

# Alaska Angel Conference 2020

- ▶ October 23, 2020  
What is due diligence? -Will  
Fowler, Signal Rock



[akangelconference.com](http://akangelconference.com)  
[@AlaskaAngel](https://twitter.com/AlaskaAngel)

# How does AAC work?

- Alaska Crowdfunding Act makes equity investing accessible to Alaskans
  - Investors commit \$5,500 to an LLC.
- Entrepreneurs apply to be a part of a 12-week conference.
- Investors learn how to conduct due diligence on applicants.
- LLC makes an equity investment in one startup.



[akangelconference.com](http://akangelconference.com)  
[@AlaskaAngel](https://twitter.com/AlaskaAngel)

# Alaska Angel Conference 2019

- Key Accomplishments
  - Created 10 new angel investors
  - Some of those new investors invested an additional \$100,000 shortly after the event
  - Built new networks between investors and entrepreneurs
  - Helped startups learn about funding options



[akangelconference.com](http://akangelconference.com)  
[@AlaskaAngel](https://twitter.com/AlaskaAngel)

# AAC 2020 Schedule

WORKSHOPS	SELECTION	FINAL EVENT
Oct 9 <sup>th</sup> – Feb 4 <sup>th</sup> Wed 5:30- 7:00pm  In Person & Online	Oct 9 <sup>th</sup> – Feb 4 <sup>th</sup> Wed 5:30- 7:00pm  In Person & Online	April 23 <sup>rd</sup>  Invest \$100K+



[akangelconference.com](http://akangelconference.com)  
[@AlaskaAngel](https://twitter.com/AlaskaAngel)

# Due Diligence for Angel Investors

Will Fowler – Signal Rock Capital



SIGNAL ROCK  
TOOLS FOR EARLY STAGE INVESTORS

# Will Fowler

Signal Rock Capital Founder  
Idaho SBDC Associate Director





# Will's Background and Experience



GRUBSTAKES VENTURES



# Experience

30+ Holdings

5 Member Managed Funds

Administered: Screening, Fund,  
Syndicate, SPVs

SLO Angel Conference

SD Angel Conference

2 Accelerator/Incubators



SIGNAL ROCK  
TOOLS FOR EARLY STAGE INVESTORS



# Due Diligence for Angel Investors



SIGNAL ROCK  
TOOLS FOR EARLY STAGE INVESTORS

# The Startup World



SIGNAL ROCK  
TOOLS FOR EARLY STAGE INVESTORS



# How Startups View Themselves





# How We View Them



# What it's Really Like



SIGNAL ROCK  
TOOLS FOR EARLY STAGE INVESTORS

# How Investors View Themselves



SIGNAL ROCK  
TOOLS FOR EARLY STAGE INVESTORS

# How Investors are Viewed by Others



SIGNAL ROCK  
TOOLS FOR EARLY STAGE INVESTORS

# What it's Really Like



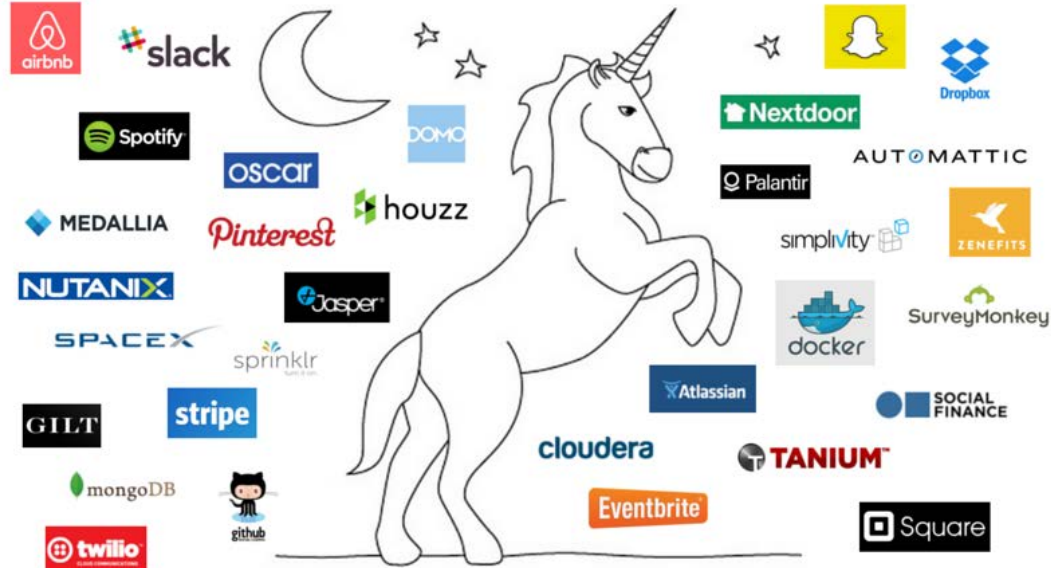


# The Most Likely Outcome Is FAILURE



# How do we Make Money?

Exit or Bust



# EXIT

A "Cash Out" event, where the company is sold privately or publicly





# Angel Investing Data

70%: Fail or return less than 1X

85%: Of returns come from less than 10%

21%: Average IRR

2.5X: Average Multiple



# Deal/Terms Vocab





# Fundraising Round

When a company wants to raise equity financing  
– they determine a “ROUND.”

Series Seed, Series A, Series B, Series C, etc..





# Fundraising Vehicle

When a company wants to raise equity financing  
– they choose a VEHICLE for that “ROUND.”

Stock, Convertible Note, SAFE, KISS, Etc...



# Priced Round / Stock

Shares of a company



SIGNAL ROCK  
TOOLS FOR EARLY STAGE INVESTORS



# Convertible Note

A loan that converts to equity based on predetermined triggers.



# SAFE

Simple Agreement For Future Equity: Much like a convertible note – but lighter.



# Why the Vehicle Matters



SIGNAL ROCK  
TOOLS FOR EARLY STAGE INVESTORS



# Taxes for Investors

Tax Exclusion 1202:

Any qualified “small business stock” that is held for at least 5 years is **EXCLUDED** from Capital Gains Tax.



# Convertibles

Delay the start of the clock for 1202



SIGNAL ROCK  
TOOLS FOR EARLY STAGE INVESTORS

**Priced Rounds can be  
Better for Investors  
(follow your market  
demand)**



**SIGNAL ROCK**  
TOOLS FOR EARLY STAGE INVESTORS

# VALUATION

Invested amount/Post Money Valuation = Ownership %





# Valuation Example

Your Raise: \$1M

Your PRE money valuation: \$3M

Your POST money valuation: \$4M

Total % Sold =  $\$1\text{M}/\$4\text{M}$  (25%)

**Lead INVESTED \$100K**

**Total ownership =  $\$100\text{K}/\$4\text{M}$  (2.5%)**





# DILUTION

The amount to which your ownership is reduced by subsequent rounds/vehicles/valuations



**Expect to be diluted 50%**





# Dilution Example

Company is Acquired for \$30M

You've been DILUTED 50% (1.25%)

**Return = \$375,000**

Company Raises: \$1M

Company PRE money valuation: \$3M

Company POST money valuation: \$4M

Total % Sold = \$1M/\$4M (25%)

You Invested \$100K

Total ownership = \$100K/\$4M (2.5%)



# Questions?



SIGNAL ROCK  
TOOLS FOR EARLY STAGE INVESTORS

# The Process of Investing





# Standard Process

Deal Flow

Screening

Due Diligence

Closing





# Deal Flow

Incoming Deals to Consider for Investment





# Screening

The “Sniff” Test on whether the opportunity is a good fit.







# Due Diligence

In depth look at the company

Validate the assumptions of the company

Determine major risk factors





# Closing

Negotiate/Agree on terms

Sign Paperwork

Send Money

Receive Certificate



# Due Diligence



SIGNAL ROCK  
TOOLS FOR EARLY STAGE INVESTORS



# The purpose of Due Diligence

To identify risks

To understand the team

To validate the startup assumptions/assertions





# What do You Need to Believe is True at the End?

1. Solid Leadership
2. Opportunity for a Sizable Return
3. Team's Ability to Execute
4. Fair Terms





# What the Startups are asking of You?

1. For You to Believe in Them
2. To Accept the Risk with \$\$\$ and Time
3. To be Patient
4. To Focus on the End-Game



Do they have a lead investor?



Do they have an attorney?



SIGNAL ROCK  
TOOLS FOR EARLY STAGE INVESTORS



# 4 things to know about Due Diligence



SIGNAL ROCK  
TOOLS FOR EARLY STAGE INVESTORS



# Step 1: Focus on what is important

1. Team = Team and Ability to Execute
2. Upside = Market/Business Model
3. Impact = Traction/Progress/Use of Funds



# 2. Don't be an Asshole

Even when they are being assholes





## **Step 3: Understand their baby is ugly and will die. Be nice about it.**

No business plan survives first contact with customers

They will change course many times before exit

They will make huge mistakes

They will need to raise more money





## Step 4: Understand the Terms

Entity

Vehicle

Valuation

Anti-Dilution

Preferred Stock



# Make it Easy

Be Responsive Be Patient Be Thorough  
Be Nice



SIGNAL ROCK  
TOOLS FOR EARLY STAGE INVESTORS

# Now for the Actual Process of Due Diligence



SIGNAL ROCK  
TOOLS FOR EARLY STAGE INVESTORS

1. Validate
2. Discover
3. Decide







# The Process of Due Diligence

## Organizational Process

- Decide on DD lead
- Set deadline for process completion
- Assign team to areas (Finances, Market, Customers, Leadership, Business Model, Terms, ect)
- Set meeting schedule
- Communicate all of the above to Startup

## Discovery/Research Process

- Send Document Request (see next slide)
- Call initial meeting – establish major risks based on document review
- Meet with CEO/Site Visit
- Conduct validation work (market research, customer calls, financial/operational review)
- Call team meeting to discuss risks and go/no go decision (or request additional information)
- Make a recommendation/Present findings





# The Big List

- Tax Returns
- Pro Forma
- Budget
- P&L/Balance Sheet/Cash Flow s
- Cap Table
- Detailed use of Funds
- Customer List and Contact Info
- Org Chart (Current and Proposed)
- Team resumes/Bios
- Business Plan
- Detailed Offering Terms



# 2 Likely Outcomes



Failure is the most likely  
outcome of any  
investment



SIGNAL ROCK  
TOOLS FOR EARLY STAGE INVESTORS

Raising more money is  
the other likely outcome



SIGNAL ROCK  
TOOLS FOR EARLY STAGE INVESTORS

# Questions?



SIGNAL ROCK  
TOOLS FOR EARLY STAGE INVESTORS

# Thank You

[will@signalrockcapital.com](mailto:will@signalrockcapital.com)



**SIGNAL ROCK**  
TOOLS FOR EARLY STAGE INVESTORS



# Thank you for joining us!

Join us October 30 at 5:30 PM for “Pitch  
Deconstruction”

Thank you Will Fowler, Signal Rock



[akangelconference.com](http://akangelconference.com)  
[@AlaskaAngel](https://twitter.com/AlaskaAngel)