial public offering (IPO).

Due to the heavy amount of work at the beginning of managing a fund, and to a lesser extent at the end, VCs frequently raise capital and start another fund after its current fund's portfolio companies are chosen. This is made simpler because most VCs organize themselves into limited liability partnerships.

Entrepreneurial Finance states, "The venture capital limited partnership has become the dominant form of fund structure for venture capital investing." This is because the LLP makes it easy for the VCs to be represented as the general partners (GP) of the fund, taking on the active management role, while the investors reduce their legal exposure by only supplying the capital and remaining limited partners.

The significant responsibilities VCs take on in the day-to-day operations of the VC fund are substantial and therefore the limited partners pay them well for

these duties. General partners typically receive an annual management fee equal to 2-3% of the fund's total value to cover operations and their salaries. Additionally, the GPs also receive 20-30% of the capital gains on the fund providing a very strong incentive for high

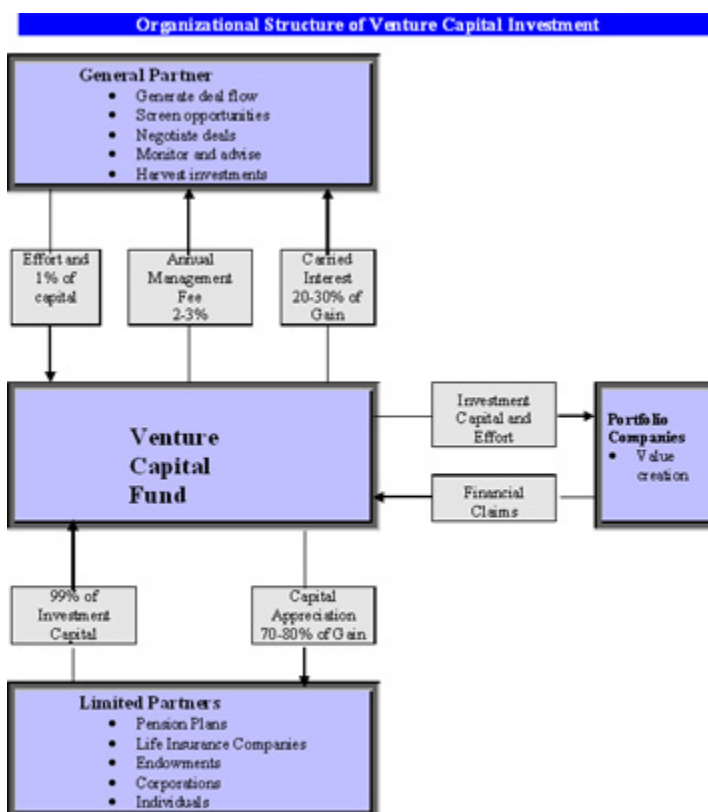


Figure 1

Source: Smith, Janet Kiholm and Richard L. Smith. *Entrepreneurial Finance 2nd Edition*. MA: John Wiley & Sons, 2004.

performance. Figure 1 depicts this relationship graphically. (Smith, 2004) For example, a \$100 million fund managed by five general partners will result in annual disbursements of \$200,000 to each partner. If the fund should appreciate by 30% each year then each partner's average annual compensation will jump to \$2.4 million. This method provides a large up-side potential for GPs, however, they typically only invest a small percentage of the funds capital so the down-side potential is quite small. The result is that VC's reputations carry considerable weight.

Fund Investors

Those that invest in a VC fund must be deemed “sophisticated investors” by the SEC and typically invest at least \$1 million. The SECs requirement and high investment requirement exist because while these funds provide an opportunity for high returns, they also bear much risk. The largest investors in VC funds are insurance companies, endowments and pension funds. (Smith, 2004) Pension funds have recently become very large investors in venture capital. In 1979, about a decade after mutual funds were phased out, pension funds were allowed to invest in venture capital, and within the next decade the industry grew to be ten times the size it had been. (Vinturella, 2004) To a lesser extent, wealthy individuals and corporations also invest. The investment will represent a small portion of the investor’s portfolio so as to increase returns but keep risk at a manageable level.

The Deal

When venture capitalists find a company they want to invest in they will usually invest the money in exchange for preferred stock. The percentage of equity VCs take depends greatly on the equity available, number of other investors and the amount being invested. Generally, VCs invest enough so they or the syndicate of investors get at least one seat on the board of directors.

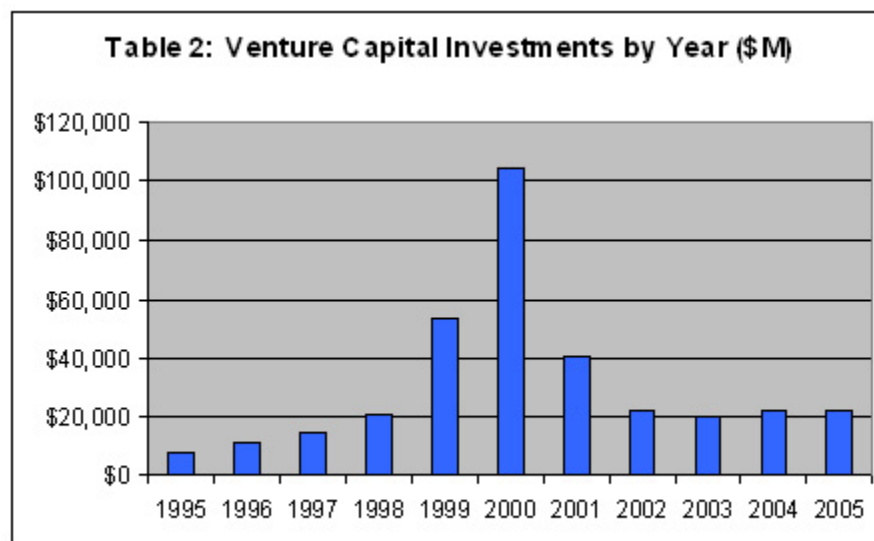
Preferred stock is the equity instrument of choice because it is usually convertible to common stock should the company have an IPO, allowing it limitless upside potential, while limiting the downside potential through the preferred aspect of the stock. If the company should have to be liquidated,

preferred equity holders will receive their full investment amount back before common equity holders receive anything. Additional downside protection usually includes antidilution clauses or ratchets to guard against equity dilution should later rounds of funding take place at lower values. This comes at the cost of common stockholders, management, so care is taken not to dilute these shareholder's equity to the point where they have little motivation to see the company succeed.

Additional provisions commonly included are blocking rights or disproportional voting rights over key decisions such as later rounds of financing, sale of stock or the timing of a merger or IPO. Also with an eye toward the future some VCs require the option to invest additional money at a later date at a predetermined price, or at least to have the right of first refusal should more money need to be raised.

Size of Industry

The size of the VC industry is commonly gauged by its activity in funding new ventures. Table 2 shows the total dollar amount VCs invested in portfolio



Source: MoneyTree Report. PricewaterhouseCoopers & National Venture Capital Association. 18 Feb. 2006
<<http://www.pwcmoneytree.com>>.

companies on a yearly basis from 1995-2005 compiled from NVCA data. The strong stock market of the late 1990's provided an excellent exit strategy for VCs as a large increase in investment activity can be seen. In 2000 264 VC supported IPOs took place, while in 2005 only 56 VC supported IPOs were recorded. (Mendell, 2006(C)) Notable is the lag between the burgeoning stock market in the late 1990s and increased investments in 1999-2001. The lag results from the long-term and complex nature of VC investments. A good leading indicator of the size of the VC industry is fundraising. In 2001 at the tail end of the boom new funding was raised for 110 new VC firms versus just 43 new firms in 2005. The funding of existing firms has also decreased from a follow-on funding of 309 firms in 2001 to 182 firms in 2005. However, 2005 displayed increased

fundraising at a level of \$25 billion, well over the \$17 billion and \$11 billion raised in 2004 and 2003, respectively. (Mendell, 2006(B)) The leading indicators point toward a resurgence in VC funding coming within the near future.

Primary Firms

The following firms represent some of the most active and respected venture capital firms in the industry. In 2005 they each did 80, 73, 71, 59, 49, 49 and 48 deals, respectively, making them the most active investors for that year. These deals represent approximately 5% of the total concluded venture deals in 2005. (MoneyTree, 2005(B))

Draper Fisher Jurvetson

Draper Fisher Jurvetson is a well respected venture capital firm that just celebrated its 20th anniversary having invested in approximately 300 companies. It has invested in companies such as Hotmail, Baidu, Skype, United Online, Overture, Interwoven, 411, Parametric, and Digidesign. DFJ states that, “In general, we look for high gross-margin businesses in large markets, not narrow niches. We are looking for entrepreneurs who want to change the world.” DFJ currently invests in and is looking for additional opportunities in the areas of information technology, nanotechnology and life sciences, and clean energy technologies. More information can be found on their website at:

<http://www.dfj.com/>

New Enterprise Associates

New Enterprise Associates was created in 1978 and has since then invested in over 500 companies with over 150 of them having gone public. It has invested in companies such as Adaptec, Immunex, Juniper Networks, Macromedia, Salesforce.com, Silicon Graphics, WebEx and WebMD. NEA states that “Combining the nation’s foremost early stage company-building experience with an unparalleled capital base, NEA is uniquely qualified to invest in venture opportunities at all points of development – to deliver performance at every stage.” NEA invests over 60% of its capital in seed and start-up stage companies, however, it also looks for later stage companies that may need larger capital infusions but will provide similar levels of growth. The company focuses exclusively on information technology and healthcare ventures. More information can be found on their website at: <http://www.nea.com>

US Venture Partners

Since its beginning in 1981 US Venture Partners has invested in over 350 “early-stage” companies resulting in over 70 IPOs. It has invested in companies such as Ask Jeeves, Callaway Golf, Check Point Software, PetsMart, SanDisk and Sun Microsystems. USVP states that, “Our strategy is to identify creative entrepreneurs who are addressing large market opportunities, invest as early as possible, and add significant value to the enterprise through thoughtful, experienced teamwork.” Its current investment interests are semiconductors, software as a service, networking solutions for storage, wireless data, Internet 2.0,

biomedical devices and new drugs with profound social benefits. More information can be found on their website at: <http://www.usvp.com/>

Venrock Associates

Venrock Associates was started in 1969 as the venture capital arm of the Rockefeller Family and has since invested in over 360 companies. It has funded companies such as Apple Computer, Check Point Software, DoubleClick, Intel, and 3Com in information technology, as well as Athena Neurosciences, Caliper Technologies, Centocor and Genetics Institute in healthcare. “Venrock’s continuing goal is to create long term value by assisting entrepreneurs in building companies from the formative stages and by providing attractive returns to its investors.” Venrock prefers to work with companies at their earliest stages and help shape strategy, build organizations, attract customers and build industry relationships. It is currently looking for investments in information technology and healthcare/life sciences. More information can be found on their website at: <http://www.venrock.com>

Sequoia Capital

Sequoia Capital was founded in 1972 and has been very successful in the technology space. Sequoia has invested in companies such as Google, Yahoo!, WeatherBug, eHarmony, LinkedIn, PayPal, Rackspace and Flextronics. It states that “we like to invest in new, rapidly growing markets where customers have enthusiasm for the company’s products. Most of our investments are aimed at the very early stages of a company and we focus on investments west of the

Rockies.” Sequoia also invests nationally in more mature companies and in Israel. It categorizes its technology investments into components, systems, software and services. More information can be found on their website at: <http://www.sequoiacap.com/>

Polaris Venture Partners

Started in 1996 Polaris Venture Partners is a newer but active fund in the industry with over \$3 billion currently under management and investments in over 75 companies. It has invested in companies such as Akamai, American Superconductor, Classifieds 2000, deCode genetics, Mariner Health Group, Momenta Pharmaceuticals, PSCI and Watermark Software. Polaris’ purpose is to “identify and invest in exceptional entrepreneurs and operating companies with innovative and disruptive ideas, the skills necessary to become market leaders, and a passion for success.” Polaris focuses on early stage investments in information technology and life sciences as well as middle market investments in a wider range of industries. More information can be found on their website at: <http://www.polarisventures.com>

Kleiner Perkins Caufield & Byers

Started in 1972 Kleiner Perkins Caufield & Byers has invested in over 475 companies. It has invested in companies such as Amazon, Sun, Genentech, Intuit, Verisign, Audible, webMethods, WebMD, Travelocity and Netscape. They “work tirelessly on behalf of entrepreneurs and share the benefits of [their] experience to develop new enterprises.” They do this leveraging their large

network, allowing entrepreneurs to learn from one another while building the “great businesses of tomorrow.” Their focus is on new technologies and its applications that will create significant change. More information can be found on their website at: <http://www.kpcb.com>

Venture Capital Myths

Startups Only Need Apply

Many people unfamiliar with venture capital hear the stories of a new company with a great concept or product getting VC funding to expand their business and assume this is the only purpose of venture capital. In fact, in 2005 just over 3% of the money VCs invested were for seed funding or startups. The remaining 97% of the funding was for early stage, expansion stage or later stage companies. (Lefteroff, 2006) These are generally considered to be companies that have been in business for at least 18 months and have a product or service that is being sold to customers.

However, some venture capital firms do specialize in startup or seed stage funding. Almost all VCs have a business stage preference along with industry and geographic location requirements. This information is typically clearly stated on the VC's website. However, many entrepreneurs send out massive emails or mailings of their business plan and are frustrated with a minimal response. Targeted emails/mailings and especially personal introductions can make a huge difference. The trick is in finding VCs and companies whose strengths and weaknesses compliment each other to allow the growth of a successful company

and investment. Selecting a VC that specializes in the appropriate business stage is one of these key factors.

High-Tech Only

Another common myth is that venture capitalists only invest in leading edge high-tech companies. While information technology companies comprised just over half of VC investments in 2005, 48% of funds were distributed to other industries. (Lefteroff, 2006)

Information Technology Related – 52%

- Software – 22%
- Telecommunications – 10%
- Semiconductors – 8%
- Networking & Equipment – 6%
- IT Services – 4%
- Computers & Peripherals – 2%

Other Industries – 48%

- Biotechnology – 18%
- Medical Devices & Equipment – 10%
- Media & Entertainment – 4%
- Industrial/Energy – 3%
- Financial Services – 3%
- Business Products & Services – 2%
- Healthcare Services – 2%
- Electronics/Instrumentation – 2%
- Consumer Products & Services – 2%
- Retailing/Distribution – 1%
- Undisclosed/Other - 1%

Silicon Valley, the mecca for high-tech companies, received an astounding \$7.6 billion in 2005, but this amount was just 35% of the total invested nationally.

(Lefteroff, 2006) Venture capitalists do not focus on industries because everyone else is talking about that particular market space, in fact this introduces additional competition. What VCs are incredibly interested in are large expanding markets that are not yet fully developed. These types of markets hold huge profit potential because of their sheer size and tend to be more forgiving of mistakes due to their high growth rates. The IT market has shown these characteristics for the last decade, and as such has been very popular. However, other markets such as

biotechnology and medical devices & equipment have also been very popular in recent years.

VC Funding is Impossible

Frequently, disgruntled entrepreneurs gripe about how impossible it is to get a VC to fund a business. There is some truth to this statement considering “they turn down about 99 percent of the business plans that come to them.” (Cardis, p. 11, 2001) It is understandable that many entrepreneurs are frustrated working to get funding from VCs. Hundreds or even thousands of business plans are reviewed each year and only about a dozen businesses rise to the top. Frederick Beste of Mid-Atlantic Venture Funds notes that his small fund invests in 4-6 of the 1,200 opportunities they see a year. (Truth, 1996)

However, a large portion of the plans VCs receive are immediately discarded because they simply do not meet the funds’ investment objectives. John Cococcia of FA Technology Ventures estimates that he discards about half of the business plans he receives because they are in an industry his firm does not cover, are addressed to a large list of unrelated VCs, spell his name incorrectly or have other signs that an entrepreneur is careless and has not done his or her homework. (Cococcia, 2006) Gordon Baty of Zero Stage Capital adds “of every 100 plans that we get, 90 are completely irrelevant because they do not match our investment criteria regarding the industry, stage of development, geographic location, or the amount of capital we typically invest.” (Institutional, 2005)

Getting a referral from a source trusted by both the entrepreneur and the VC is a good way to get a business plan to the top of the VC’s pile. After this a

clear, concise and professional business plan will hold the VC's interest as long as it covers an industry, location and business stage the firm invests in. These two simple steps are often enough to get a phone interview to describe in more detail the opportunity and business concept.

The primary responsibility of a venture capitalist is to invest the limited partners' capital to earn a significant return. It is in the VC's interest to fund growing businesses with the right qualities. In 2005 alone \$21.7 billion was invested in 2,939 deals. (Lefteroff, 2006) These thousands of companies will benefit from venture capital funding and assistance because they met the requirements of their financiers.

Struggling for Control

Some entrepreneurs claim that venture capitalists aim to take over running the companies that they invest in. Most entrepreneurs worry that they will lose control of their "baby" once they have given up a significant portion of the company's equity. While VCs do demand some weight in making decisions and the right to block certain decisions, they simply do not have the time to take over control of their portfolio companies. In Bob Zider's 1998 article *How Venture Capital Works* he dissects how most VCs spend their time. He concludes that 40% of their time is spent actually directing, monitoring and consulting with portfolio companies, of which each partner has an average of 10. This would equate to just two hours per week working individually with each company, far too little time to run a company. Even now that the industry has slowed down some, four hours a week is not enough time to wage a control battle.

Additionally, if a company is doing very well the VC will likely want to stay out of the way so as not to disrupt the momentum. The goals of a VC and company management are very closely aligned through their shared equity stake in the business. However, if a portfolio company starts to struggle the VC will likely spend extra time working with the management to set it back on the proper path to growth. This area is where power struggles can emerge. As a large shareholder, VCs have the power to influence the direction of the company and replace executives if necessary. However, this difficult position typically only arises if the company is teetering between success and failure.

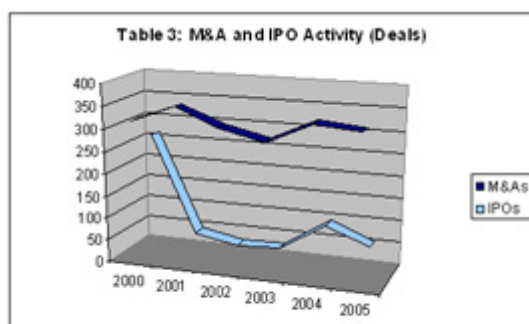
In these cases VCs can be leveraged extensively. Venture capitalists have large networks of professionals with expertise valuable to the management team of a portfolio company. Introductions to these contacts can lead to new customers or strategic partnerships. In addition to help from professionals, the VC can also serve as a great mentor. Having likely worked in the industry, and possibly run small businesses, VCs can provide invaluable information from their experiences. The best help an entrepreneur can get is often from somebody who has been there and done something similar before. VC's help as a member of the board of directors, or simply as an advisor can benefit a management team much more than it harms them. The critical aspect is willingness on the part of a portfolio company's leaders to leverage a VC's resources so the company ends up with much more than cash.

Venture Capital Industry Trends

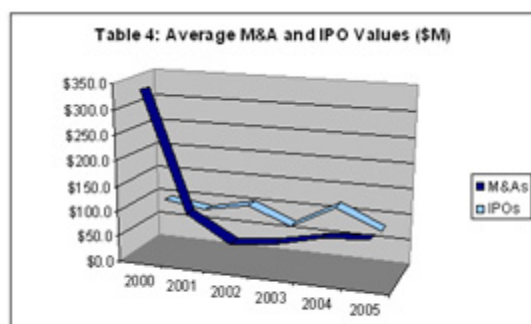
Initial Public Offerings Fall Out of Favor

The gold standard for venture capitalists and frequently for entrepreneurs has long been to take their company through a successful initial public offering. A listing on the Nasdaq stock exchange was not just a symbol that a company had “made it to the big time,” but also a welcome liquidity event for investors. Particularly during the bullish years leading up to 2000, IPOs displayed runaway performance.

Five full years later IPOs have not reclaimed their dominance as the preferred liquidity event for venture capitalists. In 2000 317 venture backed mergers and acquisitions were reported along with 264 IPOs. In 2005 M&As increased to 330, while IPOs were down dramatically to 56. M&A liquidity events have far surpassed IPOs every year since 2000. (Mendell, 2006(C))



Source: Mendell, Emily, and Joshua Radler. Venture-Backed IPO Activity Weak in Q4 and Full Year. NVCA & Venture Economics. New York: NVCA & Venture Economics, 2006. 14 Mar. 2006. <<http://www.nvca.org/pdf/EcipoipolreleaseQ42005.pdf>>.



Source: Mendell, Emily, and Joshua Radler. Venture-Backed IPO Activity Weak in Q4 and Full Year. NVCA & Venture Economics. New York: NVCA & Venture Economics, 2006. 14 Mar. 2006. <<http://www.nvca.org/pdf/EcipoipolreleaseQ42005.pdf>>.

Tables 3 and 4 point out that while the total value of IPO and M&A deals (number of deals multiplied by average value) have decreased, IPOs now represent a much smaller percentage of liquidity events. Mark Heesen, President of the NVCA commented that,

Factors including Sarbanes Oxley compliance, required revenue run rates, and the demand for larger deals in the public markets have slowed the IPO process, particularly for smaller cap companies in registration. Fortunately for many of these venture-backed companies, an acquisition remains a compelling exit strategy, as valuations have been very favorable here. (Venture, 2005)

Richard Peterson, a strategist at Thomson Financial that tracks IPOs, notes that more mature companies have been the ones running IPOs. The same *USA Today* article also points out that the median age of companies going public in 2004 was eight years, down from ten years in 2003 but significantly higher than the four year median in 1999. The historical median is seven years. Additionally, in 2004 20% of IPOs were technology related, down from the long term average of 35%. (Krantz, 2005) This again displays technologically heavy venture capitalists move away from IPOs towards other liquidation strategies.

Steven Fletcher, managing director at investment bank Perseus Group, suspects that the US IPO market will be hard for companies with market caps of less than \$500 million. However, he notes that “We’re seeing very strong activity in the M&A market.” (Borrell, 2006) Jerry Borrell, senior editor at the Venture Capital Journal, notes that “With a growing number of venture firms becoming international and the high cost of going public on U.S. exchanges due to Sarbanes-Oxley, those numbers [of US companies listing abroad] will probably increase.” (Borrell, 2006) Mark Heesen comments that while acquisitions are a good option they, “cannot alone support the level of cash disbursements expected by limited partners.” As a result he expects many companies will try going public on foreign exchanges and soliciting bids from private equity firms. Heesen also noted in the NVCA 2005 fundraising report that the excess liquidity in the buyout

fund market may fuel another exit opportunity for venture capitalists to gain liquidity. (Mendell, 2006(B))

Venture Capital Globalization

Venture capital investing has long been a domestic activity. Then again, so have public listings. Over the last few years new major public stock exchanges have sprung up around the world and the practice of dual listing on multiple global exchanges has grown in popularity. Private equity has lagged behind public equity markets in its move towards globalization, but that is starting to change.

The 2005 Global Venture Capital Survey, the first of its kind to be put on by Deloitte & Touche and the NVCA, received responses from 545 general partners in the Americas, Europe, the Middle East and Asia Pacific. Eighteen percent of respondents stated they are planning to move their investment focus out of the US, while 32% say they will increase their international focus while maintaining their investment levels in the US. (Jensen, 2005) This survey in itself serves as definitive proof that VCs are starting to think globally, but some are doing much more than just thinking.

3i, DCM-Doll Capital Management, Greylock Partners, New Enterprise Associates and Sierra Ventures all recently invested in China-based funds as limited partners. Additionally, Accel Partners partnered with experienced China investor IDG Ventures to create and partially fund a new China-focused fund. More boldly, Sequoia Capital started putting together a team in China and raising money while Ollie Curme is breaking away from Battery Ventures to start fund-

raising for his China-focused firm. (Loizos, 2006) On the other hand, also mentioned in the same *Venture Capital Journal* article is that some LPs have lost interest in the over hyped Chinese market, preferring the more “settled” Japanese market. However, with the emergence of an expanding middle class and economies growing much faster than the US, investments are sure to start taking place at increased levels abroad over the coming years. Mark Heesen suggests VCs will take an informed approach to risk taking as they climb up the learning curves into investments in energy, bioinformatics, mobile computing as well as into new locations such as China and India. (Heesen, 2006)

In speaking about emerging market opportunities Josh Lerner of the Harvard Business School said, “People figured if they can invest in India and China, perhaps they should cast the net broader.” He provided Draper Fisher Jurvetson’s success with funding Luxembourg-based Skype as an example. He also thinks that the Eastern European area has similarities with India in that there are large numbers of young English speaking workers that are proficient in math and science. He cites low labor costs and pro business leaders like Yushchenko as highly positive factors. Tim Draper states that “The Ukraine will be like Israel,” one of the US’ largest global VC partners. (Sheahan, 2006)

It seems clear that as GPs seek to find the kind of returns their LPs want, global strategies will be necessary. People are clearly starting to take notice as membership in the Emerging Markets Private Equity Association (EMPEA) tripled in 2005. (Sheahan, 2006) When the brilliant minds of Mark Heesen, Josh Lerner and Tim Draper all agree, it is hard to argue.

Initial Screening of Opportunities

As stated previously, VCs eliminate about 99 percent of the business plans they receive. (Cardis, 2001) The earlier these unattractive plans can be eliminated the more time VCs have to spend reviewing other possibilities and working with current portfolio companies. John Cococcia stated that he screens out approximately half of his plans within a few minutes of receiving them. (Cococcia, 2006) This screening process which typically eliminates at least 50 percent of submitted business plans is important to understand for entrepreneurs and venture capitalists alike.

The Referral Game

Referrals are used very frequently by venture capitalists. Some VCs give plans referred to them a slight preference while others are unlikely to even look at a business plan unless someone they trust puts it on their desk. Either way, “referrals have become more of an issue because venture capital funds are receiving more deals than they can keep up with, and they need some mechanism to establish a pecking order to sort through the reams of paper that come into their offices.” (Hill, 2001) While a referral may get a business plan to the top of a pile, its qualifications must take it from there on out. Also, a connection may help, though, the strength of the connections between the entrepreneur and the VC are important, some sources are more trusted than others.

Inner Circle

Venture capitalists' closest business associates are clearly the gold standard for a referral. Members of the firm's board of advisors, limited partners, executives of portfolio companies or associates at the firm all have something to lose should the deal head south. Steve Harris of TDH notes "[The sponsor doesn't] want to be embarrassed by referring something that's silly..." because the referrer is also putting his or her reputation on the line by making the introduction. (Cardis, p. 158, 2001) Referrals by a VC's most trusted sources can carry a lot of weight because they give a plan instant credibility in a sea of unknown sources.

Professional Contacts

The next best thing to a referral from someone in a VC's trusted inner circle is through a professional contact.

These contacts can be much easier to make and still provide a significant leg up in differentiating one business plan from the pack. It is likely that a VC will keep a wide

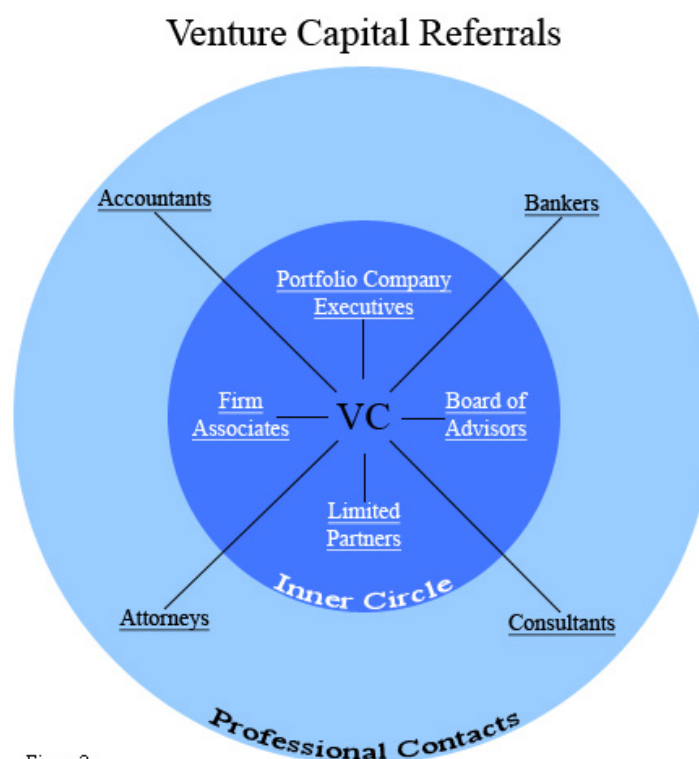


Figure 2

network of attorneys, accountants, bankers, consultants and other business community members partially to provide as a web of referrers. These professionals understand what it takes to run a successful business, and while they may not have detailed industry knowledge they can often be counted on to do at least a smell test.

Strategic Fit

When a business plan or summary eventually works its way into the hands of a VC the next hurdle it must pass is matching the type of profile the VC is looking to invest in. Having an investment niche is very common among venture capitalists and most post this information plainly on their website. The area of specialization allows the VC firm to build up knowledge and contacts in a particular area to make better informed investments and to better support their portfolio companies. (Gladstone, p. 301, 2004) Additionally, it screens out a large portion of business plans which the firm will not be interested in. “With this one preliminary question, they can eliminate many proposals in a matter of seconds: Does the business profile match the profile of the fund?” (Cardis, p. 151, 2001) This profile is primarily built on an industry, region and stage.

Industry

The most commonly used investment criterion by venture capitalists is that the company must be in an industry in which the firm is investing. In the fourth quarter of 2005 almost \$3.7 billion was invested in the software, biotechnology, medical devices and equipment, telecommunications and

semiconductors industries, representing 72% of the total invested. (MoneyTree, 2005(B)) Concentrating on a particular industry or industries allow VCs to gain a thorough understanding of the market forces and trends in that specific area. This specialization also benefits funded companies through an extensive network most VCs have generated through time and experience in the particular market space. All of the venture capital profiles listed at the beginning of this paper clearly stated the industries in which they would consider investing. Plans submitted that focus on different industries are likely to be thrown out because entrepreneurs have obviously not done their homework, notes John Cococcia of FA Technology Ventures. (Cococcia, 2006)

Location

Venture capitalists also tend to invest more frequently in companies based closer to their headquarters. With about 35% of fourth quarter 2005 investments going to Silicon Valley and 13-14% going to New England, these two areas are very popular, as they make up almost half of the country's venture investments. (MoneyTree, 2005(B)) Locating themselves in Silicon Valley where most of the world's technical innovations are hatched, or close to some of the world's top schools in New England, place VCs exactly where the action is happening. This proximity to large numbers of promising ventures makes local networking and continuing support of portfolio companies much easier. VCs typically prefer local investments because they can rely on their strong networks in the area for information gathering as well as the ease of travel to the portfolio companies' offices. This criterion is typically a preference, where industry is a requirement.

Stage

The stage of the company is typically the last part of any VC's profile. Some VCs focus on earlier stage funding because their experience and networks lead best into this area, while others concentrate on later stage funding for larger expanding or troubled companies. In the fourth quarter of 2005 less than 1% went to seed funding, 17% went to startup funding, 1.5% went to early stage funding, 36% went to expansionary funding and 45% went to late stage funding. (MoneyTree, 2005(B)) This aspect is typically the last of the three criteria VCs use to define their general investment strategy. A good fit within all three categories is usually necessary to move a business plan through the screening round to be investigated more fully.

Business Plan Quality

Without having met the entrepreneurs, venture capitalists use the look and feel of the business plan to gauge the competence of the entrepreneur and his or her plan. "They like plans that are clear, concise, thorough, and professional in presentation; practical, realistic, and credible in content; and that adequately explain all assumptions on which claims are made." (Camp, p. 6, 2002) C. Gordon Bell formerly of Digital Equipment Corporation, and now an advisor at U.S. Venture Partners states that "the ability of a CEO and his or her top-level group to write a good business plan is the first test of their ability to function as a team and to run their proposed company successfully." (Camp, p. 6, 2002) A sloppily written or presented executive summary is a good indication of poor assumptions and backup data on which the business plan is based. Venture

capitalists look for potential and professionalism in their portfolio companies, and therefore expect the same from their applicants' business plans.

Grammatical errors or misspellings show an inability to work with detail. Poor data or assumptions point towards poor decision making abilities, which are crucial to running a growing business. Verbosity and poor organization of a business plan show that executives may have a difficult time communicating a vision and prioritized goals for employees to work towards. Finally, a plan without summary charts or graphics may display an inability to understand the bottom line.

Other Investors

If a company has already moved through at least one round of funding the reputation of current VCs serve as a proxy for the quality of the business. Typically, the best VCs will choose to invest in the most promising businesses, and lower quality businesses will only be able to get funding from less respected VCs. Continued participation on the part of existing investors is also telling about the prospects of a business. Current investors will want to expand their holdings if they feel their equity will gain value, but will want to cut their losses if they expect the business to fail. This method is similar to the popular public equity tactic of buying or selling shares based on executives actions, betting that they are predictive of short run performance.

Similar to those that have already invested in the company, consideration of VCs currently thinking of investing is also used to gauge the business plan; highly respected VCs considering an investment is typically a good sign. On the

contrary, a deal having been rejected by multiple VCs likely suggests fundamental problems with the business. Also, a deal being shopped around to large numbers of VCs suggests the entrepreneur does not understand how the venture capital industry works or is too lazy to be bothered carefully choosing an investment partner. Multiple VCs can also decrease an individual VC's bargaining power when closing the deal.

Reputation of Business Associates

Typically high quality accounting and law firms will only represent high quality clients, so a business that is impressively represented is likely a good sign. Additionally, strategic partnerships with industry leading companies display a signal of confidence from these other successful businesses. Finally, signing large customers can all but guarantee success for some firms. However, John Cococcia points out that just because a big company is a customer does not mean the business has a great product, the corporate giant may just be trying all current market offerings for evaluation. (Cococcia, 2006)

Assessing Management

In discussing the risks venture capitalists face when investing in portfolio companies, Graham Anderson of EuclidSR Partners states that “The biggest risk investors assume...is management risk.” (Inside, p. 13, 2003) When assessing any investment, whether public or private, investors agree that the competence, motivation and fit of a company’s top management is of the utmost importance. This section discusses the ways in which management needs to be thoroughly assessed. These areas include checking references, interviews, ethics and integrity evaluation methods, psychological tests, evaluating through trusted sources, evaluating experience, management preparedness and completeness of the top management team. Also included are methods to assess the quality of the company’s board of directors and board of advisors.

Checking References

The first method of gaining this information is worthy of forethought. Reference checks are a valuable and logical place to start in gaining a better understanding of managers. However, the obvious weakness to checking references resides in the fact that they are chosen because they will be positive in nature. James Bergman of DSV Partners explains, “In a reference check, most people do not want to say anything bad about a person. However, if you give them the opportunity, they are often willing to name someone who might have something unfavorable to say.” (Camp, p. 27, 2002) This time consuming process of branching out is absolutely necessary to get a clear view of the

manager. The reference checks should not solely be limited to past co-workers however.

To build a three dimensional model of an officer in a possible investment candidate, bosses, lower-level employees, customers, suppliers and anyone else the manager regularly interacted with such as accountants, bankers or lawyers need to be contacted. The conversations do not need to be exhaustive, but they should be thorough enough to uncover and drill down into any potential weaknesses. The following is a subset of a list of questions that Arthur Lipper, formerly of *Venture* magazine recommends to start: (Camp, p. 28, 2002)

1. When did you first meet _____ and under what circumstances?
2. How does he handle failure or situations that do not develop as he planned or would have liked?
3. When he fails to succeed, how long does it take him to bounce back with alternative means to accomplish the same goal or with another new idea? Does he get “frozen” into one approach?
4. Can you think of anyone who might question his integrity?
5. Do you know any people who dislike or have disagreements with _____?
6. What are the best things or strongest points you can tell me about from the perspective of a future partner or investor?
7. Have you been able to observe how _____ works with other people? Does he work better with peers or those he is supervising? How does he relate to superiors?
8. Whom do you know who is closest to _____ or in a very good position to provide insights about him?
9. What do you think _____ will be doing 10 years from now? What do you think he really wants to be doing 10 years from now?
10. If you had the opportunity to invest, alone or with others, in a business to be managed and possibly controlled by _____, would you invest?

Interviews

Additionally, direct interviews and observation of key management personnel is critical. This process should be completed in the manager’s setting if

possible. Subtle cues can be very telling of the way the person runs his or her organization. A full discussion of the person's past leading up to his or her current position shows not only relevant work experience, but also triumphs or failures in the face of adversity and the manager's response. This is a good time to discuss the moves the manager has made throughout his or her career. What were the motivations behind seeking out promotions or why did he or she feel it was time to switch positions? Asking why multiple times for each significant change can reveal the officer's true personality and motivations.

The personal interview also serves as the most appropriate time to dig into the manager's relevant experience in the industry the venture is in. He or she should understand at the most detailed levels the market and customers the business serves. Past experience serving the industry or one which is closely related can be of great benefit to an ongoing business. Beyond just knowledge of the market and customers, past experience often brings with it invaluable connections. A well networked manager can provide much more value than one with solely theoretical knowledge of an industry. While functional knowledge is not quite as important as an in-depth understanding of the industry dynamics, it removes one additional uncertainty from the risk matrix. An entrepreneurial software engineer that designed a program may not be the best choice to lead the commercialization of the product.

The behavioral interview technique is by far the most popular method currently used by large corporations, and increasingly by smaller companies also. It relies on the premise that past behavior or performance is the best predictor of

future behavior or performance. Instead of asking the interviewee what they would do in a particular situation, so the interviewee can tell the interviewer exactly what they want to hear, the behavior-based technique focuses on past occurrences.

Behavioral interview questions typically start with “Tell me about a time when...” or “Describe a situation where...” The questions force an interviewee to think of a relevant event and describe what happened. A typical response will use the SAR (situation, action, result) technique. Within the answer the interviewer must be looking for any incongruities in the story. He or she needs to take careful note of the characteristics of the interviewee that become apparent in his or her answers to the questions. Problem solving skills, teamwork and pro-activeness are very easy to judge from the person’s answer. (Sample, 2006)

However, rattling through a set of interview questions and taking note of the interviewee’s characteristics is not enough. Many behavioral interviewing questions are after the same information and can be prepared in advance. Almost every interviewer asks “Tell me about a time when you were confronted with a problem, and how you solved it,” or “Describe a situation in which you had to enact change.” These are very good questions to ask, but serve only as a starting point. The interviewer must understand clearly what he or she is looking to find out in the interview, and then concentrate follow-up questions on those areas. For example, if an interviewer wanted to determine how autocratic or democratic an executive was, he or she might follow up the questions about enacting change with how the manager dealt with subordinates that disagreed with the change.

Justin Menkes of the Executive Intelligence Group suggests adding a case study to the behavioral interview. He notes that “Several companies, including McKinsey, Microsoft and GE, have taken this approach for years.” The case study allows the interviewer to evaluate the executive’s management skills such as identifying key issues in a problem or evaluating the quality of data. Watching how the executive solves the problem displays how the executive will likely behave on the job. Menkes believes that these cases, when used with other tools such as IQ tests and behavioral interview questions, provide the best method for evaluating executives. (Pomeroy, 2006)

Assessing Integrity & Ethics

The integrity and ethics of the executives at the company a VC is considering funding are crucial factors to examine. The public scandals of the last few years have rocked the public equity markets leading to Sarbanes-Oxley legislation and a general feeling of mistrust among companies and their investors. However knowledgeable private equity investors are, it is unlikely there are not similar issues of corruption at play.

In a recent issue of HRMagazine employers, or in this case investors, are urged to add a couple of behavior based integrity questions to an interview. Asking an executive if he or she has ever had to bend the rules or selectively choose data for reporting purposes while striving to reach a goal is a good starting question. William Byham, CEO of an HR training and consulting firm, recommends taking an executive out to dinner to watch how the person behaves in a social setting. He suggests asking the executive how much of a tip should be

left and then asking why that amount to discern how the person makes decisions and views or interprets the world in a general sense. (Andrews, 2005)

Background checks can also be very helpful in assessing a manager's ethics. Simply verifying the contents of the management team's résumés is important, as was demonstrated by the recent resignation of RadioShack CEO David Edmondson over incorrect academic information stated on his résumé. (RadioShack, 2006) A criminal record check and drug screening can also be beneficial and are standard practice hiring policies at many companies. After all, funding a venture carries with it the same risks as hiring a new team of managers.

However, those in the human resources profession are very careful and knowledgeable about the legality of using these methods in the workplace. For instance, a criminal record in itself is not always grounds to keep from hiring or investing in an executive. However, the forced resignation of former Boeing CEO Harry Stonecipher for his affair with another company executive did not end in the courts seemingly because he violated the company's code of conduct. (Isidore, 2005) Evaluating employees is a complex task in which legal implications must be considered. (Babcock, 2006)

Psychological Tests

There are hundreds of psychological tests that can be used in assessing personality traits. The most popular of which is the Myers Briggs Type Indicator (MBPTI). While this personality profile is not designed to determine if a person is a good leader for their company, or even a leader at all, it does determine the

person's most comfortable characteristics. It suggests what behaviors a person would engage in without any outside influences. (Gladwell, 2005)

While the information from the profile does not give any definite answers, it can be helpful in assessing the appropriateness of executives for their role in the company they are running. On the extroversion-introversion, sensing-intuition, thinking-feeling, judging-perceiving scales one might look for a CTO that falls into the INTP category. On the other hand, the CEO expanding a service business to a national level may be more successful if he or she falls into the ENFJ category. The value in this assessment is helping to determine if an executive's default personality traits are the most beneficial to the company's current stage, near future plans and functional role within the business. [See Appendix A for a description of all 16 personality profiles.]

Another straightforward psychological test is one of adjective association. After the person doing the due diligence on the venture gets to know management team members well he or she can rate the appropriateness of a list of adjectives (Appendix B) in describing the executive. The executive should also do a self-assessment at the same time to gauge differences in the way the two people see the executive. (Mani, 1995)

This simple activity is beneficial in two ways. First, it forces the clarification of the executive's personality traits. Similar to the MBTI it allows an executive's demonstrated personality traits to be directly compared to those that may be desirable for his or her current position in the company. Additionally, it brings to light any differences between how the manager views himself or herself,

and how they are viewed by the assessor. The cause could be insufficient understanding on the part of the assessor, or possibly an executive that does not have a good grasp on how others view him or her. (Gladstone, 2004)

While these two psychological tests do not provide any direct answers, they do clarify an executive's default personality characteristics. These characteristics can then be compared with those that are desirable for the executive's position. The value, and unfortunately the difficulty, is in interpreting the results.

Trusted Sources

Another incredibly valuable method of assessing a company's executives is to use sources well known and trusted by the venture capitalists. Kevin Fong of the Mayfield Fund says that his firm, "relies consistently and heavily on its network of lawyers, portfolio companies and other respected contacts to uncover the best deals." (Camp, p. 5, 2002) John Doerr of Kleiner Perkins Caufield & Byers agrees and states that almost all of the ventures his firm invests in are referred by a trusted source. (Camp, 2002) Just as VCs use their trusted sources as screening sources, they use them equally as much to evaluate the management of companies in which they are considering investing.

Vcs at Draper Fisher Jurvetson have "carefully developed a network of 'intelligent, hard working, influential people' whom they can tap when they need to check a particular reference." (Camp, p. 27, 2002) In addition to trusted associates that have likely recommended a specific deal be investigated, a VC's broader network is likely to have interacted with the company's management

team at varying levels. These known sources can provide a much more candid summary of executives than will likely come from references listed by the executive, or other past co-workers of the person. Listed references are unlikely to say anything negative about an executive, hence the reason they were listed. Similarly, others unknown to VCs are unlikely to divulge an executive's inadequacies unless he or she harmed the person in some way.

Conversely, sources close to a VC will likely give a much more level description of a manager. People generally seek to maintain their relationships, and therefore would not want to highly recommend a poor manager to a VC. In this case the VC would eventually learn of the poor quality of the executive and lose faith in his or her trusted source. Unless the source has more to gain by convincing the VC a manager is good, he or she will likely provide a more honest appraisal of the executive's skill than other references that have nothing to lose. In fact, unknown references may have something to lose by disclosing an executive's shortcomings.

Management Preparedness

Top managers must have a clear vision of where their company is headed. This vision must be clearly communicated and built from a deep and dynamic understanding of the company's market and customers. Praveen Gupta of CDIB Ventures states that the key elements of a management team are the "passion, attitude and knowledge of their markets and customers." He describes knowledge of the customer as being able to "pinpoint the exact voids that customer faces." (Inside, p. 101, 2003) Knowing a market and its customers goes far beyond

Gartner reports and government studies. It is having a clear understanding of exactly what a customer wants.

However, managers must continually watch for changes in customer demands. Praveen adds that they should be “open to criticism, ready to steer through the turbulent periods, adjust to the market and customer needs.” (Inside, p. 101, 2003) An inflexible management team is a sure recipe for disaster. While confidence is important, an ego-driven continuation of a strategy that meets a no-longer existent customer demand is not helpful. In a dynamic market, managers must be able to “adapt their business models, their competitive strategies, their products and their people.” (Camp, p. 41, 2002) But, they must “have the guts and fortitude to undertake enormous risk and fully commit themselves to achieving incredibly lofty goals, and who also have a strong belief in their own ability to achieve those goals.” (Camp, p. 39, 2002) This dedication to hitting a moving target will ensure the company is consistently headed in the right direction.

Arthur Rock sums up the importance of getting to know a venture’s management team well when he says, “After all, a good idea, unless it’s executed, remains only a good idea. Good managers on the other hand, can’t lose. If their strategy doesn’t work, they can develop another one. If a competitor comes along, they can turn to something else. Great people make great companies...” (Camp, p. 23, 2002)

Completeness of Team

Team led companies are usually universally preferred as long as they are solid teams. According to Kevin Fong, some companies seeking venture capital recruit mediocre managers just to fill the empty positions, but without regard to the future problems that will likely result. (Camp, p. 30, 2002) If a management team is not complete, venture capitalists have large diverse networks from which to pull top talent. While this does add a layer of risk, it is certainly better than a bad hire.

Of great importance is determining if the management team possesses complimentary skills and backgrounds. A team full of similar executives will not benefit from diverse viewpoints. That said, the team must be able to work closely together on a daily basis. Even the slightest dissention among executives can balloon into a large problem as the stakes rise. According to Camp, “Discord among management team members is a primary cause of venture failure.”

(Camp, p. 33, 2002)

A great sign would be previous successes of members of the management team. This history lowers the risk of problems between team members in the current venture. It also provides an excellent indicator of the methods the executive team used last time. Past work allows for meaningful reference checks to determine how the team’s employees and previous venture capitalists felt about their business relationships.

Two additional considerations are the team’s ability to recruit new stars and the time left until their replacement. Being able to convince top talent to join

the rapidly growing venture is very important. Some companies use interviews directly with their CEOs as a method of attracting new talent. (Cardis, p. 40, 2001) Whether from the top, or through current employees' networks, attracting the best is essential for success in rapidly expanding the venture. This also increases the amount of time employees will be able to function in their roles before being replaced by more traditional professional managers. The innovative and energetic types of managers more commonly present in small companies will eventually need to be replaced by big-business process oriented executives.

Assessing the Board of Directors

For relatively young expanding companies, the board of directors is a critical resource to the company's success. The board must have "diverse and balanced skills, backgrounds, personalities, and perspectives, and to be appropriately experienced and well connected." (Camp, p. 59, 2002) To accomplish this it is generally recommended that board members be representatives from the company, investing parties and executives from companies in related industries. This ensures a neutral and qualified board. (Camp, 2002) Additionally, the other commitments of board members need to be considered. Even a well intentioned board can be ineffective if its members do not have enough time to devote to guiding the company.

Evaluating a board of directors can be done similarly to the evaluation of management team members. However, the degree of investigation is lessened. A phone call to board members can give sufficient information about a member's professional experience, other commitments and board participation level. A

VC's network can again provide unbiased information on the quality of board members and any ulterior motives that might impair neutral decision making.

Assessing the Board of Advisors

A board of advisors can be assessed in much the same way as the board of directors. The difference would be that the board of advisors should be assessed more through a VC's network that knows intimately the abilities of the advisory board members. As a team comprised to guide the strategic decisions of management, and not to represent investors, the advisors' experience and talent for mentorship is of prime importance. A VC's network is best equipped to evaluate these qualities.

Assessing the Business

Market Investigation

The market and management are unanimously the two most important factors venture capitalists examine when considering an investment. While many VCs say their investment strategy is “people...people...people,” others agree that the market is first on their list. Warren Musser of Safeguard Scientifics states that the first thing he examines in a business plan is the market, followed of course by the management team. Ken Fox of incubator Internet Capital Group states that “Ninety-nine to 100 percent of the deals that we do are market-driven.” (Cardis, p. 19, 2001)

Within the market context there is also much discussion on what characteristics lead to a successful VC investment. Kevin Fong of the Mayfield Fund states that, “[W]e like existing markets.” At Sequoia Capital they, “cannot afford to wait for markets to develop” and “do not have the money or inclination to educate customers to buy products they don’t know they need,” says partner Michael Moritz. Others such as Ann Winblad say, “We’re looking for people willing to think big, who want to take over the world.” (Camp, 2002) Either of these views requires much market investigation. Generally, the process for investigating an existing market relies on published information more than investigations into creating markets like Apple or Yahoo! have done.

Beginning by talking to the company’s management gives VCs a picture of how the company views the market and a basis for comparison against other views of the market. If everyone else a VC talks to sees the market differently the

company either has very unique foresight into customer needs, or more likely does not have a grasp of the market dynamics. Questioning management personnel about the statistics and assumptions presented in the business plan is also often the first step VCs take in gaining insight into the market niche the company is attacking. This is helpful for understanding later where the company's offering fits in the market.

John Cococcia of FA Technology Ventures states that after talking to the management team he reads everything he can discussing the market. While he looks at North American Industry Classification System (NAICS) data and analyst reports he finds that these background sources are not always entirely accurate. These sources can provide large amounts of information and analysis based on survey results, but Cococcia prefers to get the information straight from the source before investing. One method he uses is to call up the competitors of a venture and ask the management of these other similar companies how they view the market. Cococcia states that about 60% of the competitors he calls truthfully and thoroughly answer his questions. In fact, he has decided to invest in competitors of companies for which he was conducting due diligence because of interest peaked through these calls. (Cococcia, 2006)

Additionally, all VCs extensively question customers. *Venture Capital Investing* suggests that "it is important to get a qualitative "gut feel" about the customers' satisfaction." (Gladstone, 2004) Also important is to understand the relationship between the customer and company, such as when and how many products were bought. Getting an understanding of customers' satisfaction with

the performance of the product and the after sales service is also critical. VCs also need to understand how customers feel about the product's pricing and how it compares to competitor's offerings. (Gladstone, 2004) Asking if a customer would buy from the company again is a good traditional question, but current research suggests asking if the company would recommend the product to others may garner more telling responses. (McGregor, 2006)

Suppliers and strategic partners are two other groups of people that can provide market information. Suppliers can be questioned about their perceptions and interactions with other similar companies they supply. Good suppliers will likely understand their customers' markets because that, in turn, determines the demands of their market. Additionally, strategic partners frequently hold vast amounts of market information. These, typically more established companies have likely considered entering the market and decided to partner instead. The rationale behind not entering the market may hold critical information.

Mike Shatner of the Onondaga VC Fund states that he relies on his extensive network for all parts of assessing a deal, including the market. He uses his network to build a consensus on the size, major competitors and the addressability of the market. By the addressability he notes that some of his associates have unique knowledge about barriers to entry or structural changes happening in an industry that are not yet commonly known. This small bit of additional information allows him to make much better decisions. (Shatner, 2006)

A VC's network, strategic partners, suppliers, customers and competitors are valuable resources to build detail into more generic NAICS and analyst information. The comparison of this picture of the market to the company's management team's vision is also incredibly valuable. In-depth market information allows for a better analysis of the company's offering and future position in the market.

Offering Fit and Future

Assessing how well the company's offering fits customer needs is a process dominated by intensive customer interviews. "You can find a huge market and research your competitors to death, but, in the end, you need to know: 'Will the dogs eat the dog food?'" (Cardis, p. 27, 2001) To help determine the answer to this question Yogen K. Dalal of the Mayfield Fund says that he asks management "What is a typical day in the life of your customer?" (Camp, p. 79, 2002) The answer to this question is very telling of how well the company's management understands their customers. A good response details the daily activities and lifestyle of the customer, with great understanding of any factors that substantially influence the customer's need for the product. A good management team will be able to describe the many factors that create the customer's need, or perceived need, the steps the customer goes through in realizing the need, and how the company communicates to the customer their solution.

Management's opinion of this process must then be carefully compared to the customer's responses during the VC's questioning. John Cococcia suggests

asking customers open-ended questions that examine how they think about their process of realizing their need, researching solutions, choosing a solution and then purchasing and using that product. He also suggests VCs ask more probing questions in an attempt to determine subconscious or automatic customer responses that influence their purchasing process. Finally, Cococcia suggests moving into how customers plan on making their purchasing decisions in the future. (Cococcia, 2006) While past experiences are typically the best predictors of future behaviors, new information or experiences can have a large effect on a customer. All information on the decision making process customers will use in the future helps clarify what the prospects of the company are, after all, the sales that the VC is investing in will happen in the future.

Darlene Mann of Onset Ventures says to be ware of “one-trick pony” companies that are not looking forward to anticipate customers’ needs. (Camp, 2002) She suggests companies use platform models that naturally breed follow-on products and services. Any type of model also needs to have future versions of current products in the works. If the management team has succeeded in truly understanding their customers they have started down the right path, but must constantly be making adjustments as customer’s desires change.

Operational Performance

Assessing the company’s operational performance happens largely in two parts. The first part is questioning the company’s bank, accounting firm and law firm. If the company switched firms or representatives recently the past firm or representative should be questioned in addition to the current one. This in itself

can be telling of an organization that is not functioning properly. Frequent switches between support agencies likely means there are problems with the company itself, not its support agencies. The second part of the process is the traditional review of documents by the VC firm's lawyers and accountants. The company will be presented with a due diligence checklist of items that need to be delivered for inspection.

When discussing the company's relationship with the bank the amount of credit and amount of debt outstanding are of obvious importance. However, the logic or formulas behind determining these numbers are just as, or more, important. This shows how risky the bank views the business. Late interest or principal payments are likely to factor highly into this decision. Also knowing if the bank has ever called a loan to the company in default is important. If management did not disclose such an event it is likely other events have been omitted. Similarly, knowing if loans have been denied helps to uncover similar issues the bank sees in the company. Finally, asking the bank if it believes the company has any operating problems can open the floor for issues that might otherwise not come up. Getting the bank to talk generally about how the bank understands the company as operating, and its view of the management team's competency create these broad opportunities for discussion. (Gladstone, 2004)

The accounting firm the company uses can also be of great help in determining the operational effectiveness of the company. Verifying the accountant's agreement with the numbers in audits that have been presented by the company ensure that there have been no misrepresentations in the company's

operating performance. However, forward looking financial statements are difficult for any party to critique. Russell Siegelman of Kleiner Perkins Caufield & Byers states that, “The financials are usually not even close.” (Roberts, p. 5, 2004) He looks at the projections made by high-growth companies as more of a credibility test to determine how the entrepreneur or management team thinks. Looking for the logic and assumptions behind the projections can tell a lot about the quality of a manager.

Examining the company’s tax return is another easy way to ensure that the past financial statements are accurate. More generally, discussing the accountant’s letter to management, if written, can bring to light what the accountant sees wrong with the operations and financial controls of the company. Issues with a company’s financial records are typically a sign of deeper operational problems. Additionally, discussing the ability of the current financial officer to continue his or her duties as the company expands can save time and prevent problems at a later date. Lastly, asking the accountant if he or she believes the company is having operating issues or if they expect the current year’s statements to be materially different opens up the conversation one last time to allow any concerns to surface. (Gladstone, 2004)

The law firm representing the company can likely give a wide array of information on the firm. It will be able to confirm and discuss the company’s corporate structure and the implications thereof. This would include any special circumstances relating to where or how the company was incorporated. The law firm will also be able to give detailed information about the status of any

intellectual property the company may own the rights to. Having a clear understanding of all issues surrounding intellectual property which the company either owns or licenses is critical given the type of investments most venture capitalists make. The recent agreement of Research in Motion to pay NTP \$612.5 million is a prime example of what can happen without careful consideration of intellectual property rights. (Krazit, 2006) Additionally, asking the law firm to describe any suits or legal issues that have been encountered, are currently undergoing, or they feel are likely to happen will help determine if the company has any material legal concerns to further investigate. In the event of any outstanding issues the law firm's opinion on the likely result can be of critical importance. Finally, asking the law firm if it sees any current or potential legal problems with the company makes one last broad sweep and allows the lawyers to discuss issues that may not have surfaced previously. (Gladstone, 2004)

Other companies involved in business with the firm seeking funding can also provide valuable insight into the firm's operations. The insurance agency can confirm that the business is properly insured and is not in danger of being dropped. The company's landlord can confirm lease arrangements and discuss the timeliness of past payments. Suppliers can also be of great help because they likely also serve similar customers by which they can build a basis for comparison. Conversations with these other businesses can help a VC understand if the company is running like a well oiled machine, or struggling to maintain control.

The second step in the process is to review and submit items from the due diligence checklist to the VC's accountant and law firm. These professionals will know what to look for without much guidance and will surely point out any issues that the company's representative may have been unwilling to disclose. A sample due diligence checklist from TL Ventures is included as Appendix C.

The Deal

After the due diligence process is completed, VCs must decide on the terms of the investment that the company's management will agree to. Mike Shatner notes that there is a big difference between a good company and a good investment. A deal that is being competed for by multiple VC firms can end with a valuation or deal terms that make an investment in even the best company a mistake. (Shatner, 2006)

Legal Issues

A competent and motivated attorney is clearly the best method for evaluating the terms of an investment. An attorney with experience in venture capital financing will be able to draw attention to critical issues for VCs to consider when deciding whether or not investing in a prospective portfolio company is attractive.

One of the issues VCs need to consider is the form of the company in which they are considering investing. Lawyers generally recommend C-corporations because of their familiarity and the substantial legal precedents that have been built for them. While they cause double taxation they allow an easy route to an initial public offering and many other benefits. The state of incorporation may also make later legal matters simple or quite complex. While incorporating in the company's home state may simplify the legal footwork initially, all states have different laws governing businesses, some very different and much more attractive than others. An attorney can help determine the

implications of a company's present legal form and ensure all necessary documents have been filed correctly. (Camp, 2002)

A law firm can also assess any pending or likely legal actions either against or by the company. As mentioned, a large settlement such as in the case of Research in Motion can have a substantially negative impact on a company's value. Legal due diligence can be somewhat lengthy and costly but pay off many times over. Intellectual property is hugely valuable to the vast majority of the companies that VCs invest in. Ensuring that any copyrighted, patented, trade marked or licensed materials are either owned by or have terms that are fully understood by both management and VCs is critical. Invention assignment contracts in addition to non-compete and nondisclosure agreements are also frequently important to ensure the continued success of a portfolio company. (Camp, 2002)

The structure of the company's equity is also of great importance. Existing investors may have special rights and privileges that change the attractiveness of an investment such as antidilution rights, approval rights or the right of first refusal. The type and conversion rights of current debt instruments additionally need to be investigated. Straight debt, preferred stock and common stock all have very different implications for new investors. Different classes of stock can have a material impact on the outcome of a liquidity event.

Finally, the rights of a VC during such a liquidity event can have a significant effect on the return they receive. The registration rights of a VC determine when, if, how and how much of their equity they can exchange for cash

at the time of the liquidity event. This is typically most important in an IPO, although a disgruntled management team could sell their equity to an outside investor without a VC's blessings under the right conditions. Drag-along, anti-lockout, tag-along (co-sale), and redemption rights help to decrease the likelihood of a negative result given an upset or greedy team of executives. (Camp, 2002)

While these few issues are simply a handful of important topics to be covered with an experienced attorney, they serve as a starting point. Negative results must be considered even with the most honest and competent executives.

Valuation

Valuation is always a hotly contested aspect of attaining venture capital financing. "Venture capitalists have a strong interest in obtaining the lowest pre-money valuations possible. Doing so maximizes their percentage ownership as well as the returns on their investments." (Camp, p. 213, 2002) Conversely, entrepreneurs have just as strong an interest in obtaining a high valuation to maximize their ownership and returns. Unfortunately, this sets VCs and entrepreneurs against each other. However, VCs have no way to create a return without entrepreneurs and entrepreneurs have no way to grow their company without VCs, so compromise must prevail.

First, both parties must agree on a terminal value, or value that the company can likely be sold for at the time of the liquidity event. Many methods for determining terminal values exist, the multiples method being one of the more popular. This method requires finding a business that will be comparable to the one being valued when it reaches its liquidity date. Size, profitability, growth

rate, capital intensity and risk are some factors that need to be considered in determining the comparability of companies. (Camp, 2002) The value of the company can then be extrapolated using the multiple of the comparable company's price to earnings or price to revenues. (Wilmerding, 2006) "That terminal value is then heavily discounted to reflect the risk, the fact that their investment is illiquid and that they have contributed to the success of the business." (Hill, p. 214, 2001)

William Sahlman of the Harvard Business School suggests that common discount rates for first stage companies are between 40% and 60%. For seed or start-up stage companies they can range much higher. (Camp, 2002) The discount rate and terminal value can then be combined with the estimated time to liquidity to discount the company's value to the investment time period. If a VC expects that further rounds of funding will be needed, he or she will also factor in the effects of the resulting equity dilution. John Willinge of Thomas Weisel Partners and Josh Lerner of the Harvard Business School state that investors must divide the required final ownership percentage by the retention ratio (percentage of the original equity stake in the company that will be owned after dilution) to determine the current amount of equity investors must demand. The investment amount is then divided by the resulting equity stake to determine the company's valuation. (Camp, 2002)

The assumptions behind the company's terminal value, time to liquidity and dilution due to additional funding are difficult to predict, and as such can vary widely between entrepreneurs and VCs. Eventually, the valuation is determined

by the values VCs offer the entrepreneur, and whichever VC is deemed to offer the most attractive valuation and services combination. There is no equation that can determine what a VC should pay, only equations from which to base negotiations.

Summary and Conclusions

Through books, trade magazines and personal interviews, this paper examines the venture capital industry and focuses on the methods used by VCs during the due diligence process. The study primarily discussed how the different steps of the process need to be conducted, and as such is most applicable to practitioners, but also informative for entrepreneurs and academics. Additionally, the research was concentrated around the due diligence process recommended for expansionary funding, as opposed to startup or turnaround financing. Startup due diligence follows a very different process because companies have no operating history, the investment is made purely on a small management team and market forces. Alternatively, turnaround financing relies very heavily on the operations of a company because this area is most heavily changed.

This research is important because of the complexity of private equity versus public equity funding. Private companies typically have much less operational data than do public companies. This creates a significant degree of risk that is difficult to quantify through traditional means. Additionally, the uncertainty of market conditions for a future liquidity event makes establishing an accurate company valuation difficult. Also, in comparison to public equity markets private equity remains an understudied area. Large numbers of participants in a market with mature companies have led to very well defined mathematical approaches to investing. In private equity smaller numbers of participants have not put in as much time, in aggregate, to develop market efficiency.

The key findings of this paper were focused around the initial screening of opportunities, assessment of management, of the business and of the terms of the deal. Key industry trends and myths were also discussed.

The process used in the initial screening of business plans is important to understand for VCs and entrepreneurs alike. The majority of plans submitted are eliminated in this first step of the venture capital due diligence process to allow VCs more time for assessing more promising investments. One of the primary methods used by successful VCs in this effort is to rely on a network of contacts for referrals. Professional contacts known by VCs serve as a first line of defense against bad business plans and teams. However, a VC's close inner circle provides the most trusted referrals and has the most to lose from a poor recommendation.

In addition to these opportunities, VCs usually consider a smaller number of plans that look to be of high quality. Submissions with any errors, a poor look and feel or that simply do not immediately impress are discarded. The remaining opportunities are then compared against the firm's preferred investment stage, geography and industries. If these qualifications match, the reputation of business associates, the management team and other investors will be considered. This initial process can be fairly subjective as VCs may weight certain factors more than others. For instance, some VCs rely almost exclusively on their network for referrals, ignoring almost all unsolicited business plans.

After the initial screening of opportunities, most VCs agree that management represents the most significant risk. As such the assessment of a

company's executive team is a very in-depth process. Checking references is an obvious place to start, but only helpful with carefully crafted questions and as a method to seek out other people that have had meaningful interactions with the person being assessed. Those with nothing to lose by being honest, or preferably those with something to lose by not disclosing all material information are most valuable. These conversations can then highlight issues that need to be investigated during the interview process. Behavioral interview questions can be very powerful when asked by someone knowledgeable in their use. Some cutting edge companies have started accompanying these questions with case studies to examine how executives interpret and solve problems.

Ethical or integrity based questions are also important in assessing a management team given the necessity of VCs trusting a company's executives in their everyday activities. Questions to determine if managers have ever bent the truth when striving for goals or reporting results give an indication of what will likely happen between the VCs and executives. Psychological tests such as the Myers Briggs Type Indicator or more advanced testing methods conducted by industrial psychologists have become popular given the complexity in assessing many executives. However, old fashioned discussions with trusted sources that have interacted with executives on a significant basis can provide the most concrete information. Full profiles are unlikely to develop, but clear themes typically emerge.

Management preparedness and the completeness of the executive team are also closely considered when assessing the management risk. Gauging how

prepared a team is to lead a venture can only be assessed through understanding the industry in which the company is operating. Management assumptions and expectations need to be compared with the consensus of industry experts. The willingness to change strategies in response to industry changes is also critical. A complete and fully functioning management team makes this process more likely to happen and more accurate. A team that compliments each other and has worked well together in the past eliminates a large amount of uncertainty.

Finally, in close relation to assessing the actual management team members, their mentors should also be assessed. A properly constructed and fully committed board of directors assures agency costs will be at a minimum. Similarly, a strong board of advisors can prove an invaluable resource for executives when they encounter unfamiliar territory. These boards are typically assessed much less rigorously through an informal phone interview and the opinions of a VC's network.

Assessing the market is also argued to be the most important aspect in assessing an investment opportunity. This aspect is clearly the most important in assessing the business. Many leading VCs suggest starting to understand the company's market niche by questioning and probing executives on their market data and assumptions. This information can then be compared to many basic readings on the general industry. Analyst reports and NAICS data are frequently used to determine broad market trends and data. More specific information can be found by questioning a potential investment's competitors, customers,

suppliers and strategic partners. Finally, trusted sources are also tapped for unique market insight from an unabated perspective.

Once a thorough understanding of a company's market and customer segments is formed the fit of the company's offering can be assessed. This is typically done through intensive interaction with customers. VCs do interviews and may have some customers try the product or service and give feedback. The goal is to get inside the minds of customers and determine what makes them tick. The company's management should already completely understand all of this information. Finally, VCs also gauge the probability of successful next generation offerings or related products.

Assessing the company's operations is generally the next step in the process through contacting current and past banks, accountants and law firms. These three firms will have unique insight into the way the company functions internally and personal or phone interviews are typically used to gather the information. Assessing operations also includes the review of documents on a due diligence checklist by the VC's accounting and law firms. This step is fairly cumbersome but can bring to light issues that were not properly disclosed.

Finally, the terms of the deal must be agreed upon with the help of the company and VC's law firms. Generally VCs prefer to step back and let the two sets of lawyers battle in this last part of the deal but do have preferences for decision making rights and rights during liquidity events. The company's valuation is always the most hotly contested aspect of the deal terms because it relies on the highly speculative value of the company many years away. The

company's management and VCs almost never come to consensus on this value but eventually the different valuations offered to the company by VCs determines the true value of the company.

Two key industry trends that will increasingly affect this process are the globalization of venture capital markets and the historically low levels of IPOs in the United States. Investing internationally adds a significant degree of complexity in assessing foreign markets and management teams with less established networks. International investing also presents differing legal and financial accounting environments requiring very well trained professionals. Additionally, the low levels of IPOs are making valuations more difficult which have typically been based on multiples of similar public companies. VCs must now increasingly gauge what the mergers and acquisitions market will look like five to seven years away.

Further research on the implications of these trends as they unfold would be very beneficial. Israel could serve as a current case study with an investigation of the likely differences and similarities in other countries that become popular, such as China. Similarly, in-depth research into valuation techniques and the implications of a slow IPO market would add value to the subject area. Many of the valuation techniques used in the boom days around 2000 are no longer the most accurate methods with the popularity of mergers and acquisitions as exits.

Finally, research specifically concentrating on interview techniques specially formulated for venture capital would help VCs ask better questions. Lists of possible questions to evaluate different aspects of a management team

and their customers would be especially beneficial. Similarly, interviews with leading VCs to discuss how they leverage their networks would open up a large black box many VCs seem unwilling to talk about. This type of information is very valuable, and as such, successful VCs are guarded about giving away their trade secrets. There are certainly many other areas for further research in the venture capital industry. It remains an area worthy of much additional study.

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Appendices

Appendix A: Myers Briggs Type Indicator

Each type, or combination of preferences, tends to be characterized by its own interests, values, and unique gifts. On this page is a brief description of each type. Find your reported type and see whether the description fits you. If not, the person who administered the MBTI® instrument to you can help you identify a better-fitting type. Whatever your preferences, you may still use some behaviors that are characteristic of contrasting preferences. For a more complete discussion of the sixteen types and applications such as career choice, relationships, and problem solving, see *Introduction to Type®*, Sixth Edition (Myers, I. B., 1998, Mountain View, CA: CPP, Inc.), or *Gifts Differing* (Myers, I. B., with Myers, P. B., 1995, Mountain View, CA: Davies-Black Publishing).

E Extraversion People who prefer Extraversion tend to focus on the outer world of people and things.	I Introversion People who prefer Introversion tend to focus on the inner world of ideas and impressions.
S Sensing People who prefer Sensing tend to focus on the present and on concrete information gained from their senses.	N Intuition People who prefer Intuition tend to focus on the future, with a view toward patterns and possibilities.
T Thinking People who prefer Thinking tend to base their decisions primarily on logic and on objective analysis of cause and effect.	F Feeling People who prefer Feeling tend to base their decisions primarily on values and on subjective evaluation of person-centered concerns.
J Judging People who prefer Judging tend to like a planned and organized approach to life and prefer to have things settled.	P Perceiving People who prefer Perceiving tend to like a flexible and spontaneous approach to life and prefer to keep their options open.

Characteristics Frequently Associated with Each Type

Sensing Types		Intuitive Types		
ISTJ Quiet, serious, earn success by thoroughness and dependability. Practical, matter-of-fact, realistic, and responsible. Decide logically what should be done and work toward it steadily, regardless of distractions. Take pleasure in making everything orderly and organized—their work, their home, their life. Value traditions and loyalty.	ISFJ Quiet, friendly, responsible, and conscientious. Committed and steady in meeting their obligations. Thorough, painstaking, and accurate. Loyal, considerate, notice and remember specifics about people who are important to them, concerned with how others feel. Strive to create an orderly and harmonious environment at work and at home.	INFJ Seek meaning and connection in ideas, relationships, and material possessions. Want to understand what motivates people and are insightful about others. Conscientious and committed to their firm values. Develop a clear vision about how best to serve the common good. Organized and decisive in implementing their vision.	INTJ Have original minds and great drive for implementing their ideas and achieving their goals. Quickly see patterns in external events and develop long-range explanatory perspectives. When committed, organize a job and carry it through. Skeptical and independent, have high standards of competence and performance—for themselves and others.	Introverts
ISTP Tolerant and flexible, quiet observers until a problem appears, then act quickly to find workable solutions. Analyze what makes things work and readily get through large amounts of data to isolate the core of practical problems. Interested in cause and effect, organize facts using logical principles, value efficiency.	ISFP Quiet, friendly, sensitive, and kind. Enjoy the present moment, what's going on around them. Like to have their own space and to work within their own time frame. Loyal and committed to their values and to people who are important to them. Dislike disagreements and conflicts, do not force their opinions or values on others.	INFP Idealistic, loyal to their values and to people who are important to them. Want an external life that is congruent with their values. Curious, quick to see possibilities, can be catalysts for implementing ideas. Seek to understand people and to help them fulfill their potential. Adaptable, flexible, and accepting unless a value is threatened.	INTP Seek to develop logical explanations for everything that interests them. Theoretical and abstract, interested more in ideas than in social interaction. Quiet, contained, flexible, and adaptable. Have unusual ability to focus in depth to solve problems in their area of interest. Skeptical, sometimes critical, always analytical.	
ESTP Flexible and tolerant, they take a pragmatic approach focused on immediate results. Theories and conceptual explanations bore them—they want to act energetically to solve the problem. Focus on the here-and-now, spontaneous, enjoy each moment that they can be active with others. Enjoy material comforts and style. Learn best through doing.	ESFP Outgoing, friendly, and accepting. Exuberant lovers of life, people, and material comforts. Enjoy working with others to make things happen. Bring common sense and a realistic approach to their work, and make work fun. Flexible and spontaneous, adapt readily to new people and environments. Learn best by trying a new skill with other people.	ENFP Warmly enthusiastic and imaginative. See life as full of possibilities. Make connections between events and information very quickly, and confidently proceed based on the patterns they see. Want a lot of affirmation from others, and readily give appreciation and support. Spontaneous and flexible, often rely on their ability to improvise and their verbal fluency.	ENTP Quick, ingenious, stimulating, alert, and outspoken. Resourceful in solving new and challenging problems. Adept at generating conceptual possibilities and then analyzing them strategically. Good at reading other people. Bored by routine, will seldom do the same thing the same way, apt to turn to one new interest after another.	Extraverts
ESTJ Practical, realistic, matter-of-fact. Decisive, quickly move to implement decisions. Organize projects and people to get things done, focus on getting results in the most efficient way possible. Take care of routine details. Have a clear set of logical standards, systematically follow them and want others to also. Forceful in implementing their plans.	ESFJ Warmhearted, conscientious, and cooperative. Want harmony in their environment, work with determination to establish it. Like to work with others to complete tasks accurately and on time. Loyal, follow through even in small matters. Notice what others need in their day-by-day lives and try to provide it. Want to be appreciated for who they are and for what they contribute.	ENFJ Warm, empathetic, responsive, and responsible. Highly attuned to the emotions, needs, and motivations of others. Find potential in everyone, want to help others fulfill their potential. May act as catalysts for individual and group growth. Loyal, responsive to praise and criticism. Sociable, facilitate others in a group, and provide inspiring leadership.	ENTJ Frank, decisive, assume leadership readily. Quickly see illogical and inefficient procedures and policies, develop and implement comprehensive systems to solve organizational problems. Enjoy long-term planning and goal setting. Usually well informed, well read, enjoy expanding their knowledge and passing it on to others. Forceful in presenting their ideas.	

Appendix B: Adjective List

- Accurate
- Achieving
- Adaptive
- Adventurousome
- Affiliative
- Aggressive
- Ambitious
- Apologetic
- Apprehensive
- Approval-seeking
- Carefree
- Comforting
- Competitive
- Concerned
- Conforming
- Conservative
- Consoling
- Creative
- Cultured
- Dependent
- Educated
- Egotistic
- Empathetic
- Energetic
- Envious
- Fun-loving
- Goal-oriented
- Good-natured
- Guarded
- Hard-working
- Help-seeking
- Honest
- Humble
- Idealistic
- Impatient
- Independent
- Innovative
- Insecure
- Intellectual
- Kind
- Knowledgeable
- Law-abiding
- Leadership
- Liberal
- Likeable
- Loyal
- Meek
- Meticulous
- Nurturing
- Obedient
- Open-minded
- Optimistic
- Outgoing
- Passive
- Persistent
- Pessimistic
- Pleasure-seeking
- Precise
- Protective
- Pro-active
- Quick-thinking
- Quiet
- Religious
- Reserved
- Responsible
- Rigid
- Sarcastic
- Secretive
- Seeks attention
- Seeks recognition
- Self-blaming
- Sensitive
- Serious
- Silly
- Sincere
- Status-conscious
- Striving
- Suspicious
- Sympathetic
- Trusting
- Truthful
- Uncaring
- Unconventional
- Virtuous
- Warm
- Wise

Appendix C: TL Ventures Due Diligence Checklist

		TL VENTURES DUE DILIGENCE CHECKLIST			
Requested	Submitted		Yes	No	Notes
		Due Diligence Request List			
		GENERAL INFORMATION			
<input type="checkbox"/>	<input type="checkbox"/>	Provide Organization Chart and other information regarding structure of the Company, including subsidiaries and other affiliates, % ownership and jurisdiction of each organization.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide listing of officers, directors and key management/ supervisory personnel with appropriate background information regarding credentials.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide summary of number of employees with relevant information, by functional group (Sales, Marketing, R&D, G&A, etc.) with approximate total wage/ salary cost of each category.	<input type="checkbox"/>	<input type="checkbox"/>	
		ORGANIZATIONAL MATTERS			
<input type="checkbox"/>	<input type="checkbox"/>	Provide all corporate charter documents and by-laws (including all amendments to date), if applicable, of the Company and any other corporation, partnership or other entity in which the Company has an equity interest which relates to any business of the Company (an "affiliate"). Comment on any unusual clauses, preemptive rights, cumulative voting, special majority and quorum requirements.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide all minutes of meetings of boards of directors, committees (including executive and finance), and shareholders for the past five years.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	For each class of stock, provide listing of current shareholders indicating name, number of share owned and special restrictions (if any).	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	For each class of stock provide listing of holders of options, warrants, rights, etc. indicating related terms (issue date, exercise date and price, vesting, etc.). Also provide copies of form of warrant, option, right agreement, etc.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide agreements relating to the purchase, sale or issuance of securities, including any warrants or options.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	All agreements under which any person has registration rights for any securities of or preemptive rights for shares of capital stock of the Company.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide information on any treasury stock acquisition or any obligation to issue or repurchase shares.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide information regarding the exchanges on which the Company's stock is traded or, if over the counter, the dealer making markets, the extent of the public float, institutional holdings, trading volume and total market capitalization. Provide copies of any SEC filings and a shareholder list, if available.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	For each class of debt, provide listing of debt holders.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide details regarding all voting agreements, voting trusts, proxies relating to capital stock of the Company.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide listing and appropriate details regarding investments in other corporations or entities.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide information regarding all corporate and fictitious names used by the Company and any	<input type="checkbox"/>	<input type="checkbox"/>	

Requested	Submitted		Yes	No	Notes
<input type="checkbox"/>	<input type="checkbox"/>	predecessors in the past five years.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide names, addresses, and contacts of Company's professional advisors, including attorneys, auditors, lenders and investment bankers.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Detail the locations of Company's financial and legal records.	<input type="checkbox"/>	<input type="checkbox"/>	
		LITIGATION			
<input type="checkbox"/>	<input type="checkbox"/>	Provide copies of the legal representation letters sent to the Company's auditors with Company responses, for the past five years.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide a summary of all litigation or arbitration, claims and proceedings (whether pending or threatened), to include worker's compensation actions, in which the Company or any affiliate or any officer or director of the Company is a party.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide all litigation files relating to any pending or threatened legal proceedings in which the Company, affiliate, officer or director is a party.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide all consent decrees, injunctions, judgments, other decrees or orders, settlement agreements, and other agreements to which the Company is bound, that requires the payment of money by the Company or prohibits any activity by the Company.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide reports, files, significant correspondence and documentation relating to any investigation or proceedings by any federal, state or other governmental regulatory agency in respect to the Company.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide a summary of any ongoing tax disputes between the Company and the federal government, the IRS, any state or local government or taxing authority, and any foreign jurisdiction or foreign taxing authority.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide information regarding in-house counsel to the Company, including legal representation, coordination with outside counsel, etc. Provide addresses and contacts at all outside law firms.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Detail any charges that may be pending against the Company by any federal or state agency regulatory body or agency.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide relevant information in the event that the Company's officers, directors or employees been involved in criminal proceedings regulatory commission violations or significant civil court litigation.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Describe, if any, legal problems that competitors have experienced, and if such problems will eventually confront the Company.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Discuss any international legal issues.	<input type="checkbox"/>	<input type="checkbox"/>	
		REGULATION AND PERMITS			
<input type="checkbox"/>	<input type="checkbox"/>	Discuss whether the Company is in compliance with environmental, equal opportunity employment, OSHA requirements or other regulations or requirements peculiar to the industry. If not, discuss what compliance will cost.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Discuss whether there are products that need governmental review and approval. If so, discuss the current stage of the	<input type="checkbox"/>	<input type="checkbox"/>	

Requested	Submitted		Yes	No	Notes
		approval process.			
<input type="checkbox"/>	<input type="checkbox"/>	List and describe and provide copies of all governmental licenses and permits required for the Company's business as currently conducted or planned (except environmental permits as covered above).	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Comment upon any governmental regulations which might impact the Company's business either domestically or in foreign countries.	<input type="checkbox"/>	<input type="checkbox"/>	
		INTELLECTUAL PROPERTY			
<input type="checkbox"/>	<input type="checkbox"/>	List and copies of patents held and applications made by the Company and all related material correspondence and documentation (including file wrapper).	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	List trademarks held and applications made by the Company and all related material correspondence and documentation.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	List copyrights held and applications made by the Company and all related material correspondence and documentation.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	List and copies of design and model rights held and applications made by the Company.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Trade names used by the Company.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Identify all persons who created or participated in the creation of the Company's intellectual property.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	List and copy of licenses for any form of intellectual property held by or granted by the Company.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Description of any pending or threatened infringement claims by or against the Company, and copies of any such claims for the last five years.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Description of any important know-how at the Company's disposal	<input type="checkbox"/>	<input type="checkbox"/>	
		FINANCIAL and ACCOUNTING MATTERS			
		General			
		Provide audited financial statements and other financial documents of the Company and any affiliates for the past 3 fiscal years. Including (where applicable):			
<input type="checkbox"/>	<input type="checkbox"/>	i. Comparative financial results by major divisions	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	ii. Detailed breakdown of sales and costs	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	iii. Detailed breakdown of general and administrative expenses	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	iv. Detailed breakdown of selling and marketing expenses	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	v. Detailed breakdown of working capital accounts	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	vi. Detailed breakdown of fixed assets	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	vii. Depreciation and capital expenditures (with particular emphasis on capitalized software development expense, if applicable)	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	viii. Tax returns, IRS reports or correspondence.	<input type="checkbox"/>	<input type="checkbox"/>	
		Provide the following, if applicable:			
<input type="checkbox"/>	<input type="checkbox"/>	i. Chart of accounts and a description of accounting practices.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	ii. Accounting procedure manuals and location and	<input type="checkbox"/>	<input type="checkbox"/>	

Requested	Submitted		Yes	No	Notes
		nature of accounting records.			
<input type="checkbox"/>	<input type="checkbox"/>	Outline any seasonal bank borrowings required.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Outline any foreign exchange requirements, procedures for hedging and value of transactions done in foreign currency.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Name and address of auditors of Company and any prior auditors (date of appointment, duration, remuneration).	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Accountants' management control letters concerning the Company and any responses by the Company for the past five years.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	All audit documentation, papers and communications between the Company and its auditors, other consultants or the IRS and any internal audit reports.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	All documentation relating to material write-downs or write-offs by the Company of notes or accounts receivable or inventories, other than in the ordinary course of business.	<input type="checkbox"/>	<input type="checkbox"/>	
		Receivables			
<input type="checkbox"/>	<input type="checkbox"/>	For accounts receivable, provide:	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	i. analysis of total receivables due from customers, officers, employees and others	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	ii. aged trial balance of receivable accounts above; compare them to aging percentages for previous years and comment on any trends, seasonality, etc.	<input type="checkbox"/>	<input type="checkbox"/>	
		For customer receivables, provide:			
<input type="checkbox"/>	<input type="checkbox"/>	i. terms of sales	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	ii. number of customers	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	iii. names of large customers and amount of annual sales to each by product line; comment on any special arrangements with any of these customers	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	iv. credit policies and comment on the effectiveness of credit department and significance of credit limits	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	v. turnover data	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Discuss collectibility of receivables and adequacy of loss reserves.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Discuss if receivables are discounted or pledged as collateral for borrowings.	<input type="checkbox"/>	<input type="checkbox"/>	
		Liabilities			
<input type="checkbox"/>	<input type="checkbox"/>	Provide detail of any assets pledged as collateral.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide detail of the Company's compliance with loan covenants.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide details about all financial liabilities, recorded or contingent, including the general terms of all notes, bonds and mortgages with particular reference to personal guarantees and accelerated maturity upon change of control.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Specifically address contingent liabilities such as:	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	i. contracts and agreements	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	ii. price redetermination or renegotiation	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	iii. sales subject to service and warranty guarantees	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	iv. product liability	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	v. unfunded past service costs of pension plans or unfunded retirement benefits.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	With respect to accounts payable, provide an analysis of payables by type (vendor, taxes, payroll, etc.) and describe payment practices for each.	<input type="checkbox"/>	<input type="checkbox"/>	

Requested	Submitted		Yes	No	Notes
		Budgets and Forecasts			
<input type="checkbox"/>	<input type="checkbox"/>	Describe the budgeting process, including capital budgeting, if applicable.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	For each of the next three years (calendar or fiscal years ended), provide consolidated projections and separate business unit projections, on a quarterly basis, including:	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	i. income statements, balance sheets and cash flow statements	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	ii. underlying assumptions including product/ service introductions, market size, market share, pricing, volumes, discounts, ramp-up costs, etc.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	iii. underlying assumptions for all major expense and capital expenditures, particularly R&D/ software development	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Discuss the amortization policy for any prepaid expenses or deferred charges	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Discuss how goodwill or other intangibles arose and how they are being amortized. Address any issues regarding the "going concern value".	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide details regarding the important metrics which management uses to run the Company (capacity utilization, sales per person, benchtime, etc.). Provide comparisons of these metrics for the past three years.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Discuss how the Company's metrics compare with the industry in general, and with peers/ competitors.	<input type="checkbox"/>	<input type="checkbox"/>	
		TAXES			
<input type="checkbox"/>	<input type="checkbox"/>	All tax returns or copies of extensions of time within which to file such reports filed by the Company with the Federal government, the Internal Revenue Service, any state or local government or taxing authority, and any foreign jurisdiction or foreign taxing authority, for at least the past three fiscal years, and any years prior thereto that remain open and subject to review by the IRS or any other taxing authority. Provide copies of all audit, determination and other correspondence pertaining thereto.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Copies of all tax-sharing and other tax-related agreements.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	All information related to any audit of any return or report filed by or on behalf of the Company for the last three fiscal years, and any pending audits for any prior periods that could affect the tax liability, credits or other tax attributes of the Company.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	For state franchise or similar tax liabilities of the Company, a schedule setting forth, for each state in which such payments were made, the most recent period for which a franchise tax or similar tax payment was made, and the date on which each payment is due and payable each year.	<input type="checkbox"/>	<input type="checkbox"/>	
		For each applicable state, discuss:			
<input type="checkbox"/>	<input type="checkbox"/>	i. if there have been any state tax audits	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	ii. if any adjustments made by federal revenue agents have been reported to the states affected	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	iii. if the state tax returns have been amended to reflect IRS adjustments	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Prepare a schedule showing the percentage of Federal Taxable Income being reported to the states in which the Company files returns (the sum of all state apportionment factors).	<input type="checkbox"/>	<input type="checkbox"/>	

Requested	Submitted		Yes	No	Notes
<input type="checkbox"/>	<input type="checkbox"/>	For personal and real property taxes, provide a schedule setting forth, for each location in which such payments were made, the most recent period for which such tax payment was made, and the date on which such payment is due and payable each year.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide a schedule describing any ongoing tax disputes, together with copies of revenue agents' reports, correspondence, etc., with respect to any pending federal, state, provincial or similar tax proceedings, with regard to open years or items relating to the Company.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide detailed reconciliations of the Company's effective tax rate for the past three years.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide an analysis of any deferred taxes.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide schedules reconciling book income to taxable income for the last three years.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide detail of the amounts and expirations of any carryovers of net operating or capital losses, investment tax credits, foreign tax credits and other tax credit carryovers.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Discuss the tax basis for the Company's assets.	<input type="checkbox"/>	<input type="checkbox"/>	
		MATERIAL AGREEMENTS and DOCUMENTATION			
<input type="checkbox"/>	<input type="checkbox"/>	Provide all documentation relating to real property owned or leased by the Company (including, without limitation thereto, purchase agreements, leases, title policies, title reports, surveys, easements, rights of way, licenses and deeds). Note: for real property, title reports and surveys are especially important.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide information regarding all mortgages and other security documents relating to any of the properties or assets (real or personal) of the Company.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	If not previously provided, Material Agreements/Documents, list and copy of all contracts with dealers, distributors, agents and others.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Copy of general sales conditions of the Company; model contracts, orders and invoices.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide the form of product warranties of the Company.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Give a general description of warranty claims during the last three years, and discuss significant or unusual claims.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide all contracts and agreements relating to the Company to which any officer, director, employee or stockholder of the Company is a party or in which any officer, director, employee or stockholder of the Company has an interest including secrecy, confidentiality, nondisclosure, assignment of inventions and non-compete agreements.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	All equipment leases (operating or capitalized) to which the Company is a party or is bound or in which the Company has an interest.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	All agreements and contracts concerning any acquisition or disposition in the past five years by the Company of any substantial properties or assets, whether real or personal, outside the ordinary course of business.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	All documents and agreements relating to any merger, consolidation or corporate division in the past five years in	<input type="checkbox"/>	<input type="checkbox"/>	

Requested	Submitted		Yes	No	Notes
		which the Company was a party or the surviving corporation.			
<input type="checkbox"/>	<input type="checkbox"/>	All loan agreements, guarantees, indentures, promissory notes, debentures, line of credit and related documentation in connection with any loan or other indebtedness of the Company.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	All loan agreements, guarantees, indentures, promissory notes, debentures, line of credit and related documentation in connection with any advances or loans made by the Company to an officer, director employee or shareholder of the Company.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	All license and royalty agreements to which the Company is a party or in which the Company has an interest.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	All agreements and contracts between the Company and any affiliate including, without limitation thereto, any royalty and license agreements.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	All sales, marketing and distribution agreements to which the Company is a party or by which it is bound (including documentation with any brokers and other independent sales persons or entities).	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	All contracts and agreements with suppliers of services, raw materials, finished or semi-finished materials, or products of the Company.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	All standard forms of purchase orders, sales orders, supply contracts, service contracts and sales contracts used by the Company.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	All agreements to which the Company is a party or by which it is bound, for the delivery, manufacture or supply of goods or services.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Any other particular agreements based on Company business.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Government contracts and subcontracts, if any.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	All evidences of intercompany debt.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	All insurance policies, and a claims history and any correspondence between the Company and the insurer.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Certificate of insurance (casualty, property, liability, errors and omissions, officer and director, etc.). To the extent coverage has changed during the past three years, please indicate.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Any other contracts, agreements or documents material to the business of the Company or any affiliate including management, service and tax sharing agreements, performance guarantees, bonds and indemnification agreements, non-compete and confidentiality agreements.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	List and copy of any contracts with independent or self-employed consultants.	<input type="checkbox"/>	<input type="checkbox"/>	
		SALES and MARKETING			
<input type="checkbox"/>	<input type="checkbox"/>	Discuss how potential customers are identified.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Discuss and provide detail regarding the average dollar sale and time requirements to close a sale.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide a list of 10 customer references with contact names and telephone numbers.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide a list of the top 10 customers for each major business segment with total sales for the past three fiscal years.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide a list of the top 10 suppliers.	<input type="checkbox"/>	<input type="checkbox"/>	

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<input type="checkbox"/>	<input type="checkbox"/>	Provide samples/ copies of all product brochures, marketing materials, promotions and advertisements.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Discuss in detail the sales pipeline process and detail the current sales backlog.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Describe the Company's major type of customer for each major segment. Respond by type of business, domestic vs. foreign, or other classification you deem relevant. Discuss if the profile of future customers will change.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Discuss the tenure of the average customer, including whether there are continuing contracts with customers. Discuss whether special terms are offered to significant customers.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	With particular emphasis on new products/services, discuss future product/service trends addressing projected marketplace, features, cost, technical aspects and competition.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	For each major business segment, provide market share information and trends.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Describe the sales and distribution strategy for domestic sales and for foreign sales (if applicable) by market segment and product line.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide a detailed listing of distribution channels/resources (personnel, OEM's, distributors, VAR's, systems integrators, etc.). Include name, address, dollar sales, percentage of total sales, commission percentage.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	For each major business segment, provide a sales breakdown (dollars and percent) by distribution channel.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide detailed information with respect to service and support.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Discuss whether future changes in sales or distribution strategies are contemplated.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Discuss any cyclical factors or seasonal factors with respect to the sale of the Company's products and services.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Describe the Customer Support and Service organization, including:	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	i. functions	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	ii. personnel	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	iii. pre-sales and technical support	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	iv. post-sales assistance	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	v. compliance resolution	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide information on complaints, efficiency and effectiveness of Service/Support function.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Discuss whether any support activities are billed to customers, on what basis, and if this is treated as cost recovery or a profit center.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Discuss any significant quality problems within the past 36 month and describe problems or returns by product line.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	With respect to competition, for each major business segment provide the following information:	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	i. describe each major competitor (size, products, profitability, financial strength, organization, etc.). Evaluate each of the competitor's strengths and weaknesses in each product line.	<input type="checkbox"/>	<input type="checkbox"/>	

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<input type="checkbox"/>	<input type="checkbox"/>	ii. Relate any significant price or cost effectiveness or the technical differentials among competing products to present and anticipated competitive market share.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	iii. Relate the most frequent basis of competition (price, quality, features, etc.) to other factors such as number of suppliers, methods of distribution, etc. that shed light on the nature and strength of competition.	<input type="checkbox"/>	<input type="checkbox"/>	
		INSURANCE			
<input type="checkbox"/>	<input type="checkbox"/>	Provide information with respect to self-insurance, if any.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide information with respect to past loss and claims experience.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide information concerning whether a change in control will cause additional cost for Workers Compensation Insurance, Unemployment Insurance or other insurance.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Discuss if there are any unusual risks, products or events that the Company has been unable to insure.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Discuss what insurance is written on a "claims made" basis.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide information concerning the Company's reporting and reserving practices.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Discuss whether any insurance policy aggregates been penetrated or exhausted.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Define who in the Company provides internal risk management and insurance management.	<input type="checkbox"/>	<input type="checkbox"/>	
		EMPLOYEE DEFERRED COMPENSATION and BENEFITS MATTERS			
<input type="checkbox"/>	<input type="checkbox"/>	All collective bargaining and labor agreements to which the Company is a party or is bound.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	A list of all officers and key employees of the Company, together with the following information on each officer or employee: (a) salary; (b) previous five years of employment history; and (c) description of present duties and responsibilities.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Description of management perquisites or other arrangements, other than those listed in items below, to include, without limitation thereto, any bonus plans or other incentive compensation arrangements maintained by the Company.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Description of any stock option or other stock appreciation, phantom stock and other similar plan maintained by the Company.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	All employee benefit plans, trusts, determination letters, IRS filings (including tax returns), filings and actuarial reports relating to any deferred compensation arrangement to which the Company is a party or by which the Company is bound.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	All documentation relating to any severance arrangement between the Company and any employee, officer, director or consultant of the Company.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	All documentation relating to any welfare benefit plan, health insurance, disability insurance, life insurance or other benefits provided to employees, officers, directors	<input type="checkbox"/>	<input type="checkbox"/>	

Requested	Submitted		Yes	No	Notes
<input type="checkbox"/>	<input type="checkbox"/>	or consultants of the Company..	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Copy of standard employment contract of the Company, for each category of employees, and indication of any difference for individual employees; and a list and copy of all individual employment contracts.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Sample copies of any standard agreements of the Company which employees are required to sign, including:	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	i. Confidentiality agreements	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	ii. Invention assignment agreements	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	iii. Conflict of interest declarations	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	iv. Noncompetition agreements	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Description of significant correspondence with labor and social security authorities for last three years.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	If not already provided in "Material Agreements/Documents", list and copy of any contracts with independent, or self-employed consultants.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	If not already provided under "Material Agreements/Documents", list and copy of any agreements currently in effect between the Company and any former officer, director or employee.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Summary of liability for termination payments to employees.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Brochures, information, booklets, policies and procedures manuals, internal regulations, or other written material given to employees or potential employees of the Company to acquaint them with the Company's business and with services, compensation and benefits offered to employees.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Summary of labor concerns, including whether any strikes are threatened or pending, all current disputes and negotiations, and all Occupational Safety and Health Administration (OSHA) issues and complaints.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	All correspondence with labor unions and all memoranda regarding communication with such labor unions or union employees.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Summary of the history for the last three years of any union negotiations, number of employees, turnover, absentee rates, and distribution.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide a summary of current compensation plans, including incentives and deferred compensation plans, with particular attention to the ten highest compensated employees.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide a summary with respect to all employment, noncompete and other agreements or contracts with any employee.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Describe any current proceedings before any State or Federal labor agency.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide the Company's Code of Conduct Manual or other personnel manual and discuss procedures that exist to monitor compliance with these policies.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	List any key management position that is currently vacant.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide information with respect to the Company's compliance with the Foreign Corrupt Practices Act.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Comment on general working conditions, employee	<input type="checkbox"/>	<input type="checkbox"/>	

Requested	Submitted		Yes	No	Notes
<input type="checkbox"/>	<input type="checkbox"/>	morale, and turnover.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Summarize the Company's policies for severance, vacations, holidays, leaves of absence, sick days, personal days, and other similar programs.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Discuss the extent to which the Company provides post-retirement medical or other benefits, including the current liability with respect to such benefits and what it is projected to be in the future.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Discuss whether any officers or directors been involved in criminal proceedings, regulatory commission violations, or major civil litigation.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide information with respect to any recent key personnel losses to competitors.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Discuss the Company's process for recruiting new employees.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Discuss any past or contemplated closings/layoffs and associated costs.	<input type="checkbox"/>	<input type="checkbox"/>	
		ENVIRONMENTAL MATTERS			
		General			
<input type="checkbox"/>	<input type="checkbox"/>	List and description of all environmental litigation or proceedings currently involving the Company, including claims, amounts, names of counsel and assessment of likely outcome.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide a general overview of environmental legislation and requirements in the Company's jurisdiction relating to the Company's activities including discussion of potential risk areas and liabilities; application of such rules in practice, political climate and experience with respect to damage claims, etc., proposed or likely future legislation.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Organization chart indicating the persons in the Company responsible for permits, contracts with the environmental authorities, reports to the management, follow up of applicable legislation, etc.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Copies of policy memoranda, programs, procedures, training courses, emergency plans, etc. relating to the environment.	<input type="checkbox"/>	<input type="checkbox"/>	
		Permits and Licenses			
<input type="checkbox"/>	<input type="checkbox"/>	List of all environmental permits and licenses required for the Company's activities including licenses with respect to manufacture, labeling and sale of products	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	History and current status of Company's compliance with permits and licenses.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Description of procedure for transfer of licenses or permits in event of a stock sale/asset sale.	<input type="checkbox"/>	<input type="checkbox"/>	
		Ownership and Use History			
<input type="checkbox"/>	<input type="checkbox"/>	Description of ownership and use history of each parcel of real property and leased property used by the Company in the last ten years.	<input type="checkbox"/>	<input type="checkbox"/>	
		Discharges			
<input type="checkbox"/>	<input type="checkbox"/>	Description of the production and storage and related environmental risks.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Description of any emissions into air or water; wastewater and other discharges; noise pollution; waste produced.	<input type="checkbox"/>	<input type="checkbox"/>	

Requested	Submitted		Yes	No	Notes
<input type="checkbox"/>	<input type="checkbox"/>	List and copy of any studies, analyses, examinations of discharges and emissions, whether produced internally or by external consultants; description of material problems or risks.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Description of removal methods of waste; cleaning methods for discharges/emissions; state of compliance with law.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	List and copies of waste removal contracts and any agreements relating to environmental matters (pollution clean-up, etc.).	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	History of any accidental discharges and results and measures taken to clean up and prevent future occurrences.	<input type="checkbox"/>	<input type="checkbox"/>	
		Relations with Authorities			
<input type="checkbox"/>	<input type="checkbox"/>	Description of Company's relationship with environmental authorities.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Description of obligations of Company to file reports or studies with authorities with copies of reports.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Description of any inquiries, inspections, examinations, investigations, etc. by environmental authorities and results; copies of documentation/correspondence; description of suspensions or withdrawals of any permits or licenses; significant correspondence for the last five years.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Description of any surrounding/adjacent conditions which could give rise to liability for the Company.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Description of insurance arrangements and environmental claims history.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Description of any injuries or illnesses of personnel, accidents during the last five years, with effect upon environmental matters.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Description of any other relevant matters with respect to the environment.	<input type="checkbox"/>	<input type="checkbox"/>	
		REAL ESTATE and EQUIPMENT			
<input type="checkbox"/>	<input type="checkbox"/>	List and description of all real property owned by the Company (and appraisals, if available); nature of the title held, and any mortgages, liens or encumbrances on the property; title documents confirming ownership; report by person authorized to conduct title searches.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	List of any property rented or leased by the Company; nature of leasehold interest; copy of the leases; description of significant or unusual clauses.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Description of compliance with land use planning and zoning laws and any other laws affecting real estate.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Limitations, if any, on the Company's real estate or business as a result of historic preservation or similar laws or regulations.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Copies of any title insurance or title searches.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	List and copy of renting/ leasing agreements with respect to machinery, equipment, automobiles not owned by the Company.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Description of compliance of use of machinery and equipment with applicable laws and regulations, and in particular, safety and environmental regulations.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	List and documents evidencing liens and security interests granted on machinery and equipment.	<input type="checkbox"/>	<input type="checkbox"/>	

Requested	Submitted		Yes	No	Notes
<input type="checkbox"/>	<input type="checkbox"/>	Describe the Company's depreciation policy.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Provide a list of surplus or idle equipment.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Summarize annual maintenance expenditures.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Discuss any related party transactions in connections with plant or facilities.	<input type="checkbox"/>	<input type="checkbox"/>	
		MISCELLANEOUS			
<input type="checkbox"/>	<input type="checkbox"/>	Copies of speeches delivered by any officer or director of the Company to trade associations, etc.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Copies of all significant articles from financial or other publications including market research, consulting reports, industry newsletters, competitive analyses, concerning the Company or its competition.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	Copies of internal or external analysis/ research regarding competitive products/ technologies.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	All customer and independent contractor complaints or demands received within the last twelve months with respect to the Company or the services thereof.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	All complaints of residents and business establishments near any of the facilities involved in the business of the Company received within the last twelve months.	<input type="checkbox"/>	<input type="checkbox"/>	
<input type="checkbox"/>	<input type="checkbox"/>	All complaints to the company received within the last twelve months regarding any employee or agent associated with the Company.	<input type="checkbox"/>	<input type="checkbox"/>	