The Money's in the Bank Once the Money's in the Bank: Back-up Plans

I recently have had conversations with several entrepreneurs who were scrambling for investment for payroll, commitments made to vendors, or who thought they'd have a paycheck and lo and behold "it's not going to happen this month." This reminds me of other conversations over the past 20 years when a VC check didn't arrive to close a round because something odd happened at the 11th hour that spooked the partner on the deal or a VC signed a term sheet without having done due diligence ahead of the term sheet and the founders were star struck over who the VC was versus what their process was and how solid was that term sheet really.

What all this has led me to is two things: 1) Hope is not a strategy and 2) The money's not in the bank and can't be spent until the money's in the bank. I have seen too many entrepreneurs believe wholeheartedly in an angel syndicate or a venture firm and not have a back-up plan should that deal not happen. The latest case is a family office investing $1.5M into a company. A tornado hit the region where the FO Leader lived and then a family member got very sick right after that. Needless to say, that person's focus is not on you and your company but on their shelter and family member (rightfully so). In this situation there were other family offices interested in the deal but the founder put a hold on these since this was the "sure near term one." There's never a sure one. Stuff happens, life happens, interest wanes. And there's bad luck in business just as there's good luck. When it comes to financing I have not seen very many good luck scenarios versus bad luck scenarios. That's because you need the money far more than the investor needs to invest in your company. Always remember that. That's why I always recommend managing investor fundraising exactly as you manage enterprise sales with all being worked but with a different probability of close for each investor. Keep as many balls juggling and moving forward as you can (oh, yes, and run your business too!) until you actually have money in the bank. And by the way, don't accrue debt thinking you will pay that back after funding closes. Investors are not putting money in to cover the past investments but are investing in the future.

How many entrepreneurs have not made a payroll, have not paid the IRS or the state tax liability on payroll ,have liquidated their 401K to cover payments thinking they'd just put that money back when sales or investors come through, or have foregone any funds for their own living expenses only to find that their credit now sucks and they're paying interest only on their credit cards and not able to refinance their high priced mortgage never mind putting their 401K funds back in place. It's a slippery slope and one that can ruin personal relationships and founder partnerships. Again, hope is NOT a strategy. When you liquidate that 401K just assume that money will never get put back. I have seen a founder do the smart thing and arrange a line of credit secured against an asset (their home is the most typical) before they're in trouble since interest rates are quite low on these and it's easier to have $100K or $200K lined up before you quit your job as a line of defense against a missed payroll or a sliding fundraising date. By the way, ask your VC for a bridge loan-that's often a good way of testing their intent versus their using the “no shop” timeframe to see if they really want to do the deal with you.

If you’re an investor, be open with the entrepreneur where you’re really at with respect to funding and any snafus or issues you’re personally dealing with that might affect timing of your investment. Being honest about your probability of doing a deal will win you lots of friends in the greater entrepreneurial community. A “fast no” is much better than a “slow maybe, let’s see how you evolve.” It’s a small town so telling an entrepreneur how long you take in your due diligence, that you have 3 issues you want to see addressed, or that you want someone else to lead the round that you like to follow will pay you back in many ways re: word of mouth from entrepreneurs recommended investors and other angels who like doing deals with you.