

EBAN Tool Kit

Introduction to business angels and business angels network activities in Europe

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Foreword

“This publication gives you an introduction to business angel activity in Europe. By providing entrepreneurs with two essential elements, finance and advice, business angels contribute to a more innovative and entrepreneurial Europe. This is important for the European Commission because we believe that innovation and entrepreneurship are the only lasting way to improve our competitiveness, growth and employment.

The importance of business angel financing for small firms is widely recognised by entrepreneurs and investors. The European Business Angel Network (EBAN) and its member organisations have done valuable work in raising awareness about business angels across Europe.

For its part the European Commission is committed to the development of risk capital financing in Europe and we view business angel investments as an essential part of early-stage business development for many firms with growth potential. Our policy is to help the development of business angel investments by identifying best practices, removing obstacles and promoting cooperation among investors – and we encourage the Member States to do the same.

Business angel networks add value by matching entrepreneurs and angels, and by increasing trust through codes of conduct. The increasing number of angel networks in Member States with mature financial systems indicates that in many cases the business angel market is reaching a stage where finding a sustainable business model is more important than expansion. This provides new challenges for angel networks.

Although business angel networks are mostly local and regional, we see also an opportunity for a more pan-European approach. Very few countries have domestic resources to finance, for example, medical or biotechnology companies beyond the first financing round and investor cooperation is needed. Syndicated investments among angels and co-investment schemes between angels and venture capital funds provide both synergy and leverage. Furthermore, cross-border risk capital investments benefit recipient firms by giving them an opportunity to achieve a real European dimension”.



Timo Summa

Director, Past SME Envoy 2003-2005

European Commission, DG Enterprise & Industry

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CHAPTER 1: DEFINITIONS AND CONCEPTS

I) Stage / Type of financing definitions

Seed	Financing provided to research, assess and develop an initial concept before a business has reached start-up phase.
Start-up	Financing provided to companies for product development and initial marketing. Companies may be in the process of being set up or may have been in business for a short time, but have not sold their product commercially.
Other early stage	Financing to companies that have completed the product development stage and require further funds to initiate commercial manufacturing and sales. They will not yet generate a profit.
Expansion	Financing provided for the growth and expansion of an operating company, which may or may not be breaking even or trading profitably. Capital may be used to finance increased production capacity, market or product development, and/or to provide additional working capital.
Venture capital	Provision of equity for generally young, unquoted companies with high growth potential and high commercial uncertainty – ranges from seed to late stage investment with key feature of being “hands-on” involvement by the finance provider.
Equity	Ownership interest in a company or corporation that is represented by the shares of common or preferred stock held by the investors.
Equity stake	An equity ownership position in the company that is provided to a funding source, usually lenders or other investors, as compensation for providing management consulting, financing, or miscellaneous services.
Prospectus	A disclosure document prepared to provide potential investors with detailed information regarding the purchase of securities, including debt or equity offerings.
Mezzanine	Finance used, mainly in larger deals in profitable companies, which combines a small amount of equity with loans secured, where possible, on the company’s assets. Often used as expansion capital.

II) Business angel and business angel network definitions

Business angel (BA)	A business angel is as a private individual who invests part of his personal assets in a start-up and also shares his personal business management experience with the entrepreneur.
Virgin Angel	Individuals with funds available who are looking to make their first investment.
Latent angel	Rich individual who has made an angel investment, but not in the past three years.
Wealth maximising angel	Rich individual and experienced businessman who invests in several businesses for capital gain exclusively.
Entrepreneur angel	Very rich, entrepreneurial individual who backs a number of businesses for both fun and as a better alternative to stock market investment.
Income seeking angel	Less affluent individual who invests some funds in a business to generate an income or even a job for himself or herself.
Corporate angel	Companies that make regular large angel type investments often for majority stakes.
Business angels network (BAN) or angel portal:	An organisation whose aim is to facilitate the matching of entrepreneurs (looking for venture capital) with business angels. BANs tend to remain neutral and generally refrain from formally evaluating business plans or angels. BANs make a market place for matching services.
Matching process:	Any action aimed at facilitating encounters between business angels and entrepreneurs.
Deal / matching:	The conclusion of an agreement whereby a business angel invests in a company's stock.
Investment Forum:	A meeting in which entrepreneurs each have 15–20 minutes to present their business project to a range of business angels who have been pre-selected or have previously expressed an interest in one or more of the projects.
Yield rate	The number of investment opportunities that are brought to the attention of investors (by the business angel network) and which resulted in an investment ¹ .
Business angels Syndication:	The gathering of several business angels into an informal consortium for the purpose of creating a critical mass of funds above what each business angel could—or would be prepared to—invest. This term also applies to the pooling of competencies in order to offer more managerial skills than any individual business angel could display.
Serial angel:	A business angel who closes two or more investment deals per year.
Investment readiness:	A privileged moment in time when entrepreneurs are ready to meet and negotiate with business angels, as they understand what the prerequisites of the involvement of the business angel in a company are. (Also applies to other types of investors when the entrepreneur knows what is expected from the different types of financing bodies.
Exit route:	The ways in which business angels sell their stake in an investee business. Possible exit routes include management buyouts, sale of stock to another business angel or a formal venture capital firm and—in few cases—listing on the stock market.

¹ Sohl Jeffrey E. and Sommer Bruce, "Angel investing: changing strategies during volatile times", p.9 2002.

Sophisticated Investor:	An investor recognised by a third party as someone who is sufficiently knowledgeable to understand the risks involved with investing in an unquoted company. The individual has already made previous investments and has a long history of investing in a range of financial instruments.
Equity Gap	Gap in the financial market in the area of SME financing, especially in the seed phase.
Due diligence	Process of evaluation of a project by a potential investor based on material facts.
Co-investment fund	<p>An investment fund dedicated to the provision of equity finance to SMEs in which business angels have committed to invest provided that they are able to source a co-investor. The co-investment fund invests under the same terms and conditions as the angels, on a pari-passu basis. The fund is run by an independent fund manager who uses to a large extent the due diligence work carried out by the business angels in order to reduce costs. Funds can be managed by business angels, public authorities, venture capitalists, private equity groups, or any combination of the above.</p> <p>In some cases (side-car funds), angels that are already part of an investment structure (BAN) pool resources into a fund for specific investments, in parallel to the activities operated at the BAN level.</p>
Early Stage Fund	Early stage venture capital and seed funds are those who invest in the equity gap (500.000€ to 3 million€), i.e. making a maximum of 3 million€ investment per company in young innovative SMEs across Europe.

CHAPTER 2: ABOUT BUSINESS ANGELS

I) Social, professional and personal profile of a business angel

A) General profile

The various surveys conducted on business angel profiles have yielded the following results:

- A majority of males;
- Aged between 35 and 65;
- Successful experience as an entrepreneur or a manager;
- Available at least one day a week to advise trustworthy entrepreneurs.
- Prepared to invest 25,000€ – 250,000€ or the equivalent of 15% of their own funds in a single deal. In the UK, the investment can be up to 400,000€² (in the UK real estate is not included in the calculation of net personal worth)³;
- Contribute their network of personal contacts in business and company finance circles.

Business angels generally feel that the longest they are prepared to commute to investee businesses is up to one half-day trip. However, the attitude of business angels is gradually changing with the evolution of new communication technologies and lower travel costs. Cross border initiatives or transnational networks (Go Beyond Ltd, MEDIA DEALS, etc.) have emerged in recent years.

Some of the benefits of having business angels on board a company are:

- 2 wings: business angels provide not only capital but also mentoring/coaching
- Invest early – take a higher risk
- Invest in different sectors
- More flexible and reactive than other investors
- BAs give access to networks and new potential customers
- BAs acts as an ambassador for the business = credibility
- Make easier to raise follow-on funding

² In the UK, BA investments vary between 15.000€ and 400.000€ though the average tends to be below 80.000€.

³ Mason Prof. Colin M., The Supply of Business Angel Finance: a survey of investors registered with NBAN (UK), 12 November 1999.

Stages in the Business Angel's Investment Decision⁴:

Deal origination	The investor becomes aware of the opportunity – typically through one of the following channels: chance encounter, referral from business associates or other individuals or organisations in their network, or personal search.
Deal evaluation	Two stages: (i) Initial screening/first impressions: key considerations are the 'fit' with the investor's personal investment criteria, their knowledge of the industry/market and their overall impression of the potential of the proposal. Also influenced by the source of the referral. (ii) Detailed evaluation: the investor will examine the business plan in detail, consult with associates, will meet the principals, take up references, and research the proposal. The decision will be influenced by the potential of the industry, the business idea, impressions of the principals and potential financial rewards.
Negotiation and contracting	Negotiations with the entrepreneur over valuation, deal. Main factor is pricing.
Post-investment involvement	Investor is likely to become involved with the business in some kind of hands-on capacity, including advice and mentoring, networking, functional input and member of board. Degree of involvement may vary according to the stage of business development and the performance of the business.
Harvesting	Exit from the business, either because it fails or by selling their shares to another investor. Investors normally exit from successful investments by means of a trade sale.

Some of the trends identified today are:

- An increasing number of angels and angel networks on the market
- Angels investing smaller amounts in larger deals as venture capitalist move further along the financial supply chain
- More investments in clean technologies and industries related to sustainable development
- More investments are made in syndication or through co-investment funds
- More interest for cross border investments

What should be kept in mind is that despite the characteristics mentioned above, business angels remain a heterogeneous group. More detailed information sorted by country follows and illustrates this diversity.

⁴ Mason Colin M, "Informal sources of venture finance", Hunter Centre for Entrepreneurship, University of Strathclyde, August 2005, To be included in Simon Parker (ed) *The Life Cycle of Entrepreneurial Ventures: Volume 3. International Handbook on Entrepreneurship*, Kluwer, 2006.

B) Characteristics of business angels in Europe

❖ Business angels – characteristics, investment criteria and expectations in Europe⁵

Type	Characteristics	Wealth and level of investment	Investment objectives	Main criterion for investment	Investment location	Other factors
Entrepreneur Angel	The most active and experienced angel	Worth over €1.6m, with annual income €167K. Invest over €837K.	Financial gain, but also fun and satisfaction	Personality of company founder	Not important	More open than other angels to investing outside of its own field of experience
Corporate Angel	Companies (or directors) making angel-type investments	Almost 40% of survey group had invested over €837K in new ventures	Financial gain, but this is often less than earned by individual angels	Personality of founder or manager	Prefer to invest close to location	Own experience in sector is important
Income seeking angel	Active individual investors, but with lower level of investments than other types	30% of group worth less than €167K. Invest €40-84K	Create a job for self and financial return	Personality of founder or manager	Not important	
Wealth maximising	Private individuals with several investments in new ventures	80% of group worth over €837k. Invest €40-167K	Financial gain and job for self	Personality of founder or manager	Not Important	Opportunities for co-investment; access to knowledge of other investors
Latent	Inactive for the past three years, but having made at least one investment before that	50% of group have over €167 available for investment; some much more	High financial return and job for self	Personality of founder or manager	Strong preference for venture close to angel	Clearly available exit routes
Virgin	Not yet made an investment in an unquoted venture	Less funds than all other angel types, but this not felt to be a restriction	Higher return than from stock market; also job or income for self	Personality of founder or manager	Prefer to invest close to location of angel	25% say own experience in sector is important

⁵ CORDIS Innovation papers NO 12 “Informal investors and high-tech entrepreneurship”, p. 48.

Diane Mulcahy⁶ classifies angels in the following categories:

1. The “technology guru”: angels with industry expertise, attracted by your technology and who want to work with you to succeed;
2. The “teacher” who is generally a formal entrepreneur and acts as a mentor;
3. The “status seeker”;
4. The “investor” making strictly rational decisions based on assessment of financial returns;
5. The “portfolio manager” with no entrepreneurial experience but wealthy, who believe that angel investing is a good financial activity;
6. The “virgin angel” who has never made an investment and therefore are unpredictable.

❖ What does an investment imply for a business angel?

Colin Mason from the Strathclyde Hunter Centre for Entrepreneurship made a presentation during the 4X4 Symposium on Entrepreneurship in Louvain-la-Neuve (B) in November 2003 on what it implies to be a business angel:

- Being a business angel is high risk: only invest if you can afford to lose;
- There is potential for very high reward: angel investing is a very useful part of an investment portfolio;
- Don't skimp on due diligence: this is the biggest post-investment regret of angels;
- Don't “fall in love” with your investments: be ruthless with your poorly performing investments – consider the opportunity costs of the time you spend with these investments;
- Most angels have a portfolio of less than 5 investments: this is too small given the likely success: failure rate and encourages a cautious outlook;
- Successful investments do not share a common set of characteristics – there is no recipe for successful investing;
- “Deep pockets” are needed for successful investing: bigger deals and follow-on funding are linked to investment success;
- Consider investing as part of an angel syndicate: deeper pockets, better deal flow, bigger investments, wide range of expertise for tap for due diligence and post investment support, opportunity to learn more from experienced investors, social dimension;
- Establish a relationship with venture capital funds: co-investing with VC funds did generate a high proportion of successful investments;
- Be patient: don't panic when the failures start to emerge;
- Need to develop an exit strategy at an early stage – develop relationships with possible trade buyers.

❖ Business angels' primary motivation for investment across Europe

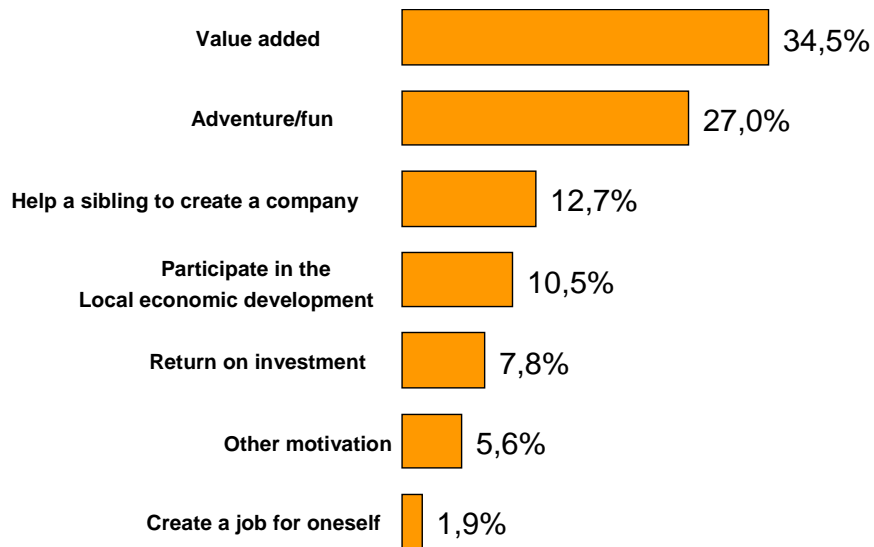
According to the research conducted by EBAN in 2008 on angel market activities in 2007, reasons why angels invest are the following:

⁶ Mulcahy Diane, “Venturing forward – A practical guide to raising equity capital in Ireland”, Oak Tree Press, 2005, p.95

1. Financial return
2. Personal satisfaction
3. Diversification of portfolio
4. Economic development
5. Self-employment

❖ Business angels – characteristics and investment criteria in France

Business angels' primary motivation for investment in France⁷



❖ Sector of investment of business angels in France⁸

The investments made in companies financed in 2007 have been done in the following sectors:

1. ICT/internet/e-Commerce (33%)
2. Software/Multimedia (30%)
3. Industry (30%)
4. Life sciences / biotech (30%)

Other sectors mentioned were: construction, press, consultants, tourism and leisure.

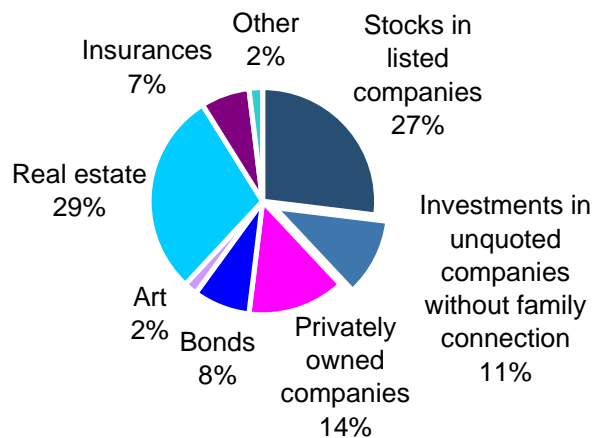
❖ Business angels – characteristics and investment criteria in Sweden

Below is the result of a 2005 study from Lund University⁹ on the origins of the net worth of Swedish angels:

⁷ Results of the 2003 French business angel survey conducted by France Angels, www.franceangels.org

⁸ EBAN Directory of Networks 2008, www.eban.org

⁹ Månsson N. and Lanström H. "Business Angels in a Changing Economy" Lunds University, Sweden, 2005



A 2005 study of the characteristics of 400 Swedish angel investors highlighted the following¹⁰:

- 96% were men
- At least 90% had started a company
- On average the investors had 11 years experience in the informal venture capital market
- 77% had earned their money through profits in privately-owned companies or by selling a company
- Early stage investments represented 11% of their total assets invested
- 49% had a household income of over 110.000€ while 10% had a household income of over 444.000€
- 59% had an active role in the companies.

❖ Business angels – characteristics and investment criteria in Spain

In Spain, business angels had the following characteristics in 2006¹¹:

- 70% men and 30% women
- Average age of 40 years old
- 87% of business angels had another daily activity
- 42% admitted to not having sufficient knowledge to initiative a capitalisation process
- The volume of investment per project was 18.5000€ to 36.000€

❖ Business angels' investing characteristics in the United Kingdom

A survey study conducted by Stephanie Macht, from the Newcastle Business School, Northumbria

¹⁰ Månsson N. and Lanström H. "Business Angels in a Changing Economy" Lunds University, Sweden, 2005

¹¹ ESBAN "Los business angels en España, una nueva via de financiación para la PYME", Estudio para el fomento de las redes de business angels en España, p.52, 2006

University about the “The Post-Investment Period of Business Angels - Involvement and Impact”¹² revealed the following:

- ✓ A vast majority of business angels (i.e. over 70%) have both founded and owned a small business before, while at the same time calling themselves entrepreneurs.
- ✓ Business angels are highly motivated to invest because of financial considerations (i.e. financial return on investment). However, at the same time, they display an almost equal enthusiasm to invest due to non-financial factors.
- ✓ Business angels tend to invest in young companies, but not in pre-seed businesses and also prefer to stay away from turnaround situations.
- ✓ Business angels tend to become involved in companies located in close proximity to their home place.
- ✓ Only a minority (just over 30%) stay within industries in which they have had prior work experience. The remaining respondents have made at least one investment in an industry in which they have never worked before. For some angels, a vast majority of their investee companies operates in industries in which they are not experienced themselves.
- ✓ Business angels think that their involvement in their investee companies is very active.
- ✓ Business angels become mainly involved post-investment in order to support a particular entrepreneur and in order to reduce their own risk. Further strong motivational factors are the enjoyment of being related to entrepreneurial ventures in general and enjoying the involvement, whereas taking control is the least important motivator.
- ✓ Most business angels have a structured approach to spending time with their investee, i.e. they become involved on a regular basis and not only on occasions when their input is desperately needed. In addition, their high degree of activeness suggests a very high frequency of contact (i.e. more than one day per month, often even more than one day per week).
- ✓ Nearly all business angels provide their investee with the following resources: skills, networks of contact, experience and knowledge. Most investors further indicated that the entrepreneurs are receptive to their resource provision in that they internalise and re-use these resources.
- ✓ A vast majority of business angels (just under 87%) do not require the investee to ask them to be involved; instead, they offer their involvement to the investee voluntarily.
- ✓ Only one quarter of responding business angels have ever received some kind of formal training in investing or mentoring.
- ✓ Business angels tend to not become involved in replacing management team members, chairmanship of the board and being employed by the investee. On the other hand, only very few angels are not involved in responsiveness to requests, moral support, as well as being a friend and sounding board to the management.
- ✓ In business angels' viewpoint, all activities they undertake for their investee impact at least moderately positively upon the company.
- ✓ Strategic activities (e.g. formulating strategies) impact most positively upon investees' efficiency and success or survival.
- ✓ Business angels' investment in more than one subsequent round impacts most positively upon an investee's profile in the eyes of external parties.
- ✓ The least positive impact can be found for activities related to business angels becoming employed with their investee (i.e. being a literal employee, being an employed consultant and becoming a member of the management team).

¹² Macht Stephanie, “The Post-Investment Period of Business Angels - Involvement and Impact”, Newcastle Business School”, New Castle Business School, Northumbria University, United Kingdom, 2007.

- ✓ Over 40 percent of business angels think that both their involvement and their money are equally important to their investee companies, whereas around a quarter each consider either their money or their involvement to be most important.
- ✓ Most angel investors think that involvement is equally important, no matter what age the company is.
- ✓ Nearly half of business angels each believe that their involvement is most important either independent of the investee management's level of experience or in the situation of an inexperienced management team.
- ✓ Entrepreneurial management teams are rather responsive to their business angels' involvement activities.
- ✓ When asked about their own view on their major impact, business angels gave a wide variety of responses, which can be catalogued under the following categories: Financial inputs, other inputs, involvement activities and other ongoing processes.

C) Characteristics of business angels in the United States

The first study on returns on angels' investments was carried out in 2007 by Robert Wiltbank from the Willamette University and Warren Boeker from the University of Washington in November 2007 and supported by the Ewing Marion Kauffman Foundation and Angel Capital Education Foundation¹³. The main findings were the following: The study pointed out the characteristics of Investors in Angel Groups in the US being the following:

- ✓ The typical group-affiliated angel investor has been investing for just over nine years on -average, and has made slightly more than one investment per year.
- ✓ The responses collected from the study consisted of 86 percent male participants who were on average, 56 years old.
- ✓ Ninety-nine percent of them hold college degrees; more than half hold graduate degrees.

Entrepreneurial experience is the norm among the investors in this sample.

- ✓ As a group, the risk taken by these angels is rewarded with overall returns—2.6X in 3.5 years;
- ✓ The angel investors may positively influence their rates of return by making wise decisions about due diligence avoiding ventures in unfamiliar industries, follow-on investments, and productively participating in the ventures post-investment;
- ✓ The angel investing is a risky undertaking: as with other forms of equity investment, relatively few ventures earn very large returns;
- ✓ In any particular venture, an angel investor is more likely to lose than to make money, and a significant portion of the angel investors in this sample experienced a return less than 1X.
- ✓ Angel investing can be done well in the pursuit of legitimate financial returns.
- ✓

¹³ Wiltbank Robert, Willamette University and Boeker Warren, University of Washington, "Returns of Angels Investors in Groups", supported by the Ewing Marion Kauffman Foundation and Angel Capital Education Foundation, November 2007. The report analyses results received only from those investments from which the investor has exited.

❖ Investment Characteristics

Concerning the timing of Angel Investment, group angel investors interviewed made very early-stage investments (34% of the deals were done in the seed stage and 41 % in the start-up stage, and 18% in the early-growth stage, and only 7% in the later stage).

Also, it worth noticing that in the sample considered 45 % of the ventures had no revenue at the time the group angel investors made their investments, while the median revenue for all of the ventures at the time of the angel investment was of only \$125,000.

Investment Sizes:

Each individual investor's median investment was \$50,000, and the mean investment was \$191,000, per venture¹⁴.

Industries of investment:

As in traditional venture capital, software is the lead component, followed by health care and biotech investments. Also, it was noticed that industry differences are not a major factor in the returns found in the sample. Other frequent investment sectors are energy, clean-tech, environment, manufacturing, food and retails, business and consumer products & services, creative industries, etc.

Trends that bear watching in the United States are¹⁵:

- The evolution of the relationship between business angels and venture capitalists,
- The institutionalisation of the VC market,
- Evolution of the yield rates (The annual rate of return on an investment, expressed as a percentage),
- Increasing number of angel groups and formal angel alliances.

A comparison between the United State and European angel market: characteristics¹⁶

2007	EU	US
Networks	297	270
For profit	36%	47%
Estimate nr of angels	75.000	250.000
Average investment per round	165.000 €	210.500 €
Total estimate invested annually	3 billion € ¹⁷	20 billion € ¹⁸

¹⁴ This includes all follow-on investment plus the initial investment, though followon investing was relatively rare in this sample.

¹⁵ Sohl Jeffrey E., "International trends in angel investing». Presentation at the EBAN Annual Congress of April 2006.

¹⁶ EBAN Winter University 2008, Brigitte Baumann and Claire Munck intervention. www.eban.org

¹⁷ EBAN estimates 2008.

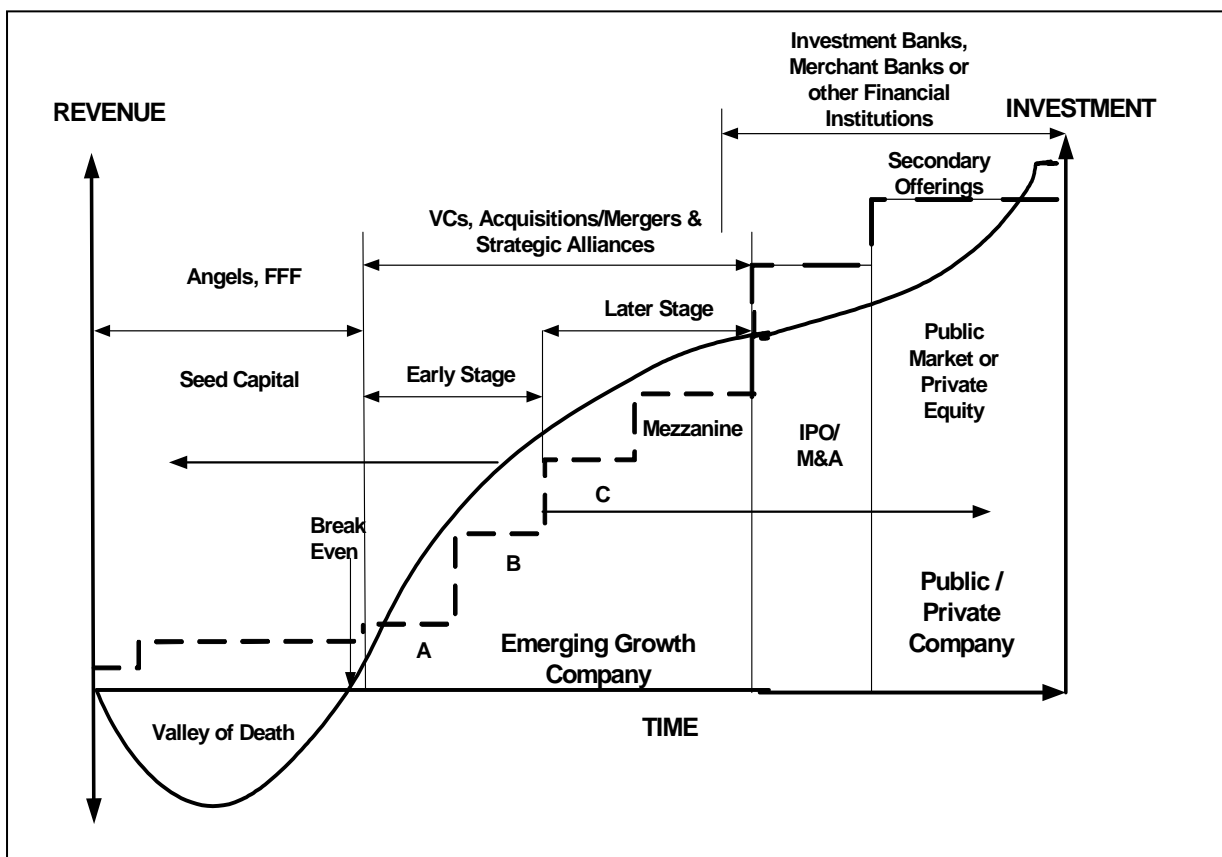
¹⁸ Center for Venture Research estimates 2008.

II) Operational environment of the business angel

Business angels have a role in:

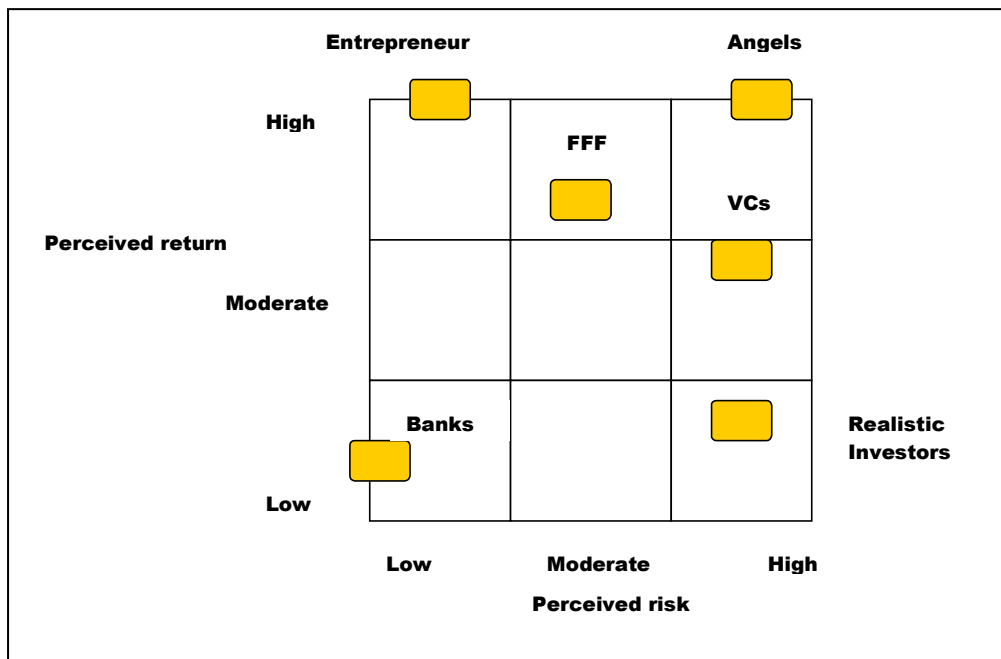
- Filling the equity gap in the start-up phase;
- Investing in companies at a stage where VCs are no longer active;
- Being an integral part of the chain of integrated finance tools;
- Contributing to the culture of entrepreneurship in the region;
- Agglomerating the existing investment capital in a region.

The following graphs illustrate the stage in which the business angels intervene and the presence of the equity gap between the different sources of finance for the entrepreneur¹⁹.



¹⁹ Source: US Department of Commerce –ITA.

Business angels and their relation to risk²⁰:



As venture capitalists are moving up the ladder to higher amounts, business angels are increasingly active in the very early stage of companies, and are required to invest in several rounds of financing for the same company as there is a lack of follow-on investment. This new equity gap concerns amounts from 1 million to 3 million €, depending on the country.

III) Ways business angels exit their investments

There are several ways of exiting an investment:

1. a management buy-out: when part of the staff buys the shares
2. a trade sale: when the company is bought out by a bigger firm or competitor;
3. an IPO: rarely

By definition, companies seeking investment from Business Angels will not have their shares traded on any recognised Stock Exchange, but if the company is successful it may subsequently float on the stock market. Alternatively, it may be sold to another business (a trade sale). Either of these routes, or the purchase of your shares by another shareholder, will enable you to cash in all or part of your investment. It is important to define your possible exit routes and the basis on which the price for shareholder-to-shareholder deals will be struck. Professional advice is strongly recommended.

²⁰ Source: US Department of Commerce –ITA / FFF: Friends, Family Fools; VC: Venture capitalist.

The results from the survey conducted by Colin Mason²¹ show the following:

1. Trade sales dominate (26%) both high and low performing investments;
2. IPO's are the exception (7%) and largely confined to investments generating returns in excess of 50%;
3. The sale of shares to existing shareholders (16%) and to new third party (10%) is mainly restricted to the more moderately performing investments.

In terms of characteristics of the exit:

- The average holding period was 4 years;
- The holding period for loss-making and break-even investments was 2 years;
- The holding period for the most successful investments was 4 years;
- The holding period for moderately performing investments was 6 years.

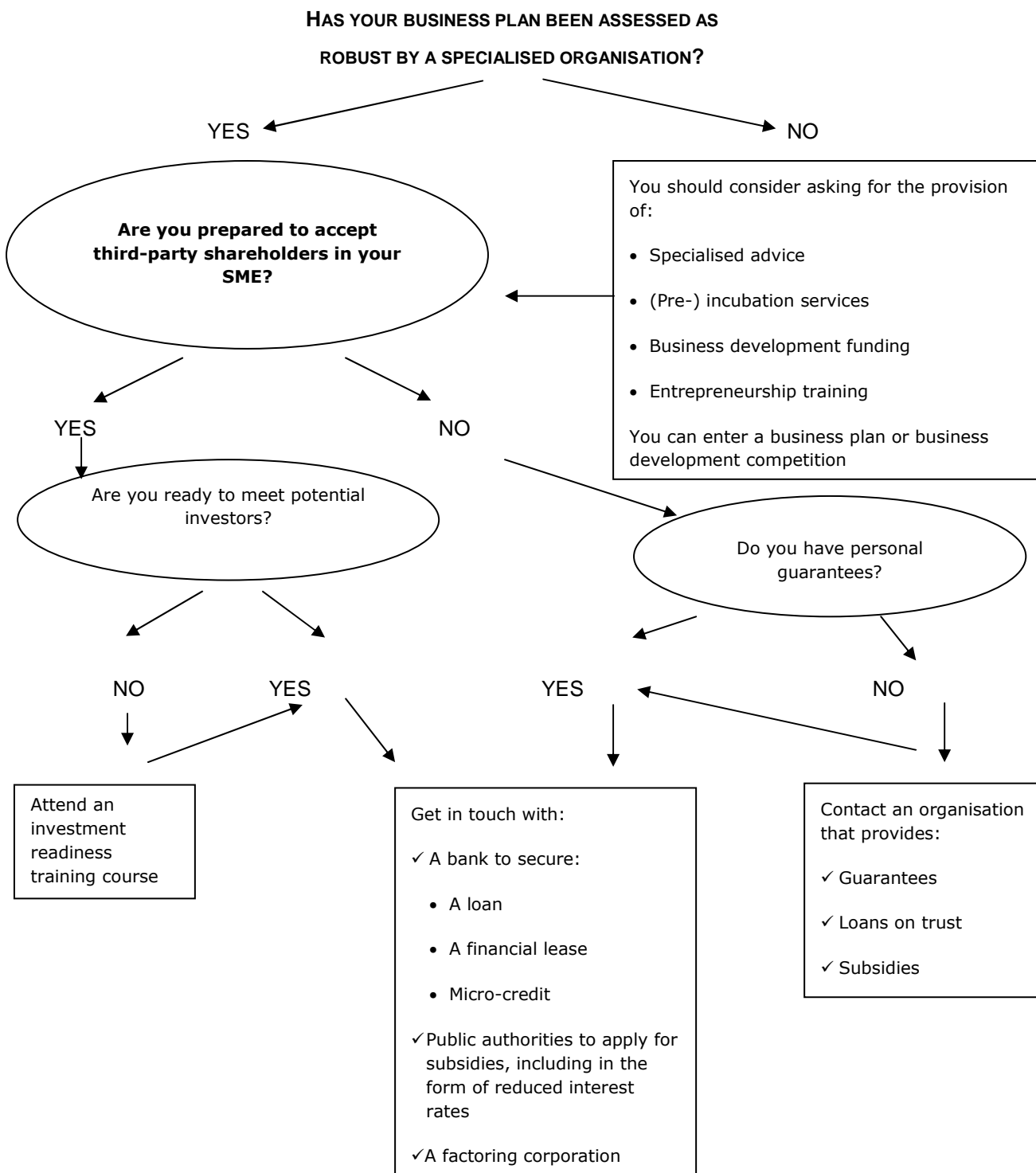
²¹ 1998-1999.

CHAPTER 3: ABOUT THE ENTREPRENEUR

I) What is the right path to access finance for an SME?

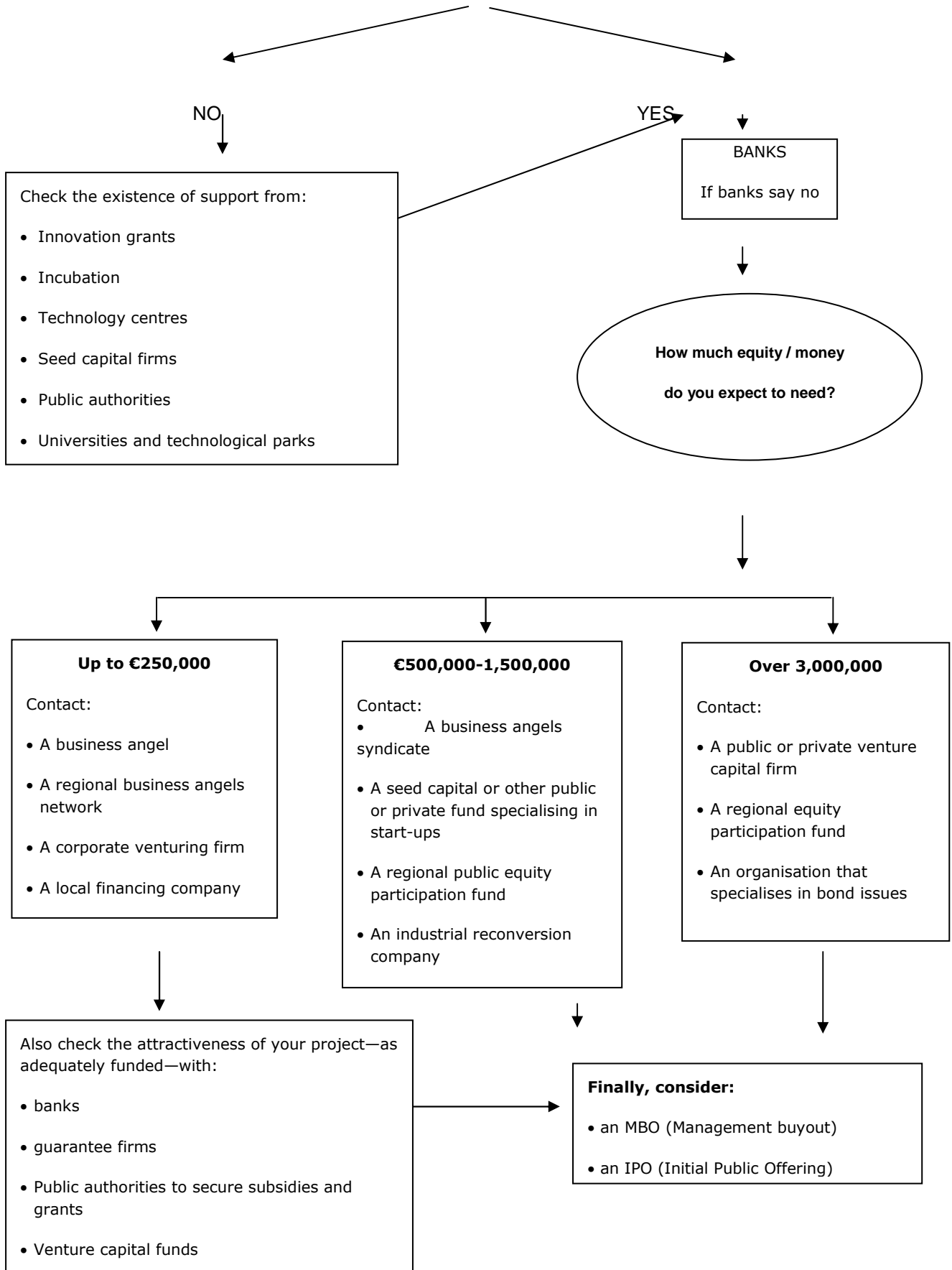
For the entrepreneur wishing to start a company, the world of financing is often a blurry and very complicated one. The difficulty stems from the fact that the entrepreneur, to get financing for a project, needs to be at the right place at the right time and with the right proposition.

This table²² will certainly help the entrepreneur understand the different steps that exist in the process of finding finance for his/her project.



²² Source: EURADA, Between Theory and Practice: Delivering Entrepreneurship and Innovation Support Services at Regional Level, Christian Saublens, September 2008.

**IS YOUR PRODUCT / SERVICE
READY FOR THE MARKET?**



II) What kind of enterprises need private venture capital?

Not all companies are suited to receive venture capital, and some will do better with loans or other forms of financing.

According to Katarina Bonde²³, Managing Director of KUBI, the following companies can benefit from private venture capital:

- A) Companies with business ideas with significant commercial potential;
- B) Companies with enough growth or profit potential to generate a good return on investments;
- C) Companies in dynamic and changing industries;
- D) Companies built on technical innovations;
- E) Founders who can share control of the company.

²³ Workshop on venture capital policy, Lund, Sweden, 30-31 May 2006.

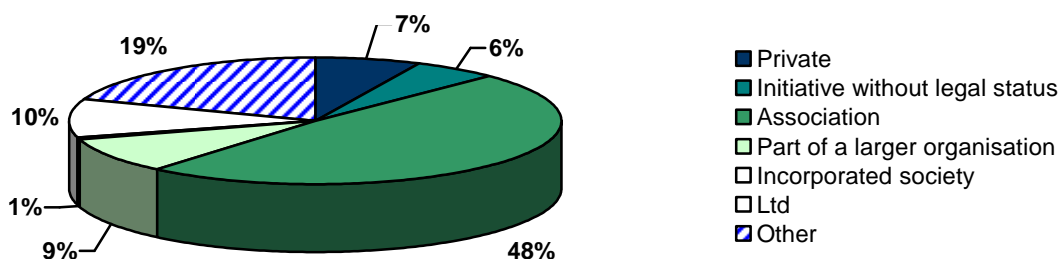
CHAPTER 4: ABOUT BUSINESS ANGEL NETWORKS

I) Legal form of business angel networks in Europe²⁴

The majority of business angel networks operating in the European Union are legally set up as not-for-profit organisations, private entities, or possibly foundations. They can be founded also by regional development agencies, Universities or incubators.

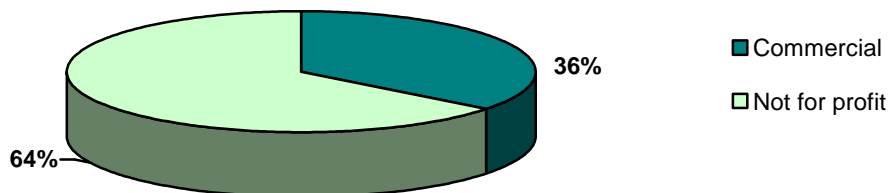
Legal status

The graph below illustrates the legal status of the networks based on 138 answers, including aggregate data provided by France Angels. 6 networks have a double structure.



Type of network: for or not for profit

The graph below illustrates the type of networks based on 109 network answers, including data provided by federation of networks in Europe.



II) How to set up a business angel network

A) Which partners should be involved at regional level?

Some well-known regional institutions can be invited to collaborate with the BAN: banks, financial intermediaries, venture capital and seed funds, incubators, science parks, chambers of commerce, regional development agencies, business support providers, etc. These institutions can provide the business angel network not only with deal flow or exit opportunities but can also infrastructure, collaboration on the organisation of events, dissemination of information about the activities of the network.

²⁴ EBAN Statistics Compendium 2008. Available at : www.eban.org

This collaboration can be reciprocal, for instance:

1. For the bank: securing new clients and/or co-investment funding;
2. For the incubator: a new client;
3. For the region: a renewal of the entrepreneurial base
4. For the financial organisations: potential clients
5. For seed and venture capital funds: co-investing
6. For a Chamber of commerce: additional service for its members

Networks can also be founded by Universities:

Reasons why a university would want to create a BAN²⁵ are the following?

- They are an important part of an entrepreneurial programme;
- Technology transfer and research opportunities for the faculty;
- Opens channels for students – learning and start-up funds;
- Active involvement of alumni;
- Engagement with the local communities.
- Generates wealth in the hands of entrepreneurs engaged in building businesses and jobs;
- Investor wealth brings benefits to the University;
- Models ethical investing standards for students.

Overall contribution of the BAN to the region:

- Raising awareness of entrepreneurship potential in the region;
- Professionalisation of the private equity market;
- Concentration of investment possibilities;
- Transfer of entrepreneurial knowledge and skills from one generation of entrepreneurs (the business angel) to the other (the entrepreneur getting BA' smart money and support).
- Stepping stone for other investors and in particular VC markets

B) Examples of recently founded business angel network in Europe

Grenoble Angels (F)²⁶

The idea of creating a business angel network in the Grenoble region first came from the **Chamber of Commerce of Grenoble**, to leverage the existing potential for promising start ups businesses in the region. Created in May 2005, with 15 members, Grenoble Angels²⁷ counted 130 members 3 years later.

1. Starting of the activities:

²⁵ ACEF Annual North American Summit, "How angels groups and universities can work together", April 27, 2006.

²⁶ EBAN Winter University 2008, Luxembourg. Presentation by Jean Maire Bernad.

²⁷ Website: www.grenobleangels.grenobleecobiz.biz

Grenoble Angels was created and developed under the Chamber supervision as follows:

- Choice of a charismatic leader, and gathering of the first six business angels. A well known and recognised person vis a vis of the Chamber other economic actors in the region representatives was specifically selected for this role
- Pooling together the first group of angels. The recruitment of new members has been done by co-optation; subjected to the approval of the members, all new candidatures require the unanimity to be validated.

The choice of the right leader has been underlined by Jean Maire Bernad as the most important aspect for successfully setting up the network.

- Structure of the Association and services to the members
- Development of a communication strategy for the recruitment of new members
- Development of the network activities

The Grenoble region has been very active in the ICT sector and presented an economic environment favourable for the creation of new projects and companies, and therefore an untapped demand for the financing of new companies.

To facilitate the implication in the analysis of the files:

After a first filter produced by the moderator of the club, a binomial of Business Angels is made up in order to deepen the file: in order to use competences as well as possible, each Angel writes a card detailed on his track records and its competences, the database is then used to dispatch the selected files.

To facilitate integration in the group:

- A welcoming kit, including those necessary tools to introduce new members to the activities of the network is distributed
- Integration into the network: several meetings are organized throughout the year, which help to:
 - Speed up the sharing of knowledge between members (1 to 2 per annum). These are also use to assess the new member partners
 - Training the new members: a training cycle is proposed throughout the year, which includes:
 - A school of business angels,
 - A technical training cycle with focus on due diligence, shareholder agreement, investment vehicles, valorisation, finance, law, etc.

2. Evolution:

Thank to the excellent connection with the Chamber of commerce of Grenoble, which offered venues, as well as other facilities, etc. the network grew fast and managed to catalyse the attention of other public and private actors, such as banks in the region. This cooperation with other actors has been beneficial to both angels and entrepreneurs in the region because of the substantial increase in the access to financing opportunities and to both public and private funds, grants and other services.

Angels for Growth (IT)²⁸

Italian Angels For Growth²⁹ is demonstrating ability to rapidly build a new Angels Network in a difficult market like Italy being able to integrate and balance different features:

- Build-up a cohesive group able and willing to share and operate with an outstanding commitment
- Operations over a broad territory: ability to attract members and deals from North to central Italy

²⁸ EBAN Annual Congress & Award Ceremony 2008, Arnhem, Netherlands. Candidate for the "Best Initiative on the market" Award.

²⁹ Website: www.intalianangels.net

- Maintenance of strong international links, both at the European level (with a regular participation in events such as the EBAN Winter University and Annual Congress, other European venture events and the EASY forum) and internationally.

The first input to create this network was given by the **Embassy of the United States in Milan** which first invited the future AIG co-founders to participate in their annual “Partnership for Growth” initiative. The network was then created by a group of pioneers BAs in January 2008.

Starting of the activities:

A study-trip to Milwaukee and in the Silicon Valley was organised by AIG co-founder members at the early stage of the angel network’s activities in order to familiarise with what was being done by some of the most performing BANs in the US, such as Golden Angels. This was also the occasion for the team to visit some of the most innovative business companies in the US, such as Yahoo, and the Kauffman Foundation, the largest foundation devoted to entrepreneurship in the US. The team found out the in most of the cases US BA groups visited were composed of few people, running the network as a spare time activity, and looking for fun besides than capital return. The trip helped the team to realise the feasibility of the project, both in term of resources available, and return expected.

Soon after the starting of the activities in Milan in January 2008, AIG recorded a high success both in terms of requests for membership and business propositions received, which revealed the existing gap in the access to finance for innovative start-up companies. This gap is mainly caused by a lack of structures in Italy capable to finance the R&D initiatives, to support the demand for business development financing.

1. Match-Making methodology:

A few months after the beginning of the activities, the network had already received circa 200 businesses propositions.

Investors meetings for members are organised every three months.

Only 3 maximum 4 projects are selected to be presented to members during these meetings and selected companies are given 1 hour (20 min. for pitching, 20 min Q&A, and 20 min discussion).

2. Due diligence on the network recruitment:

The first recruitment of angels in the network was by cooptation. Currently, an investor willing to join the network would need to know someone in the association for its request to be considered. Still requests are validated by the Board of Directors.

The introduction of such a strict recruiting method was needed in order to cope with the increasing number of requests received and in order to balance the number of those angels having great availability in terms of time but not in terms of capital, and vice-versa. The high number of both business plans and membership received is a clear signal of the market gap in the access to early stage finance in Italy.

Bulgarian Business Angels Network (BG)³⁰

2006 marked “the birth” of the BA market concept in Bulgaria. When Anton Todorov and Jivko Ivanov discovered there were not any networks or any known BA deals in Bulgaria they initiated a website, presenting the Bulgarian Business Angels Network (BBAN)³¹ as a general concept. It gradually drove so much attention and enquiries from start-ups and the government that a year later the team, supported by their first mentor and future partner – a serial entrepreneur Mr. Borislav Borislavov, established the Network as an official entity. The mention to the website had a significantly influenced the EU Operational

³⁰ Business Angel market in Bulgaria: Market Overview, May 2009

³¹ Website: www.bban.eu

Porgramme, which the Ministry of Economy & Energy was developing in the meantime. The OP explains the various target areas, schemes and priorities of use of expected EU support in order to meet the Convergence goals of the country. In April 2006 the Operational Programme "Development of the competitiveness of the Bulgarian economy" was submitted for approval to Brussels authorities which explained in detail the lack of funds for SMEs and the limited PE & VC investment market. In October 2006, when a next version of the OP was approved, it quoted the already informal website and included a special scheme to fund the establishment or the development of Business Angel Networks in Bulgaria allocating up to EUR 1 mil. of the budget. The call for projects under this scheme is expected to be announced in 2010.

The Bulgarian Business Angels Network was officially registered as a for-profit, professionally managed limited liability company on 22.11.2007. By December 2007 the Network conducted its first presentations to regional authorities and concluded its first partnership deals. In May 2008 one of the key support organizations in Bulgaria – the Center for Executive and Entrepreneurship Development conducted the first public event to help meet entrepreneurs and investors. In the next 6 months the Network invested in research and development of a website and a software platform known as EXCHANGE.bban.eu - a tool for screening and communication between investors and entrepreneurs.

In June 2008 the Bulgarian Business Angels Network became a full-member of EBAN. This received huge media coverage due to a press release issued by BBAN. By the end of 2008 the Network invested in promoting the concept, raising awareness and attending conferences for networking and brand building. In April 2009 Mr. Todorov took part in the EBAN Annual Congress in Madrid. Mr. Todorov is now an active member for the EBAN Marketing Committee.

Income sources of the network:

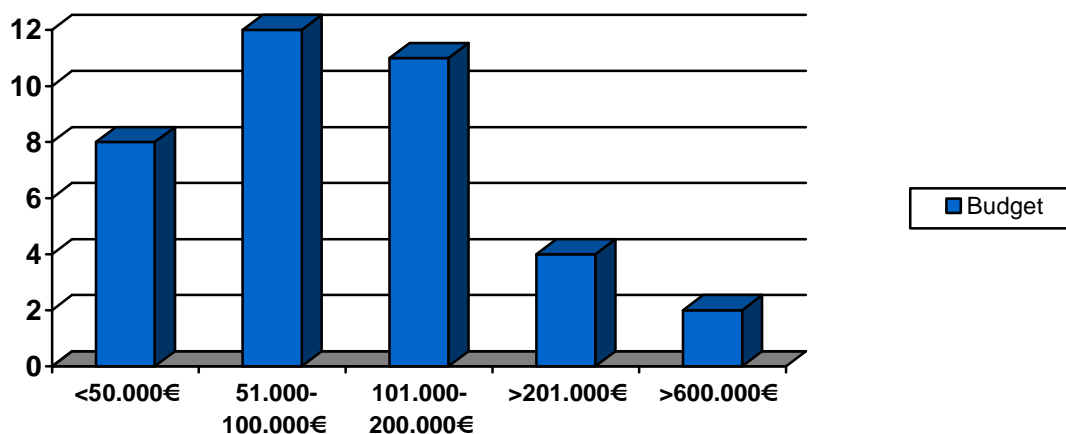
In the beginning the Network charged upfront fees from entrepreneurs for presenting their projects. The size of the fee depended on the length of time that proposals were active. Employment was not full-time. The model was reversed a year later. Currently angels pay an annual membership fee and entrepreneurs are allowed to submit projects for free (after screening) provided they agree to a success fee in case of a successful deal. Currently the network has 2 full-time employees, several part-time experts and a 5-member Board of Directors. The Network is entirely privately funded, with an expected capital increase and a pending restructuring into a joint-stock holding company. In terms of number of angels the Bulgarian Network's membership base increased to 19 angels. In the past 6 months the Network managed to conclude 2 deals – one in 2008 and one in 2009. BBAN managers expect to reach at least 50 members by the end of the year 2010 and to conclude at least 3 deals.

Currently, it is considered to be the most active organization of the informal capital market in Bulgaria.

III) Financing a business angels network

A. Annual budget of a BAN

According to the EBAN collection of statistics data in 2008, the average annual budget of business angel networks in 2007 was 180.000 €³². An illustration of the BANs budget distribution can be found in the graphic below.



B. Source of revenues

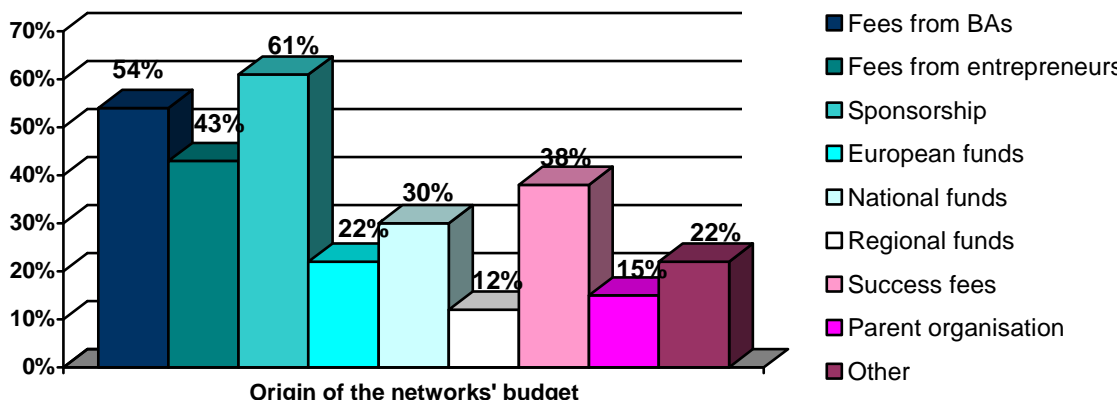
Most of the networks have a fee system. The system is either a mix of registration fee and success fee or a registration fee only. According to the EBAN collection of data in 2008, 64% of the networks charges fees to investors (between 100 and 1.500 €) and 30% to entrepreneurs (from 25 to 750 €). Moreover, 30% charge success fees to entrepreneurs (from 1.5 to 8% of the investment made), and 16% charge success fees to investors (from 2 to 20% of the investment made).

Other funding sources of the networks are:

- Sponsorship (covering from 2% to 100% of the networks' budget)
- European funds (covering from 2% to 100% of the networks' budget)
- National funds (covering from 12% to 100% of the networks' budget)
- Regional funds (covering from 20% to 100% of the networks' budget)
- Funding from parent organisation (covering from 10% to 100% of the networks' budget)
- Other funds (private funding by the partners or owners, municipal funds, private company funds, subsidies, event, trainings and visits).

³² Source EBAN Statistics Compendium 2008. 39 managers provided information on the average annual budget of their business angel networks.

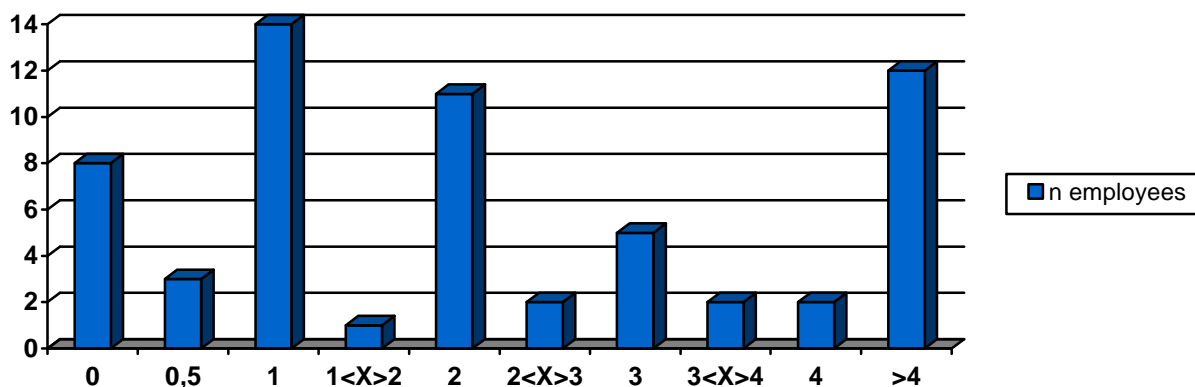
These figures are illustrated in the graph below.



Like any service-provider organisation, a substantial share of a business angel network's operational expenses is dedicated to human resource costs. Some BANs are managed by quasi-volunteers, while the majority would not have more than 2-3 employees.

According to the EBAN Statistics 2008, the average number of employees reported by responding BANs was 2007³³ 1.4 employees per network.

The graph below is an illustration of the number of employees per network, based on 114 received detailing the number of employees.



According to the same report, the 3 main cost items for business angel networks are: staff costs, marketing costs, and organisation of events for members.

Promotional costs often represent half of the budget of a BAN. For example, half of the 300.000€ budget of NEBIB (NL) goes to awareness campaigns. In Spain, 10% of the 130.000 euro budget of BANC is spent on raising awareness of the industry in the region of Catalonia.

³³ In 2007, 165 BANs reported 226 employees in total. Source: EBAN Statistics Compendium 2008.

IV) How business angel networks work and services proposed

A) Basic services

A network usually provides the following services to its members.

- Identifying potential business angels, their motivations or priorities as well as their investment preferences. The matching process is illustrated by the graph p. 30.
- Identifying potential projects (screening) and entrepreneurs willing to open their capital to a third party;
- A matching database;
- Organisation of forums where entrepreneurs present their ideas to potential investors
- Organisation of business plan competitions;
- Publication of newsletter or bulletins providing members with information on potential deals, displaying the following information on the company:
 - a. Sector of activity;
 - b. Amount of financing requested;
 - c. Short description of the project or company;
 - d. Stage of the company;
 - e. Region of investment;
 - f. Contact person.
- Organisation of seminars;
- Supporting angel syndication
- Developing leverage mechanisms including co-investment funds
- Mentoring;
- Legal support to business angels and entrepreneurs for the closing of the deal;

Some BANs use internet-matching services only. However all existing research shows that the angel market has always been working with face-to-face interviews whether it is for deal sourcing or for investment decisions. "Prior to the last economic cycle, research indicates that electronic networks in the private equity market had been largely unsuccessful, with less than 1% of equity raised being attributed to online sourcing"³⁴. In the latest research by the Centre for Venture Research, "angels are once again investing close to home, with more than 95% of the investments located within a half-day's travel from their principal residence"³⁵.

A.1) Role of a business angel network:

For the entrepreneur	For the Business angel
- Identification of potential investors	- Organisation of investments forums/clubs

³⁴“Sohl Jeffrey E. and Sommer Bruce, “Angel investing: changing strategies during volatile times”, p.8.

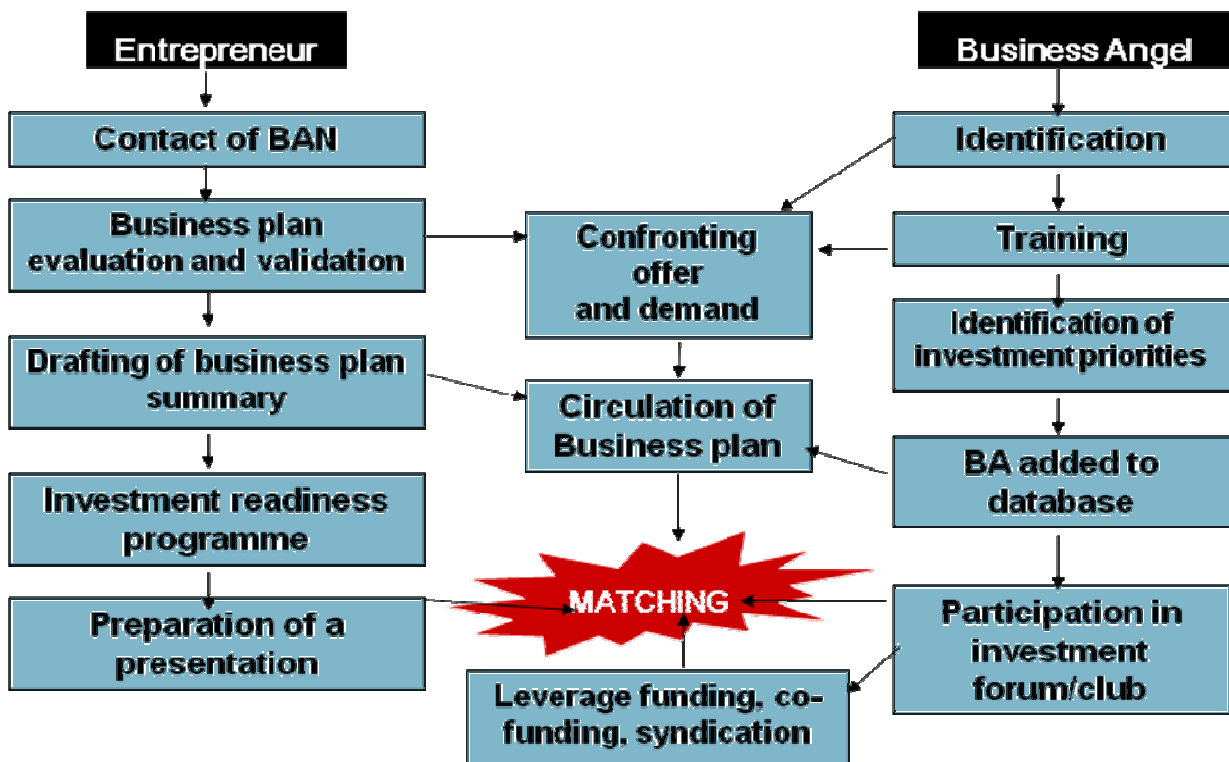
³⁵ Sohl Jeffrey E., “Angel investing, a market perspective” in “State of the Art: An executive briefing on cutting-edge practices in American angel investing”. Edited by John May and Elizabeth O’ Halloran, Darden School, Batten Institute, p. 9, 2003.

- Preparing the contact with BA	- Information bulletins, magazines, newsletters
- Financial advice	- Database of potential good projects
- Visibility	- Personal introductions
- Assistance for the matching	- Access to regional deals flow
- Information on additional fund raising	- Possibility of co-financing with other BA (syndication, co-investment)
	- Links with other networks

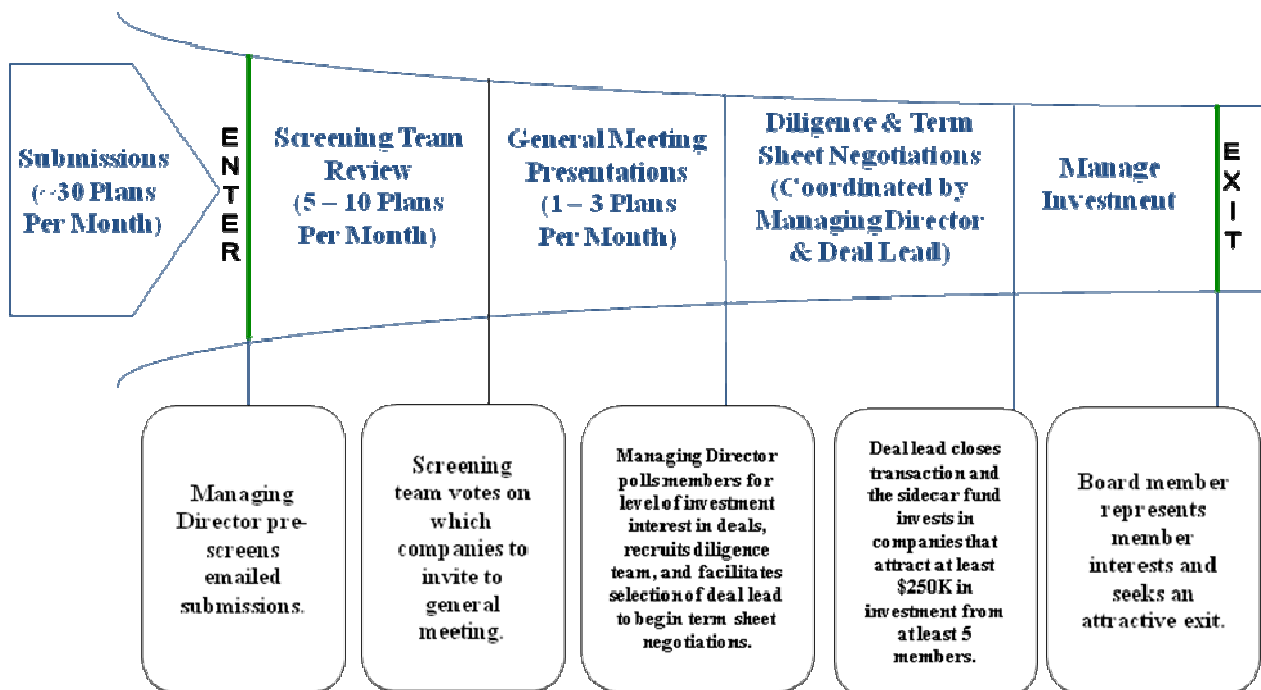
According to the private English network Envestors (www.envestors.co.uk), a good angel network should perform all of the following functions for potential investors:

- Provide a steady source of quality deals;
- Offer a degree of matching based on your specified investment preferences
- Ensure a level of due diligence is performed on both the deals and the entrepreneurs behind them
- Be able to guide and advise investors in the investment process
- Keep investors regularly updated on new and current opportunities with communications such as newsletters
- Provide investors with the reassurance that the equity requirement is part of a balanced funding package
- Provide investors with advice on valuation.

A.2) The matching process: when angels and entrepreneurs meet³⁶



The typical deal process³⁷:



³⁶ Source: EBAN

³⁷ Source: James Geshwiler, CommonAngels, Boston

B) Add-on services

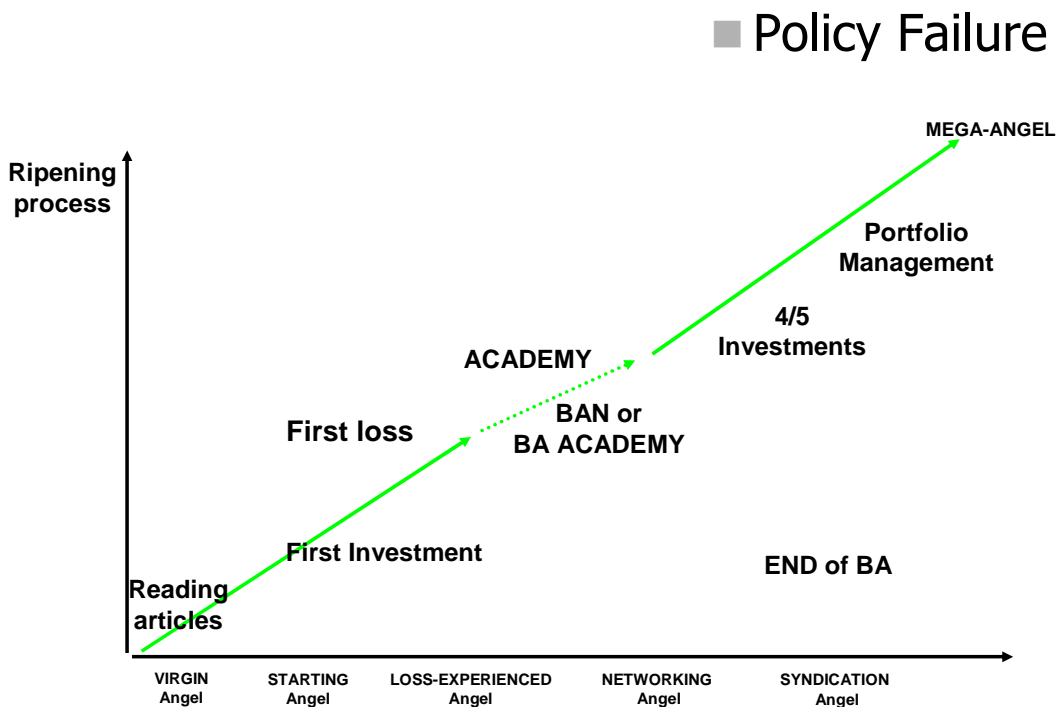
Some business angel networks have diversified their activities and offer a wider range of services. The EBAN Secretariat publishes a compendium of BAN add-on services which has identified a great number of additional value-added activities. This document is available on request at the Secretariat.

The graph below illustrates the role of business angel networks and business angel academies in reducing investment failures and encouraging new angels to the market³⁸.

B.1) Business angel academies

The objective of business angel academies is to train the participants and create platforms allowing the exchange of experiences and giving participants the necessary skills to manage the investment procedure. They also provide coaching angels to assess a proposal, help them grasp the extent of their role for the business, the risks involved and the opportunities learn about exit routes and success stories. The programmes are useful both for active and passive investors, experienced investors or virgin angels.

"Virgin business angels are affected by (the) lack of knowledge in the first and decisive stage of investment: the recognition and evaluation of opportunities. (...) Active angels primarily value training in the area of new business valuation (...) Passive business angels would initially invest in the lower range of investments, which reflects their higher risk perception"³⁹



³⁸ Aernoudt Rudy, "Efficient networking: successful example of close collaboration between national governments and angel networks", Presentation at the 2005 EBAN Winter University.

³⁹ San José Amparo, Roure Juan and Aernoudt Rudy, "Unleashing the potential for business angel investment", in Venture Capital Volume 7, No2, April-June 2005, p.161.

The topics to be discussed often include: the informal equity market; how to identify the investments chances; enterprises validation and investment analysis; procedure structure and negotiation; due diligence procedure and others.

The training can take various forms depending on the service provider: from a 1 day workshop to the incorporation into week-long training seminars.

Here are two examples of how BA academies are organised:

France Angels, The French National Federation of BANs, has been a pioneer in organising such events. Their program, which extends usually over a two-day period, includes the following elements:

For the BA:

1. What is a business angel?
2. Financing enterprise creation: the role of the BA
3. Due Diligence
4. BA-Entrepreneur relations
5. Becoming a business angel
6. The shareholders' Pact
7. Practical Case
8. Business angel investment in unquoted companies

For the BAN manager:

1. Presentation of a model BAN
2. Presentation of a specific BAN
3. Overview of American BANs
4. Experienced relations between the entrepreneur and the investor
5. Investment readiness
6. Relations between BA and entrepreneurs: Legal aspects
7. Investors: marketing of the network
8. Creation of networks of investors (informal and formal)
9. Fiscal issues
10. Evaluation of projects
11. Shareholders' Pact: Practical case
12. Legal and responsibility issues of the BAN itself
13. The concept of BAN: theoretical and practical aspects
14. Evaluation of the BANs and relations with local partners

The Solvay Business School in Belgium also organises sporadically business angel academies with the following program:

- The role of the business angel: generic approach and risk identification, role of the BA in the entrepreneurship process, personal evolution from being an entrepreneur to a business angel, and do's and don'ts.

- The investment cycle: general introduction, practical case followed by a debate, exchange of experience between the participants.
- Selection and analysis of the opportunities: criteria to assess a project, typology of innovation and sources of added value, discussion forum followed by a debriefing to establish a list of set criteria to evaluate a proposal.
- Best practices in “high tech” entrepreneurship: evolution of financing needs according to the stage of development of the company, business planning, marketing high tech, intellectual property rights, building a management team and selecting external contractors.
- Financing high tech and optimising the leverage effect of the BA: financial planning in a changing environment, overview of available financing sources (equity, debt and public sector support).
- Due diligence – reducing the risk: evaluating the management team, evaluation of technologies, evaluation of the market, and legal –accounting – administrative aspects.
- Valorisation of the investment: valorisation techniques, term sheets, and shareholders conventions.
- Coaching the investment: active or passive coaching and its limits, do’s and don’ts of coaching entrepreneurs, organisation of a professional general assembly.
- Exit routes: preparing the exit route as soon as possible, selling the shares, IPO.
- Exchange of experience and conclusions.

Other important services include:

- Investment readiness programmes
- Providing syndication opportunities to business angels by giving them a platform to meet;
- Providing co-investment opportunities by establishing co-investment funds where public authorities invest on a pari-passu basis with the angels to increase the amount of funding available for a company;
- Specialised financial products including equity guarantees, loan guarantees.

B.2) Investment readiness programmes

These programs consist of helping the entrepreneur to enhance the quality of his/her business plan, and a coaching service for the entrepreneur to prepare him to present his/her project to different types of investors. Indeed, business angels, VCs, banks and so on will not be looking for the same information, return on investment, exit routes, etc in a project.

In the framework of the Ready for Equity! (Training for Angels and Entrepreneurs) 2 years EU funded Project, EBAN has published a Mapping Exercise: “Analysis of the supply and demand for informal venture capital” was published in 2007 and updated in 2008. Also, a **Resource Pack** has been produced, which includes tools developed to facilitate the implementation of training courses:

1. Training curriculum for angels and entrepreneurs
2. Guidelines for the implementation of training courses
3. Pedagogic guidelines,
4. Recommendations, and check list for implementing a programme,
5. Mapping Exercise: Analysis of the supply and demand for informal venture capital.

The Ready for Equity ! Resource Pack materials in multiple languages, namely English, Dutch, French, German, Italian and Spanish can be downloaded free of charge as an “open source” at the project dedicated website: www.readyforequity.eu.

A new follow on project, Ready for Equity! II - building on the achievements of Ready for Equity! kicked off in December 2008 for a 2 year period. The project aims to develop and strength content curricula for angel and entrepreneurs developed under Ready for Equity! delivering training in less mature early stage markets in Europe. More information about the Ready for Equity! Project 1 and 2 are available at www.readyforequity.eu.

Investment readiness programmes are designed:

- To reduce the number of projects refused funding as a consequence of the lack of quality of the business plan or the presentational skills of the entrepreneur;
- To make the entrepreneur understand that not all types of finance are appropriate for his/her business and that they also vary according to the stage of development of the business.

Exemplas in the United Kingdom runs an investment readiness program that is organised around 2 stages: awareness seminars and advisory panels.

- The awareness seminar aims at making the entrepreneur understand that not all sources of finance are appropriate through presentations made by bankers, venture capitalists, private equity investors and asset financiers.

- The advisory panel is the second stage where the entrepreneur presents his/her company to a panel made of a banker, a VC, a private investor, a sector specialist...who give the entrepreneur an honest advice about the financial credibility of his projects according to each one's prerequisites.

In between the two stages the entrepreneur is given advice by the BAN on his business plan, the key aspects of the company that need change, what is good and needs to be looked into...

Other important services include:

- Providing syndication opportunities to business angels by giving them a platform to meet;
- Providing co-investment opportunities by establishing co-investment funds where public authorities invest on a pari-passu basis with the angels to increase the amount of funding available for a company;
- Specialised financial products including equity guarantees, loan guarantees.

B.3) Co-investment schemes in Europe

Co-investment is the pooling of different investors making investment together usually directly into companies or in a fund, where other financial parties or private investors invest, with the aim to fill the equity gap for early business finance. In particular, co-investments allow an investor to invest in larger deals without mobilizing as much as high amount of capital in a single deal as well as reducing exposure to the risk because of the sharing of the deal source funding and risk with other investors.

Since a few years, a series of business angel networks and actors, such as the public sector (government) or banks, have developed co-investment schemes to leverage equity invested by angels.

❖ The Scottish Co-investment Fund

With around 18 angel groups in the region, Scotland records a mature and professional angel syndicates market, where some syndicates have the capacity to finance the company from start-up to exit, without the involvement of other financial actors. In the year 2007, €20.453.600 were invested and 41.304.000€ including co-investment.

In January 2008, the Bank of Scotland has launched a new co-investment programme in conjunction with the Oxford Investment Opportunity Network (OION), connecting companies and new businesses to the

network of business angels and corporate investors in order to raise equity funding⁴⁰.

Some characteristics of the scheme include:

- Members of OION invest alongside Thames Valley Investment Network and Oxford Early Investments members;
- The bank made £2m available, with deals of between £25,000 minimum and £250,000 maximum matched funding per qualifying company;
- All investments are made on the same terms as OION's investor members.

The scheme focuses on:

- High Tech Research, Proof of Concept, Proof of Principle.
- And include the following sectors:
- Life Science, MedTech, Biotech, Technology, Precision Engineering, Software/IT/Wireless, General Technology, Film, TV & Theatre, Green Technology and Lifestyle.

The benefits of the programme include:

For the Bank of Scotland

- Access to companies at earlier stage than current portfolio
- Find the 'stars' at this stage of development
- Establishment of relationships with high net worth investors.

For Companies and Deal leaders/ OION investors⁴¹

- Increased capital injection to allow companies to progress growth plans
- More security for OION investors
- Deal leader has improved position to improve terms

❖ United Kingdom

The Seraphim Capital Fund (www.seraphimcapital.co.uk) based in London is a £30 million generalist co-investment fund that invests alongside leading business angels and other private investors drawing on the deal flow and investment experience afforded by the funds' diverse investor base. The fund is managed by a coalition of 'business angel' networks and focus on investments in companies throughout the UK predominantly in the early stages of development.

❖ Sweden

In Sweden, STING Capital (www.stingcapital.com), a €4.2 million pre-seed venture capital fund, combines funding from government agencies, private business angels, other VC companies and private institutional investors. The fund aims to solve the lack of seed capital in the Stockholm region so that technology start-

⁴⁰ Modal, Eileen from Oxford Investment Opportunity Network Ltd (OION), "OION's relationship with Bank of Scotland". Presentation at the EBAN Winter University October, 2008.

⁴¹ EBAN Winter University 2008, Presentation of Eileen Modral from Oxford Investment Opportunity Network Ltd (OION) about "OION's relationship with Bank of Scotland".

ups can be developed to later stages where they can attract more traditional VC funding.

B.4) Guarantees for business angel networks

In certain European countries, guarantee schemes to shoulder part of the risks taken by their business angels have been developed.

❖ Austria

AWS, Equity guarantees (www.awsg.at/www.business-angels.at) has the objective to enhancement of the equity basis of small and medium-sized enterprises. Eligible for guarantees are individual investors (natural persons), enterprises, and institutional investors (e.g. Investment Funds, Banks). The Equity capital guarantee covers the invested capital (but not a return on capital) of the private investor in the case of insolvency of the SME.

Advantages for SMEs:

- Strengthening of the Equity Basis of the SME
- Equity may be used as Leverage for additional Loan Financing
- Experienced Investors contribute to the Business Development
- No collaterals required
- No fixed Costs of Capital

Advantages to investors:

- Risk Coverage
- Possibility of high Rates of Return
- Project assessment through aws
- Guarantee Fee below Market Rate

Advantages to bank:

- Improvement of the Capital Structure of the SMEs
- Reduction of the Credit Risk
- Equity may be used as Leverage for additional Credit Financing

Guarantees of this programme are partly counter guaranteed by the European Investment Fund.

❖ France

OSEO GARANTIE (www.oseo.fr) in France covers up to 70% of the amount invested by the angel.

❖ Belgium

In Belgium, the Walloon Region, through Sowalfin - Société Wallonne de Financement et de Garantie des Petites et Moyennes Entreprises (www.sowalfin.be) and in collaboration with the Walloon BANs, proposes a guarantee scheme to angel investors. BAN Vlaanderen, for the Flemish Region, has subscribed to this scheme.

Co-investment funds have emerged in the last few years in different countries in Europe, including the Netherlands, Germany and Poland.

V) Ethical aspects of business angel networks

National and regional business angel networks are urged to define and/or enforce a code of conduct in order to ensure the establishment of a sound relationship between all players involved in the matching process (i.e. the network itself as well as the business angel and the entrepreneur).

Below is an example of a an investor agreement form that London Business Angels imposes to its member investors, followed by an example of a code of conduct that **BBAA** (The British Business Angels Association) recommends to its members. **London Business Angels Investor Agreement Form**

Essential Information

London Business Angels Limited LBA provides an information service to exchange data between firms and potential investors. It does not advise on the merits or risks of investment and is not authorised to arrange transactions or circulate offering documents under the FSMA 2000 but rather is an exempt body under Statutory Instrument 723 of 1988 as a non-profit making organisation.

Investment, whether in new or existing businesses, carries high risks as well as the possibility of high rewards. It is consequently very speculative and potential investors should be aware that no established market exists for the trading of shares in private companies and such investments are not readily realisable. It must be appreciated that there could be difficulty in selling such investments at a reasonable price and in some circumstances it may be difficult to sell them at any price. Similarly, there are risks of non-repayment in the case of an investment made by way of loan or guarantee of a loan. Accordingly, you should consider carefully whether such investments are suitable in the light of your circumstances and commitments and the financial resources available to you.

Before investing in a project about which information is provided by LBA, potential investors are strongly advised to take advice from a person authorised under the Financial Services Act 1986 who specialises in advising on investments of this nature. Whilst the persons responsible for issuing the details contained in LBA information will take reasonable steps to ensure that the information it contains concerning proposals requiring capital is neither inaccurate nor misleading, they are reliant upon the information provided by the firms concerned and no independent verification or investigation is carried out by LBA, because of the number of applications handled and in the context of the resources available. Accordingly, no responsibility can be accepted by LBA, for any damage or loss of whatsoever nature due to negligence, disclosure or non-disclosure or any cause occasioned by an investment in any business registered LBA where the investment arises as a result of information provided under the LBA scheme. The function of LBA is solely to bring together prospective investors with firms and in consequence LBA strongly recommends that all prospective investors make their own legal and other professional enquiries before proceeding with any investment.

Operative Provisions

I/We have read the Essential Information above and agree to all the conditions and disclosures that are set out therein. I/We accept that any decision to invest in any business introduced to me/us by LBA is my/our responsibility and that I/we will notify LBA if I/we make any investment directly or indirectly arising out of any introduction made under the LBA scheme.

I/We declare that the information supplied by me/us is accurate and complete to the best of my/our knowledge and that I/we am/are not disqualified from holding office as a director of a company nor have

been convicted of any criminal offences in relation to a business activity nor have been adjudged bankrupt nor suffered the making of any application for a bankruptcy, administration or like order pursuant to the Insolvency Act 1986, nor have I/we been involved in any capacity in any company or business which has entered into liquidation, administration or receivership which I/we have not disclosed fully and in writing to LBA.

I/We agree to hold confidential any information provided to me by any business introduced to me by LBA or any LBA affiliated agency and agree to execute a confidentiality agreement direct with the business if called upon so to do. Further I/we undertake that I/we will not solicit business from any company seeking investment nor in any way use any introduction as made under the LBA scheme for my/our own commercial gain, other than as envisaged by the terms of the scheme.

I/We hereby request to enter into an Agreement with LBA on the above terms and acknowledge that LBA reserves the right to refuse a request for membership of LBA without providing a reason.

BRITISH BUSINESS ANGELS ASSOCIATION

Code of Conduct

1 Terms and abbreviations

“**Articles**” means the Articles of Association of BBAA for the time being.

“**BBAA**” means British Business Angels Association

“**BBAA Logo**” means the identification logo of BBAA as appears on this page, or other logo adopted from time to time.

“**the Board**” means the Board of Directors of BBAA in accordance with the Articles

“**Code of Conduct**” means the BBAA code of conduct as amended from time to time

“**Disciplinary Procedure**” means the BBAA disciplinary procedure as amended from time to time

“**FSMA**” means the Financial Services and Markets Act 2000 as amended.

“**Member**” means a Full Member of BBAA in accordance with the Articles

“**Membership Criteria**” means the standards that must be achieved by a Member for the application for membership to be successful. The Membership Criteria is set out on the application form

Best Practice

Members shall conduct their business in a professional manner and will not engage in practices, which would be damaging to the image of the business angel market.

Members shall promote and maintain ethical standards of conduct and at all times deal fairly and honestly with all parties.

Members shall ensure that they display the BBAA Logo on their website, letters, forms and other paperwork at all times, as soon as practicably possible.

Members shall ensure that they comply with the Membership Criteria so long as they are a Member.

Members should have appropriate Professional Indemnity Insurance.

Members should use all reasonable endeavours to ensure that investors and investees are fully conversant with the investment process.

Before a member enters into a contract with an SME, a competent and experienced member of the member’s team will have received a copy of the comprehensive business plan of the SME and will have a meeting with the authorised representatives of the SME to discuss the plan and the SME’s fund raising proposals generally.

Service Levels

Members must have clear written terms of business.

Members must have a clear registration process for engaging companies seeking investment and investors.

Members must have written procedures in place for handling complaints that is available on demand.

Information on Fees

Members must provide clear information on fees charged.

All fees that are to be charged must be disclosed by the Member before any contract is entered into.

Confidentiality

Members will take all reasonable precautions to keep investor's information and investee's information private and confidential.

Members must return to the investee on demand any written information or other materials.

Members will use investee information solely for the purpose of raising finance, and not exploit it or otherwise apply it in any way.

Members will restrict access to information to those responsible employees and partners whose knowledge is essential for assessment and evaluation for the purpose of raising finance.

The above undertakings do not apply to any information which is in the public domain or is already in the possession of BBAA or which subsequently becomes known to Members independently.

Information to BBAA

Members shall supply such information to BBAA as may be reasonably requested by the Board. In particular Members will complete a "statistics sheet" (in the form determined by the Board from time to time) every quarter providing details of all transactions completed in the previous three months.

Update Members Profile

The Member is responsible for keeping their profile on the BBAA website up-to-date.

FSMA

The FSMA is all-embracing and all members must be fully conversant with its provisions.

Compliance

Members must at all time comply with the Code of Conduct (as amended from time to time by the Disciplinary and Membership Committee (as defined in the Articles)).

A Member's failure to comply with the Code of Conduct will be dealt with at the discretion of the Disciplinary and Membership Committee in accordance with the Disciplinary Procedure.

Edition: August 2008

Moreover, BANs produce their own documents governing the various relationships that exist between themselves and entrepreneurs, the network and business angels and between business angels and entrepreneurs. These documents address each party's roles, costs and confidentiality rules. There are usually called "statutes of the association" whether they concern not-for-profit or commercial business angel networks. The EBAN Secretariat can provide some examples on request.

VI) Cross-border business angel activities

A) Cross-national networks

Austria develops contacts with partners in Slovenia while Finland develops contacts with both Sweden and Estonia. Go Beyond Ltd, based in Switzerland, has set up a trans-national network around groups of corporate investors based in several European countries, such as France and UK. An electronic platform has been set up to exchange information about deals. Other networks that invest cross-border in Europe are Media Deals (in the content industry) and Quantum Board GmbH (focused on photo-voltaics). As transnational networks, they operate in France, Switzerland and Germany.

B) EASY – Cross Border investments for early stage investors in Europe

The EASY programme was the two years EU co-funded project, launched in 2006 and supported under the PRO INNO initiative that aimed at bringing together early stage investors and innovative businesses seeking risk capital from across Europe. The partnership was lead by Greater London Enterprise (GLE) and was constituted of 17 organisations from 11 different European countries.

Through the organization of transnational investors forum, the project ends in December 2008, has achieved the following so far:

- brought together 750 investors from 25 countries
- 76 selected companies from 20 countries – Sectors ICT, Media, Med Tech, Clean Tech, transport & logistics
- 4 transnational deals closed – 5M Euros
- 9 national deals closed – 10.5M Euros
- Pipeline 5 further heads of terms signed – 4M Euros

Other activities developed in the framework of the project were the following set of tools:

- Complete cross-border toolkit developed for entrepreneurs and investors
- Quality Framework and Code of Conduct and Legal Templates for cross-border investing and syndication under the coordination of EBAN.

To know more about the EASY project more information are available at: www.earlystageinvestors.org

VII) National Federations

A federation of networks is an association of business angel networks at the European level, such as EBAN, at the national level such as British Business Angels Association in the UK, IBAN in Italy, SVCA in Sweden, BeBAN in Belgium, France Angels in France, SECA in Switzerland, etc., or at the regional level such as ACC10' CIDEM (Catalonia).

Their role is to:

1. Lobby the national /European administration;
2. Raise awareness of the BA and BAN concept and the visibility of the industry;
3. Exchange best practice;
4. Gather statistics on the activities of the business angels;
5. Promote ethical rules and codes of conduct;
6. Increase matching opportunities: there is often an agreement between business angel networks that if a good project does not find its BA in one particular BAN, they will pass the profile to a colleague.

VIII) Strengths and weaknesses of the environment in which business angels networks and individual business angels operate in Europe

The advantages of the informal venture capital market segment include:

- Providing capital at a moment of high-risk for the start-up;
- To associate the business angel to the project and consequently to introduce a human aspect on top of a financial one between the entrepreneur and the investor. This also leads to complementing young entrepreneurs' managerial skills, thereby improving business survival rates;
- To increase the confidence of the future investors and to enhance the credibility/ legitimacy of the company;
- To facilitate the involvement of informal, institutional and other type of investors in the second phase of the development of the enterprise for follow-up rounds. The leverage effect of business angel involvement is very important:
Ex: The Business angel leverage effect⁴²

Deals	Number	Business Angels	VC companies	BayernKapital, KfW	Sum
2008	5	300000	2640000	2760000	5700000
2007	6	1026376	5100000	1730000	7856376
2006	7	375000	3250000	2425000	6050000
2005	7	716000	3350000	2200000	6266000
2004	8	2119878	850000	1800000	4769878
2003	8	3685000	6320000	960000	10965000
2002	10	3161355	2978952	3634598	9774905
2001	19	8340934	6617426	9943814	24902173
2000	24	5857765	7828958	6050786	19737508
1999	6	771938	9387319	7884121	18043378
Total	100	26354246	48322655	39388318	114065219

⁴² Source: Netzwerk|Norbayern 2008.

Informal venture capital activities face the following hurdles:

- A tax environment that is often not favourable—and sometimes even discriminatory—especially when it comes to taxing capital gains and writing off losses (only 2 countries, namely UK and France, out of 27 provide up-front tax incentives to business angels);
- Inappropriate regulation concerning investments by private individuals into companies (financial services provision and prospectus rules);
- Local/regional—and sometimes national—authorities lack the willingness to provide financial support for business angels networks during their first few years of existence while this is sometimes absolutely vital and despite the role played in favour of the local economy;
- The absence of potential regional exit routes for business angels. In some EU regions, the development of the formal venture capital market segment, which is the natural exit route for business angels, is still embryonic. Moreover, there is a lack of understanding and communication between business angels and venture capitalists, making it difficult for BA to exit through VC involvement
- The low number of training schemes for potential business angels and entrepreneurs;
- The information asymmetries between investors and entrepreneurs;
- The low visibility of the equity finance market in comparison to debt finance solutions for financing start-ups.

IX) Collaboration between BAs and VCs

The importance of the collaboration between BAs and VCs is the more and more important and this due to different factors. Recent trends in the equity industry show that:

- VCs are slightly moving away from the financing of the early stage companies, with an average amount of money invested by VCs around just 3% of their overall activities in early stage companies. This creating a new equity gap in access to finance for early stage innovative companies seeking for between 500.000 and 2-3 M €.
- A significant number of deals is now made by angels in syndication or through co-investment schemes. This new trend allowed for the emergence of bigger and better structured deals, with characteristics that are closer to those sought by VCs when considering investing in a business.

In the light of the above considerations, a strengthened and better structured collaboration between BAs and VCs would represent a valuable solution to fill in the equity gap in access to finance for innovative and high growth companies.

In the framework of the collaboration with EVCA (European Association of Private Equity and Venture Capital Association), and in conjunction with other BANs in Belgium (BAN Vlaanderen and Be Angels) EBAN organized on the 21st of October 2008 the Benelux's first BA/VC Forum. The forum gathered around 30 representatives from the angel and VC industry, and provided the opportunity to both BAs and VCs present to meet and discuss about challenges and future scenario for a strengthened collaboration. The forum represented a pilot test to be duplicated in other European countries at national or regional level.

Suggested solutions that would enable a potential closer collaboration between BAs and VCs in the future have been:

- The professionalization of the angel's investment since its inception
- Well organised angels groups

- More co-investment activities between BAs and VCs
- Use of the same legal documents to standardize investment procedures.

To achieve these goals, building trust and increasing knowledge between the two types of actors is a preliminary condition and the event was certainly useful to put BAs and VCs closer to better understand mutual challenges and scenario for collaboration.

A repetition of the event on regular basis could be used as a way to improve awareness raising among both communities and improve deal flow and funding opportunities for both actors.

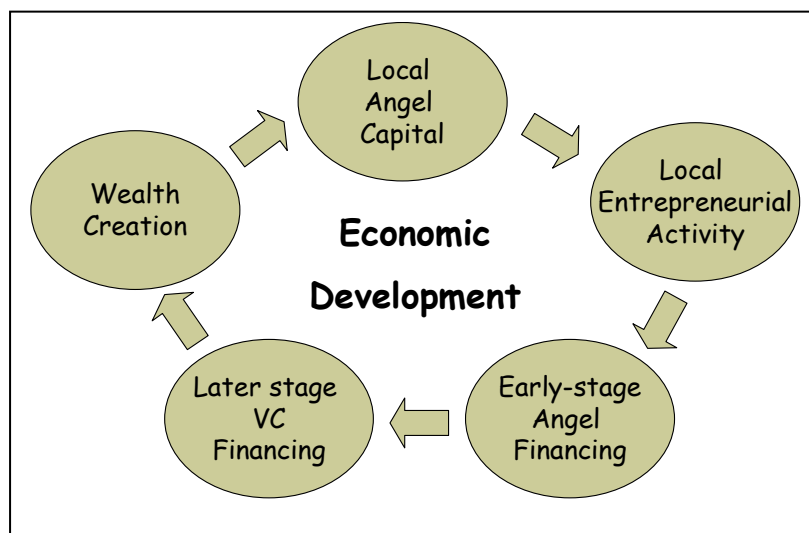
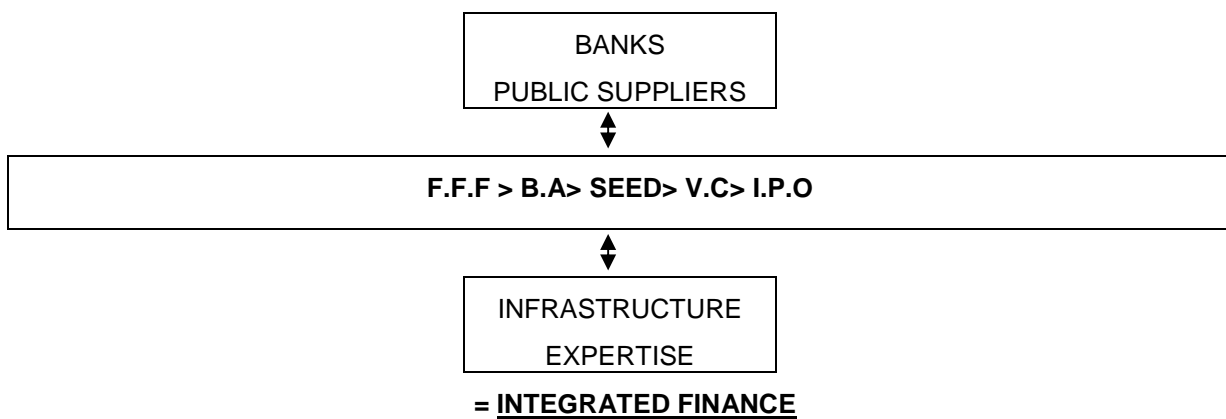
X) The role of public authorities in the development of the informal venture capital market

A) Regional public authorities:

Regional public authorities can:

- Organise awareness campaigns to circulate information about the usefulness of business angel networks as contributors to business and regional development;
- Provide financial support to BANs – help them to at least break-even financially;
- Provide support to integrated finance schemes and investment readiness programs both for entrepreneurs and investors;
- Promote codes of conduct for BANs and BAs;
- Integrate BAN activities in the overarching regional entrepreneurship strategy;
- Provide help for the screening of business plans which is time-consuming for BANs.

Making sure that one instrument can be the raw material for the next one.



Source: Presentation by Rudy Aernoudt, 2005 EBAN Winter University, "Efficient networking – successful example of close collaboration between national governments and angel networks".

A) National public authorities:

National public authorities can:

- Raise awareness on the role of BA and BANs for the economies;
- Improve the legal, administrative and tax environment in which business angels networks and individual business angels operate
- Improving the fiscal environment by providing capital gain or loss exemption from tax, favourable income revenue taxation for individuals if they invest in start-ups
- Change Prospectus Laws - A prospectus is a disclosure document given to investors by issuers when they want to raise capital and/or when they want their securities admitted to trading.
- Change the rules applying to financial services provision.
- Address business angels and their networks as an integral part of the VC chain and help the fluidity of exit route by strengthening the relationships between each link of the chain.

B) European policy makers:

SMEs represent 99% of all business in Europe, and have been defined by the Commission itself as the “backbone of the EU economy”. The European Commission has designed and developed both EU policies and financial instruments. In the last few years access to finance at European level has been fostered by the following Commission initiatives/programmes:

- The adoption of the “**Small Business Act**” for Europe (**SBA**) in 2008, reflecting the political will of the Commission to recognise the central role of SMEs in the EU economy (the SBAs also put into place for the first time a SME policy framework for the EU and its Member States)
- Commission Communication “**Financing SME Growth – Adding European Value**”, 2006, in which the Commission acknowledges the crucial role of business angels for European economies and the need for member states to support their operational environment
- “**Risk Capital Summit 2005**” that discussed about the importance of risk capital can to support European innovation and growth of SMEs
- The Financial Instruments of the **Competitiveness and Innovation Programme (CIP)** helping SMEs raise equity and debt finance, an running from 2007 to 2013
- Also, between 1996 and 2002 the DG Enterprise and Industry of the European Commission supported several actions aimed at disseminating the concept of informal venture capital.

- Communication on “Financing SME growth – Adding European Value” (June 2006).

In this document the Commission acknowledges the crucial role of business angels for European economies and the need for member states to support their operational environment.

“Knowledgeable private investors are critical for the launching of entrepreneurial businesses, but there is a serious and persistent lack of business angels and other seed investors in Europe”

“The Member States are invited to create incentives for private investors that are willing to invest in enterprises, including by using public funds to target co-investment with business angels. The Commission will identify and spread good practices that can help improve the conditions for business angel investment”.

“Enhance investor cooperation in seed investment, paying particular attention to business angels, by identifying and spreading good practices”.

“Identify and spread good practices in investment readiness programmes”

“To enhance pre-seed and seed financing, the Commission will also promote cooperation between Commission-financed activities like Europe INNOVA and PRO-INNO Europe and networks such as the European Business Angels Network (EBAN)”

- **Conclusions from the “Risk Capital Summit 2005” organised in the framework of the UK Presidency of the EU**

“Europe’s 50,000-100,000 Business angels provide much-needed risk capital to businesses with high-growth potential, at a stage where venture capital funds do not yet get involved. However, the business angel sector is fragmented and business angel networks need greater visibility. Closer cooperation between business angels and venture capitalists could further improve the provision of risk capital. “

Business angels should be encouraged by:

- The public sector investing in co-investment funds that are available to Business Angels;
- Fiscal incentives that encourage early stage investment;
- A supportive regulatory environment; and reduction of obstacles to cross-border investment.
- Raising awareness of angel finance and stimulating the demand for risk capital. The European and National Business Angel Associations should play a greater role.
- More co-operation with venture capitalists. This would be of mutual benefit and would improve access to risk capital for high-growth companies throughout their financing cycle.

- **Competitiveness and Innovation Programme (CIP) 2007-2013**

The CIP foresees that the European Investment Fund will be able to invest in co-investment funds set up by BANS, under the heading “Growth Investment Facility”.

Fiduciary, management and monitoring aspects shall be agreed between the Commission and the EIF. The Commission shall apply specific guidelines on treasury management.

GIF1 and GIF2 shall target commercially oriented intermediaries managed by independent teams combining the appropriate mix of skills and experience. The intermediaries shall be selected in conformity with best business and market practices in a transparent and non-discriminatory manner, avoiding any conflict of interest with the aim of working through a wide range of specialised funds or similar structures.

GIF shall be complementary to the own-resource based activities of the European Investment Bank Group including the EIF by adopting an investment policy involving a higher risk profile, both as regards intermediary funds and their investment policies.

GIF 1 shall invest in intermediary venture capital funds investing in SMEs up to 10 years old, typically starting from pre-A (seed) and A (early stage) rounds and providing follow-on investment where appropriate. The maximum aggregate investment in an intermediary venture capital fund shall be 25 % of the total capital held by the relevant fund, or up to 50 % for new funds likely to have a particularly strong catalytic role in the development of venture capital markets for a specific technology or in a specific region as well as business angels’ investment vehicles. The maximum aggregate investment in an intermediary venture capital fund shall be 50 % in those cases where the fund’s investment focus is on SMEs active in eco-innovation. At least 50 % of the capital invested in any fund shall be provided by investors operating in circumstances corresponding to normal market conditions (under the “market economy investor

principle”), irrespective of the legal nature and ownership structure of the investors providing this part of the capital. No commitment in a single fund shall exceed 30 million€. GIF1 may co-invest with EIF own resources or resources under the EIB mandate or other resources managed by the EIF.

Other documents underlining the role of business angels include:

- The OECD Brasilia Action Statement for SME and Entrepreneurship Financing 2006
- Green Paper on Entrepreneurship 2003
- Risk Capital Action Plan 2003
- BEST report, Benchmarking Business Angels, European Commission, N°1 – 2003

C) Public sector intervention to stimulate the informal venture capital market:

Professor Colin Mason from the University of Strathclyde has recently carried out a study on the public sector intervention in the informal venture capital market to improve access to finance for SMEs in Europe⁴³ that should be key priority for policy makers.

According to the study, the forms of public intervention has evolved from a supply-side approach (using tax incentives targeted at high net worth individuals), through an intermediation approach (aimed at improving information availability, through capacity raising and funding of business angels networks providing capacity building functions), to a supply-side approach based on using public money to leverage private investment.

The widening equity gap increased by the recent venture capital funds withdrawal from the early stage market, lead Governments to establish co-investment funds to invest alongside angel groups and to enable them to make larger and follow-on investments.

However, because of the difficulty to measure the size of the angel investing market due to its private nature, there is very little evidence of the impact of the various governmental forms of intervention, and *“supporting the informal venture capital market has therefore been largely an act of faith by governments”*.

“A key priority for governments must be to invest in appropriate methodologies which can accurately measure investment trends in the early stage venture capital market over time, and specifically angel investment activity, so that the need for public sector intervention can be demonstrated and the impact of such interventions can be measured”.

XI) Policy recommendations: The EBAN White Paper and Financial Statement⁴⁴

A) The EBAN White Paper

EBAN’s White Paper is a statement by the EBAN Board on ways in which the European Union, national, regional and local governments can now play a positive role in developing Europe’s business angel market which is currently some 15% of the size of the US angel market. The purpose of the EBAN White Paper is to present the key issues at stake for business angels and their environment in the next few years, and promote the development of a professional and vibrant angel market to the benefit of high

⁴³ Mason Professor Colin M., “Public Policy Support for the Informal Venture Capital Market: A Critical Review”, Hunter Centre for Entrepreneurship, University of Strathclyde, Glasgow, United Kingdom, September 2008, to be published in *International Small Business Journal*, vol. 27, 2009.

⁴⁴ EBAN, White Paper, August 2007, www.eban.org.

growth start-ups across Europe. The White Paper is an invitation to all concerned actors to take action in favour of the proposed initiatives.

The White Paper includes eight key recommendations to consolidate the start-up market segment, grouped into four categories:

Supply side issues: The investors' perspective

1. Leveraging untapped investment potential and activating virgin angels through greater market awareness and angel training
2. Improving the link between different types of market actors to facilitate the growth of companies and exit opportunities
3. Achieving company growth and closing the equity gap
4. Improving SME investment readiness

Environment issues

5. Strengthening the dialogue between business angels and venture capitalists
6. Visibility and market perception
7. Regulatory issues

Fiscal issues

8. Introducing fiscal incentives stimulating business angel investing in all European countries and improving the fiscal environment for business angels in cases when they already exist.

B) The EBAN Statement for Policy Makers:

Following the financial crisis in October 2008, EBAN issued a statement for policy makers about the "Impact of the financial crisis on the activity of business angels and early stage investors - What should policy makers do to make sure that great innovations find access to finance at their early stages?"⁴⁵.

Main finding can be summarised as follows:

- The financial crisis increases the equity gap⁴⁶ - More business angels are needed
- The impact on business angel networks (BANs)
- What can policy makers do to support the early stage investment market:
 1. Attracting more investors to the market
 2. Improve transparency on the market – monitoring angel activity
 3. The role of trade associations and business angel groups
 4. Reinforcing the collaboration between business angels and venture capital funds.

⁴⁵ Source: EBAN www.eban.org

⁴⁶ Equity gap: the phase between 500.000 and 3 million euros where high potential start-ups have the greatest difficulties in accessing finance. In some countries the gap starts from 150.000€ on to 3 million€.

XII) Examples of good practices aimed at promoting the emergence of an informal venture capital culture in the European Union

Exchanges of experiences in the framework of EBAN activities have made it possible to identify a number of practices that contribute to the emergence of a culture that is supportive of the development of informal venture capital activities at national and regional level.

United Kingdom

One of the most attractive BA legislation support is to be found in the UK. Indeed, the EIS (Enterprise Investment Scheme)⁴⁷ is a government scheme that provides generous tax reliefs for investors who subscribe for qualifying shares in qualifying companies.

Individuals may invest any amount in EIS shares. However, only the first £500,000 invested in any one tax year (£200,000 prior to the tax year 2006/07) with a minimum subscription of £500 per company will qualify for income tax relief and capital gains tax exemption. For this purpose a husband and wife are treated separately. Individuals must subscribe a minimum of £500 in any one tax year. Several subscriptions can be combined to meet these limits.

- A 20% income tax relief. This relief takes the form of a credit against an individual's personal tax liability. It is given at the lower rate, currently 20%, of the sum invested subject to there being sufficient tax liability to absorb the relief. Thus the maximum tax credit available to an individual is £100,000 in each tax year.
- Capital Gains Tax (currently at a maximum of 40%) on a gain from the disposal of any asset can be deferred against an EIS share subscription. The tax on any gain rolled over in this way only becomes due on disposal of the EIS shares or if the individual ceases to be UK resident within 3 years of issue of the shares. There is no requirement to obtain income tax relief to qualify for capital gains tax deferral and the amount of the gain which can be deferred is unlimited. To qualify for deferral relief the investment must be made during the period one year before the realisation of the gain to three years after.
- Capital loss: if a loss arises on the disposal of EIS shares then, subject to adjusting for the income tax relief previously claimed, that loss will be available to the investor. This relief can either be claimed as a capital loss or as a loss for income tax purposes.

Investors who defer a gain from one EIS investment to another will be able to calculate their taper relief from the earliest acquisition of EIS shares. This is an exception to the normal rule that taper relief is calculated by reference to the holding of the original asset and frozen at the point of disposal of that asset. This relief is also available to trustees of some trusts.

The money raised by the issue of EIS shares must be wholly applied in qualifying business activities. The funds must be applied within 12 months of the share issue, or where it is a new trade, within 12 months of the start date.

Evaluation of the importance of the EIS Scheme in the UK (PACEC Evaluation 2003)⁴⁸:

>'...an estimated 52%-62% of the monies invested would not have been invested in the absence of the scheme.'

>'...the estimated cost of the EIS in terms of Income Tax and Capital Gains Tax forgone has been 55-66 pence for every additional £1 invested through it.'

>'...for every £1 million in tax forgone, EIS companies are estimated to have increased their sales turnover by £3.3 million and have increased their employment by 65 jobs.'

⁴⁷ For more information about the EIS see also: www.eisa.org.uk

⁴⁸ White Malcom, Presentation at the 2006 EBAN Annual Congress on the Enterprise Investment Scheme (EIS).

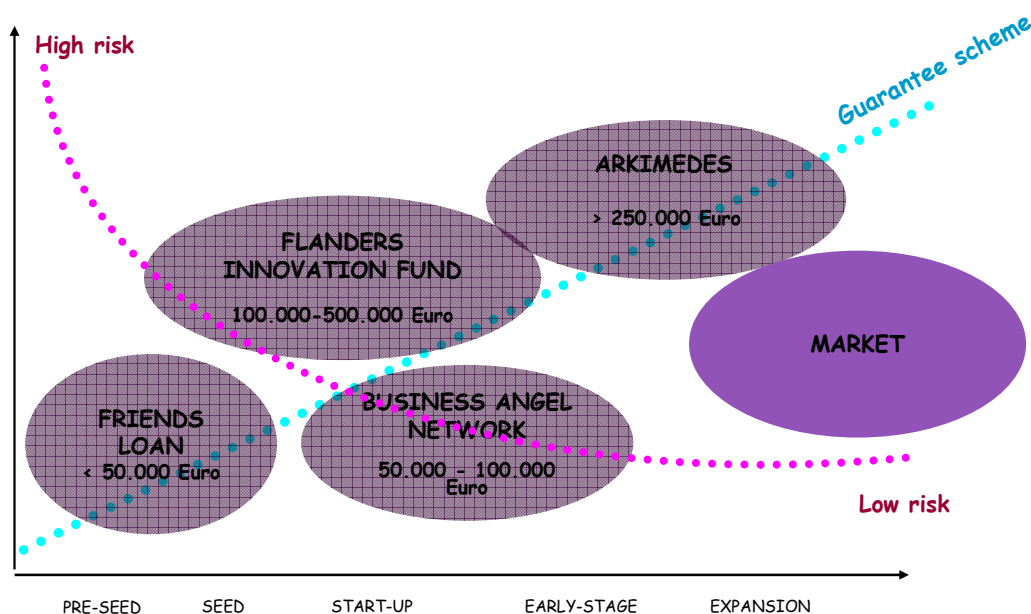
Since March 2005 'The Financial Services and Markets Act (2000)' makes it a legal requirement that Business Angels wishing to receive promotions from firms must be self-certified as either high net worth individuals or sophisticated investors. A sophisticated investor is a person who is knowledgeable to understand the risks associated with the particular description of investment. A self-certified sophisticated investor is an individual who has signed a statement for certified high net worth individuals not more than 12 months when the deal happens. The ability to self-certify simplifies the process where previously accreditation was by an FSA approved third party.

BBA National Angel Investing Awareness Campaign 2009

Also, the British Business Angel Association - BBA has recently gained the support of BERR Department of Business Enterprise and Regulatory Reform to launch a major national and regional awareness campaign. The aim of the BBA Angel Investing campaign is to raise awareness of Business Angel investing and to increase the overall pool of angel investors across the UK regions. Actions will be taken at both national level through a main event and marketing programme and special dedicated web-site as well as regional level awareness events and workshop activities to build the capacity of new angels. Notably the actions are designed to support the actions being taken by the local Business Angel networks and to work directly with the regional development agencies (RDAs) and all professional advisers and intermediaries who are advising wealthy or sophisticated individuals who may be attracted to business angle investing. More information can be found at: <http://www.bbaa.org.uk>.

Belgium

- Favourable Capital gains taxation
- Public support to BAN- in Belgium the active involvement of the public sector has strongly encouraged the BANs to act very professionally and cooperate actively with each other. In 2004, the four networks of the Flemish region merged to create BAN Vlaanderen (www.banvlaanderen.be)
- Promotion of codes of conduct to be able to be part of BEBAN, the Belgian national association of BANs.
- BEBAN awareness seminars with all other enterprises financing key players
- Integrated approach from the federal government:



Friends' loan:

Yearly tax credit: 2.5% / tax payer

>Max. 1250 €/year

Unique tax credit: 30%

>In case of bankruptcy / liquidation

>On the amount definitively lost

Modalities:

>Loan: subordinated

>Amount: 50.000 €/SME/tax payer

>Interest rate: > ½ legal interest rate

< Legal interest rate

>Duration: max. 8 years

>Repayment loan: bullet

>Interest payment: yearly

Guarantee scheme

>Shared risk: 75% Flemish government 25% financial institution

>Amount: max. 500.000 €
if > ministerial authorisation needed

>Duration: 20 years

>Purpose: investment purposes

>Premium & minimal securities required

>First working year: 150 million €
→ 360 million € SME-credits

France

- Savings plan through shares in unquoted companies;
- Risk Capital Company status for favourable taxation schemes;
- A special status is given to business angels in order to protect and encourage private investment in companies in France through the "Uni-personal risk capital investment company (Société unipersonnelle d'investissement à risque)" whereby the BAs will benefit from a tax exemption for 10 years on their investment and on their exit route benefit made during the 10 years of subscription.

The French government has launched a call for proposal in 2006 and 2007 to support the operational costs of BAN for a 3 year period under certain conditions. The call for proposals is available at the EBAN Secretariat in French and English.

The TEPA Law and its Impact on BAs in France⁴⁹

The TEPA (Travail, Emploi, Pouvoir d'Achat) law, adopted in France in August 2007⁵⁰, allows for individual eligible to the wealth tax (Impot sur la Fortune) 50K€ (75%) deduction on early stage investments made by BAs directly or through BA Holdings, and for a 20K€ (50%) deduction only if the investment is made through new Private Equity Funds investing more than 40% in early stage.

Some positive effects of the TEPA law identified so far:

- new BAs and BA networks,
- new syndication structures (Holdings),
- increase of the network investments (80M€)

First results⁵¹ indicate that in 2008:

- 23 management companies have raised capital
- 29 investment funds have been created
- More than 350M€ have been raised (230M€ direct + 120M€ thru 25 new BA Holdings) and 530M€ through Private Equity Funds. 55.000 new individual investors have been identified
- The fiscal products have been used by more than 45 000 eligible contributors,
- or 9 % of persons who are eligible to ISF
- The average amount subscribed was 11 200 €

ISF SME Holdings and foundations

- 25 holdings have raised 120 millions €
- Foundations have raised 50 millions €

Direct investments

- 1 million were raised directly
- Close to 1 billion € collected by 30th of June 2008

Some negative effects of the TEPA law identified so far:

- a demand for investments that exceed the offer: the price of companies has doubled and the amount of capital expected to be received increased (x4)
- unfair competition
- confused BA image (emergence of tax savings motivated investors and gamblers)

Another result of the TEPA Law has been the enhanced collaboration between business angel networks the banks, since banks and private equity money were eagerly looking for deal flow, and therefore

⁴⁹ Philippe Glantz, "The role of banks in leveraging angels activity. The Paris Business Angels Case. EBAN Winter University 2008.

⁵⁰ French Law n° 2007-1223 – 21/08/2007.

⁵¹ ISF SME Source : AFG - AFIC

partnership with BAs structures. This fostered the professionalization of BA structures and networks, thanks to the development of various types of partnerships with banks, such as:

- Sponsoring : hosting of network meetings, funding of general costs , special marketing events
- Marketing sessions: recruitment of new members of networks or BA investment funds as well as new customers for private banks
- Co-investment opportunities, on case by case, with banks and private equity funds, for second or first rounds
- Structured partnerships with Co-investment or side car funds
- Referral programs for retail banks with BA target companies

The FranceAngels Business Angel Week:

Among other initiatives, FranceAngels - the national association for business angel networks in France has been organising once a year now since 2005 the successful initiative called: Business Angel Week. Taking place simultaneously in different cities in France, this week has raised the attention of both the media and the public, and helped to raise awareness about the theme of business angel investing near potential angel investors, entrepreneurs looking for seed finance, and policy makers at the different local, regional and national country levels. More information about this initiative are available at the website: www.franceangels.org

Germany

- Awareness campaigns, training programmes, templates and publications available via the national association BAND
- Business plan competitions linked with local BAN networks and other financial institutions.
- Business angels panel
- Roundtable between BA and VC representatives

Ireland⁵²

- Business Expansion Scheme (BES): Companies can obtain up to 1.000.000€ of equity capital from a BES fund or BES investors. 'Qualifying companies' receiving money from 'qualifying investors' are eligible, with possibility to sell ordinary shares in BES financing. www.revenue.ie
- County and City Enterprise Boards: Proposes low interest loans, grant programmes, and equity financing in the form of redeemable preference shares, which are an equity investment that gives investors the right to redeem their investment. www.enterpriseboards.ie
- Enterprise Ireland provides grants and equity financing to manufacturing or internationally traded services companies. Enterprise Ireland requires that the capital it will invest be matched or exceeded by one or more private equity investors.
- The programme also has a Seed and Venture Capital programme funding several venture capital firms, as well as a variety of support services for entrepreneurs.
- www.enterprise-ireland.com

⁵² Mulcahy Diane, "Venturing forward – a practical guide to raising equity capital in Ireland", Oak Tree Press 2005, p.80-82.

- Equity Network/IntertradeIreland: provides detailed education and awareness programme on the benefits and availability of private equity. Programmes include investment readiness, non-executive director networks, and a centre of excellence on private equity related matters. www.interreadeireland.com
- Seed Capital Scheme: provides tax benefits for entrepreneurs who invest their own capital into their company. www.revenue.ie

Italy

The Italian Association of Business Angels Networks – IBAN (www.iban.it) promoted in spring 2009 a successful lobby initiative together with the Italian Venture Capital and Private Equity Association AIFI and two other active players of the venture capital market in Italy (Assonime and Eversheds Piergrossi Bianchini Lawyer's office). This is a first formal recognition of the importance of the role played by business angels in the financial supply chain in Italy.

The new disposition approved foresees that capital gains realised on both qualified and not qualified participations by private individual investors (i.e Business Angels), not in business capacity, are tax-exempt starting from 1 January 2009, if:

- Participations have been owned at least for three years;
- Participations owned in companies which are at maximum seven years old;
- Participations owned in companies which have realised “industrial/productive” investments;
- Capital gains must be reinvested into “start-up” companies within 2 years the gain accrued.

This kind of disposition, already in force in a few European countries although with some local differences, has a clear potential for replicability across Europe, especially in less mature angel market and countries, such as the Eastern and Southern Mediterranean countries.

Spain:

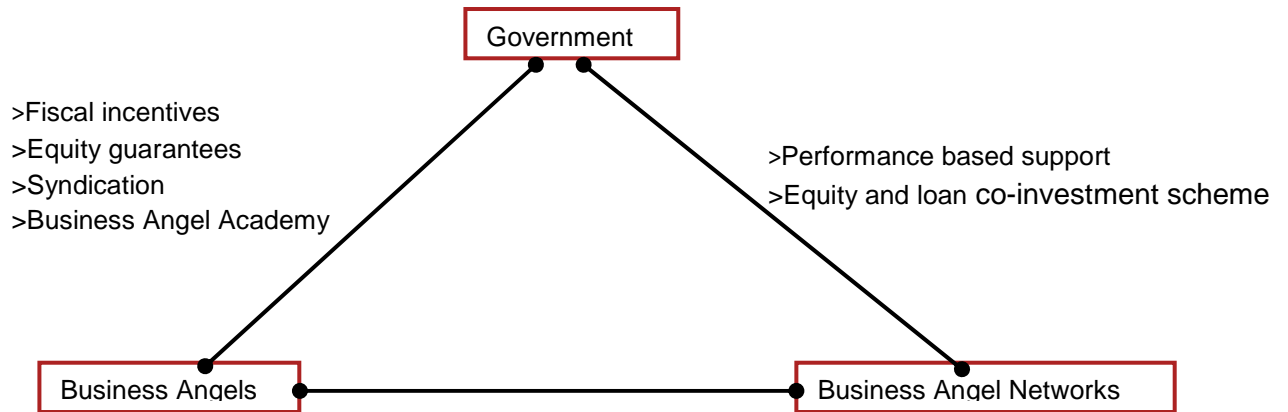
The Catalan parliamentarian group CIU has recently presented a new legal proposition to boost the role of business angels in Spain. The "Ciencia e Innovacion" Commission of the Deputy Congress in Spain approved on April 2009 the law proposition number 161/00858 aiming to regulate the figure of the business angel as an instrument to enhance innovation in the economic sector. The new proposition also urges the Government to establish collaboration between the public administration and the business angel networks in Spain to improve their legal and financial regulation frameworks. Finally, the proposition highlights the importance of fiscal and financial incentives to facilitate and increase investments by business angels in early stage businesses.

The intensive work to promote tax measures for business angels carried out by ESBAN the Spanish Business Angel Network in recent years, has given its first fruits in Catalonia, which will be the first "comunidad autónoma" in the country to launch a first tax incentives for business angels investing: a deduction from the income tax of up to 4.000 Euro in the tax bracket

Luxembourg

Business plan competitions linked with local BAN networks and other financial institutions.

The following graph illustrates the virtuous collaboration triangle between the government, business angels and BANs⁵³.



⁵³ Aernoudt Rudy, Presentation at the 2005 EBAN Winter University, « Efficient networking – successful example of close collaboration between national governments and angel networks ».

The Netherlands:

As of 2009, Minister Van der Hoeven of the Dutch Ministry of Economic Affairs has recently announced to support a 'Business Angel' programme with an annual 2 million euros. Among other things, this boost should help new and innovative companies with solid business plans to attract 'Business Angel' capital. According to estimates, this financial impulse should create a spin-off of at least 25 million euros in additional business finance on an annual basis. One of the initiatives funded by the 2-million euro financial boost is a training programme for both business angels and entrepreneurs. In addition, the funds will be spent on raising awareness about informal investment opportunities and on reinforcing business angel networks in the country. The whole programme will be carried out by the Dutch Business Angel Network (the official name is not known at this stage) to be launched in Q3 2009 in collaboration with TechnoPartner.

XIII) Benchmarking EU angel activity with the US market

According to the data collected by the Angel Capital Association in 2008 the estimate of the number of business angels group operating was 270. There are in 2009 circa 300 angel groups operating in the US. This data is inferior to the number of existing BANs in Europe, which is circa 325. Despite this data, the US market records around 250.000 angels in US, this is three times the number of business angels detected in Europe. In terms of total amount invested annually, the US estimated around 26 billion euro the total invested in 2007, while Europe estimated this amount in the year 2007 in Europe to be around 3 billion euro.

The figures are reported in the table below⁵⁴:

2007	EU	US
Networks	297	245
Estimate n of angels	75.000	250.000
Investment per round	165.000€	210.500€
Total estimate invested annually	3-5 billion€	20 billion€
Total invested by VC annually in seed (EVCA data)	-	4 billion €
		20 billion €

⁵⁴ Source: Compiled information from EBAN, ACA and Center for Venture Research.

CHAPTER 5: FREQUENTLY ASKED QUESTIONS

I) General questions

Why do we need Business Angels?

An entrepreneur can resort to a BA for several reasons.

- Lack of personal assets
- High level of risk of the project
- Need for business experience and contacts on top of the financial requirement

Why is equity capital attractive?⁵⁵

- No repayments: equity capital comes without the burden and cash-flow drain of the monthly repayments required by debt;
- Value-added capital: equity investors can offer, at least in theory, much more value to a company than just capital. Business angels and venture capitalists can bring industry expertise, customer and strategic contacts and proven experience in helping young companies grow;
- Deep pockets: equity investors may be a source of follow-up financing if the business requires it a later time, adding a sense of financial stability to a growing company;
- Increased discipline: external investors can bring new and higher levels of financial discipline, as well as greater requirements for good governance to your business;
- Enhanced reputation: an equity investment can meaningfully improve the reputation and status of a company, which can help to attract employees, acquire customers, and interest future investors.

What is the magnitude of business angel activity in Europe?

No comprehensive statistics are available on the number of business angels operating in Europe or the amounts they invest. This is due to the fact that they operate in total discretion and that not all are members of a network. EBAN estimates an average of 297.000 business angels active in Europe in 2007, with around 16.487 business angels member of networks, based on the aggregate data provided by the national federations of BAs⁵⁶.

Can business angel networks operate for profit?

Very few networks operated on a for profit basis when EBAN started to collect information on the angel market in Europe in 2003. In 2007, 36% of the networks in Europe operated on a commercial basis, according to statistics data collected by EBAN in 2008. The growing number of business angel networks run for profit is due to different factors, among which the development and stabilization of the business angel market in some Western European countries. An increasing number of add on services offered by the networks to their members as well as the introduction of a for profit management are part of the solution to the self sustainability of the networks, which, especially in some Western countries, are faced with financial constrains due to the decreasing financial support coming from public institutions.

⁵⁵ Mulcahy Diane, "Venturing forward – a practical guide to raising equity capital in Ireland", Oak Tree Press 2005, p.5.

⁵⁶ EBAN, Statistics Compendium 2008, www.eban.org

What differences exist between informal venture capital (i.e. business angels) and formal venture capital (investment capital)?

Business angels invest their own assets and contribute their managerial skills, whereas venture capitalists invest the funds of others. Business angels also invest lower amounts than venture capitalists. They tend to be involved in the early stages of a business’s lifecycle and their expectations in terms of ROI are more modest. Moreover BAs make their decisions of the future growth of a new business while venture capitalists are looking to the past records of already existing companies.

Key differences	Business Angels	Venture Capitalists
Personal characteristics	Entrepreneurs	Financial managers
Invested funds	Own money	Fund investors’ money
Investees	High potential start-ups and early stage	Medium-sized to large growing companies
Due diligence	Experienced-based Lower cost	More formal Expensive
Geographical proximity	Important	Less important
Form of contract	Simpler deal structures with emphasis on fairness	Complex and demanding
Post-investment monitoring	Active, hands-on	Strategic
Involvement in management	Important	Less important
Exit route	Less important	Very important
Return on investment	Important, but probably less demanding overall because of lower costs of the investment process	Very important

What are the benefits of syndication for business angels?

A grouping of several business angels allows:

- Increasing in the level of financing of a project (usually up to 2 m€) and providing follow-on finance for subsequent rounds
- Diluting the risk to take for individual investors
- Enables to broaden the panel of possible investment sectors. For instance, in biotechnology, the investment level is so high that it renders syndication almost compulsory, as business angels are unable finance projects in this type of high-level finance sectors on an individual basis. It is also a leveraging mechanism for business angels and a way to share network contacts and investment expertise.
- Attracting virgin angels to invest alongside experienced angels.

According to a study conducted by Colin Mason in 2005, angel syndicated reduce inefficiencies in the market including by making informal investors more visible and syndicates are also more credible in the eyes of venture capitalists than individual investors (perception that deals are less complicated)⁵⁷. - Finally, in some countries syndication allows for eligibility to a fiscal regime equivalent to that of formal risk capital investors.

⁵⁷ «Informal sources of venture finance» Colin M Mason, Hunter Centre for Entrepreneurship, University of Strathclyde, August 2005, To be included in Simon P. 39.

In Denmark, “a total of 66% of angels have co-invested with other investor types within the last year. This means that Danish Angels syndicate more than their British counterparts, but less compared to business angels in the US. Only 8% of business angels prefer to invest alone. Those angels who have not made any syndication claim that it is due to not being able to find either the right investors or the right investment” “When Business angels syndicate, it is more likely to be with other angels. One-fifth syndicate with venture capitalists. The angels describe the relationship with the formal venture market as being valuable although they acknowledge that any collaboration with VCs is not without problems. The angels fear there is a serious risk of their stakes in companies of being “washed out”, when the venture capitalist enters the investment”⁵⁸.

Syndication can also present some disadvantages:

- More time being spent
- More hassle in closing a deal if one person falls out at the last minute
- Less direct involvement in the investment
- Frustration if the syndicate is poorly led.

A NESTA⁵⁹ study from January 2006 and prepared by Stephen R. Carriere summarises the advantages and disadvantages of syndication:

The realities of angel syndication	
Benefits	Drawbacks
Reducing risk (Portfolio theory)	False sense of security – underestimating risk.
Additional bargaining power and the ability to participate in future rounds.	Makes deals more complex, more formalised, therefore longer decision making, choosier in investments.
Ability to learn from more experienced investors.	Difficulty in working with many different personalities.
	Complications with multiple lead investors.

❁ Why should local/regional authorities subsidise the early years of a BAN’s operation when business angels are, by definition, wealthy individuals?

Business angels networks play a role that is in the public interest as they contribute to bridging the equity gap—thereby solving a market failure—and to the activation of inward potential, both in terms of entrepreneurial culture and in terms of mobilising private capital. The leverage created by business angel networks’ intervention is very powerful, and at extremely low cost per job created for regional/local authorities. In the United Kingdom, statistics have shown that the cost per new job created as a result of a BAN’s intervention is in the area of 3,000€. In Europe as a whole, the average cost of public support per successful deal was under 10,000€ in 2000.

⁵⁸ Kjaergaard Rolf, Napier Glenda, and Nordstrom Borup Jacob, “Business Angels in Denmark”, 2002.

⁵⁹ Carriere Stephen R, « Best practices in angel syndication” in association with NESTA and BBAA, January 2006, p.26.

Finally, business angel networks are actually not in the best of positions to demand that entrepreneurs or business angels contribute financially to their running costs as businesspersons are looking for equity while business angels are looking to supply equity. It is therefore quite difficult to contemplate asking either to contribute heavily to the functioning of a network. However, some BANs are remunerated when a matching operation is concluded (success fee). Consequently, a BAN's budget will often depend on sponsorship, subsidies or its links with a business support services provider.

In Flanders (Belgium), regional authorities have granted newly created BANs a flat-rate yearly subsidy of 60,000€ for the first three years until 2003. Since 2004, the regional authorities announced that their support was conditional on the merger of the 4 BANs operating on their territory. Business angels want to fund companies for which entrepreneurs do not have money for, or have been denied start-up capital from banks. As a consequence, the need to support strengthened intermediary structures which can provide with advanced add on services to their members and entrepreneurs.

Are there practical examples of businesses that grew thanks to business angel intervention?

Of course, there are! Some very famous examples include Amazon.com, Apple, Body Shop...

More recent examples include:

- Easy design and self-print solutions VISTAPRINT;
- Networking platform OPEN BC;
- XING
- STARBUCKS
- Facebook, Twitter

What is the level of association of Business Angels?

Business angels are part of at least one association or business angels network (the most part being a member of 2 or 3). However, these associations tend to be regional ones and few BAs like to do business outside their usual "business circle". This forces BAs to seek by themselves investment possibilities and renders their real contribution to enterprise creation less visible.

Are any reference books, publications or web sites available on the informal venture capital industry?

Yes, there are. Below are a few useful references:

- Mason Colin M., "Public Policy Support for the Informal Venture Capital Market: A Critical Review", Hunter Centre for Entrepreneurship, University of Strathclyde, Glasgow, United Kingdom, September 2008, to be published in *International Small Business Journal*, vol. 27, 2009.
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- When Venture Capitalists say “NO”- Creative Financing Strategies and resources, Ron Peterson, Comanche Press MD 2003.
- Business Angel – Une solution pour financer les start-up, Gildo Pallanca-Pastor; Jean-Paul Cailloux ; François Cazalas. Published by Editions d’Organisation in 2000.
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- Rudy Aernoudt and Hilde Goossens, Business Angels, Rare vogels of ware engelen, Roularta Books, 2002.
- Mari Mustilli and Mario Sorrentino, Business Angel in Italia, G. Giappichelli Editore, 2003
- European Commission, BEST Report, No 1, “Benchmarking Business Angels”, 2003.

Links and organisations of interest:

- The European Trade Association for Business Angels, Seed Funds, and other Early Stage Market Players - EBAN, (EU): www.eban.org
- The World Association of BA network leaders – WBAA, (Int): www.wbaa.biz
- Angel Capital Association – ACA, (US): www.angelcapitalassociation.org
- National Angel Organisation – NACO, (CA): <http://www.angelinvestor.ca/>
- British Business Angel Association – BBAA, (UK): <http://www.bbaa.org.uk/>
- European Commission, DG Enterprise and Industry – Access to Finance: http://ec.europa.eu/enterprise/policies/finance/risk-capital/business-angels/index_en.htm
- Angel Investor, Wikipedia: http://en.wikipedia.org/wiki/Angel_investor



***What are the advantages and shortcomings of a business angel network?*⁶⁰**

Advantages	Limitations
Provide easier access to potential investors than an individual search	May be too localised
Provide a pool of experience which benefits less-experienced investors and entrepreneurs (some provide training)	May lower their acceptance thresholds for venture proposals to attract enough investors which lack skills to access start-up capital
Stimulate demand for private equity finance, by promotional actions	May need to improve quality of screening of proposals
Preserve privacy of investors, protecting them from unsolicited demands	Angel network officials not able to offer advice or recommendations due to legal liability
Improve the quality and reliability of information moving between investor and entrepreneur	Many angels are very independent and reluctant to join a formal network
Provide a forum for discussion	Financing a network may need public support as unlikely to cover cost from fees
Able to interact with business incubators and with technology commercialisation officers of universities.	Dependent on the quality of the manager
Opportunities for training, syndication and co-investment	

⁶⁰ CORDIS Innovation Papers, “Informal investors and high-tech entrepreneurship”, NO 12, p.50.

II) For the potential BA: do I fit the business angel profile?

✿ *How much capital do I need to invest?*

There is no minimum not maximum to invest. Investors should know that business angel investing is a risky business, which can bring amount many benefits but also many losses. You should invest what you can afford to lose.

✿ *How can I identify business opportunities?*

Here is how business angels identify new investment opportunities in Sweden⁶¹:

Source of information	Importance		
	Important (%)	Neutral (%)	Not important (%)
Business associations	66	15	19
Active personal search	59	10	31
Business angel networks	57	13	29
Entrepreneurs making contact	44	19	37
Family and friends	36	16	48
Venture capital firms	27	14	59
Media	22	20	58
Banks and stockbrokers	22	18	60
Accountants	22	12	66
Solicitors	20	14	66
Non-profit organisations	15	9	76
Governmental organisations	7	5	88

In Wales, the sources of opportunities considered are the following:

Source	Importance 1 (none) to 5 (most)
Xénos – the Wales BAN	3.96
Business Associates	3.48
Other	2.67
Friends	2.44
Other BANs	2.09
Accountant	2.09
Media	1.79
Solicitor	1.60
Stockbrokers	1.37

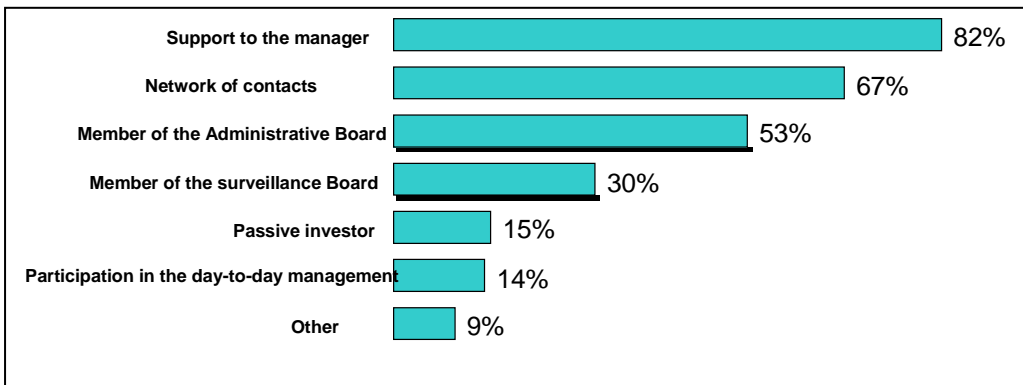
⁶¹ Mansson Nils and Landström Hans, "Business angels in a changing economy", 2005, p.35.

• **What is the average size of a deal (in the first round of investment) in Europe?**

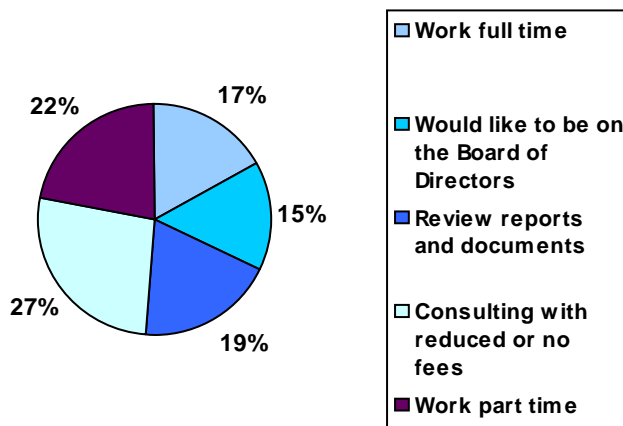
According to research conducted by the EBAN Secretariat in 2008, in 2007 the average size of deals in the majority of European countries was 165.000€, while in the UK in 2008 the average was 327.628€ (including co-investment funding). Business angels can invest less, or more especially if co-investing with other angels.

• **What is the role of the business angel involvement in the venture?**

In France⁶²



In the US⁶³



• **What returns can I expect?**

Business Angel investments are generally high risk, so the returns can be extremely good. But recent research among existing Business Angels has shown that one in three investments resulted in the total amount being lost. However, one in five investments provided a cumulative return of 50% or more per annum.

⁶² Result of the 2003 French Business Angel Survey conducted by France Angels, www.franceangels.org
⁶³ www.1000ventures.com

Results of the research recently undertaken by Professor Rob Wiltbank on angel group financial performance in the US and the UK⁶⁴, and sponsored by the Marion Kauffman Foundation and to NESTA in the UK, report that business angels stand to make a substantial profit from investing in start-ups, with an average Internal Rate of Return (IRR) of 22 per cent over four years, compared with 27 per cent IRR in the US.

Outcomes of the researches produced showed a similarity in the types of investment performance in each country. Some noticeable themes as identified during the presentations these results at the occasion of the EBAN Congress 2009 in Madrid⁶⁵ are:

- Returns are improved by doing greater due diligence and by having a regular mentoring or board position at the company
- They are also improved by having expertise in the industries in which your portfolio companies operate
- Angels need to invest patient capital as the best investments can take six or more years to mature and exits successfully
- Statistically, the volume of investments required to get a winner which returns more than 30x your investment is 30 or more
- But a significant amount of angels do not make money on their investments

In terms of differences between the UK and the US, the principal ones were:

- UK angels have a greater variation in work experience
- UK angels lose more deals than their US counterparts and get less really big wins but outperform the US in terms of achieving exits in the 10x-30x range.
- UK angels hold their investments marginally longer than US angels
- UK angels invest in later stage opportunities than US angels.

Colin Mason from the Hunter Centre of Entrepreneurship in Strathclyde, Scotland, has done a study on angel investment returns⁶⁶. The key findings are the following:

127 angels responded/372 investments made/51 angels had exits, 128 exits in total (90% occurred between 1985 and 1996).

- 34% of investments involved total loss;
- 6% involved partial loss;
- 8% broke even;
- 7% had return of under 10%;
- 7% had a return of 10-24%;

⁶⁴ The researches analyse responses received from 538 angels in the US and 158 angels in the UK, and examine 3,097 investments and 1,137 exits and closures, and 1,080 investments and 406 exits in the US and in the UK respectively. Sources: Robert Wiltbank, "Siding with the Angels - Business angel investing – promising outcomes and effective strategies", NESTA - BBAA Research Report: May 2009, and Wiltbank Robert, Willamette University and Boeker Warren, "Returns of Angels Investors in Groups", University of Washington, publication supported by the Ewing Marion Kauffman Foundation and Angel Capital Education Foundation, November 2007.

⁶⁵ Summary of the Madrid 2009 EBAN Congress session: "How much return on investment do angels really make? A UK/US Benchmark" by Modwenna Rees-Mogg, moderator of Day 2 of the conference.

⁶⁶ Study conducted in 1998/1999, questionnaire distributed through business angel networks in the UK.

- 13% had a return of 25-49%;
- 25% had a return of over 50%.

In comparison with early stage venture capital funds:

- Business angels have significantly fewer investments losing money (40% vs. 64%)
- Business angels have significantly more investments, which break even or generate low returns (24% vs. 7%)
- Business angels have a similar proportion of very successful investments (23% vs. 21%)

In Wales, the data is the following concerning the result of exiting investment⁶⁷:

Full loss	7	26%
Partial loss	5	18%
Break event	4	15%
Profit	11	41%
Total	27	100%

In the United Kingdom, the analyse of deal flow, deal characteristics and deal closing in a regional BAN in the UK⁶⁸ in 2006, showed the following key fundings:

- Only 3% of initial company enquires result in a closed deal
- The largest attrition rate (75%) occurs in the stage from formal enquiry to registration
- On average companies are likely to receive half the funding sought (£182k cf £83k) and a typical company (median) is likely to receive about one-third (£150k cf £50k)
- 28% companies registering with the BAN receive offers and 57% will accept the offer for angel investment
- The offer rate is higher for companies presenting to gatherings of business angels than from printed bulletins, but there is more chance of an offer being accepted from the latter than the former.

In the US, the main findings of the study “Returns of Angels Investors in Groups”⁶⁹ based on results received from those investments from which the investor has exited only were the following:

- As a group, the risk taken by these angels is rewarded with overall returns—2.6X in 3.5 years;
- In any particular venture, an angel investor is more likely to lose than to make money, and a significant portion of the angel investors in this sample experienced a return less than 1X.
- Angel investing can be done well in the pursuit of legitimate financial returns.

⁶⁷ Hurcombe Ray, Davies Leanna, and Marriott Neil, “Business Angels in Wales: putting some boundaries on our ignorance”, 2005, p.27.

⁶⁸ Neil Marriott and Leanna Davies “Deal flow, deal characteristics and deal closing in a regional business angel network”, Institute for Small Business & Entrepreneurship, United Kingdom, October-November 2006.

⁶⁹ -Wiltbank Robert, Willamette, University and Boeker Warren, University of Washington, “Returns of Angels Investors in Groups”, supported by the Ewing Marion Kauffman Foundation and Angel Capital Education Foundation, November 2007.

Do I need business experience?

Business Angels are actively involved in the company and will therefore need business skills in order to achieve the potential of the company in which they invest and accelerate the growth of the company. Angels are often entrepreneurs themselves or have a solid entrepreneurial experience, as their role is also to provide expertise to the company in its first stages. We have seen earlier that in Sweden, as much as 90% of the angels had created a one or several companies.

If your business experience is limited, you should consider aligning yourself with an experienced Business Angel in a syndicate.

What control will I have over my investment?

This is for personal negotiation with the company, and much will depend on the agreement. Generally speaking, the greater the percentage of shares you acquire, the greater your control; but you should seek professional advice before signing a contract.

How much time will I need to devote to the company?

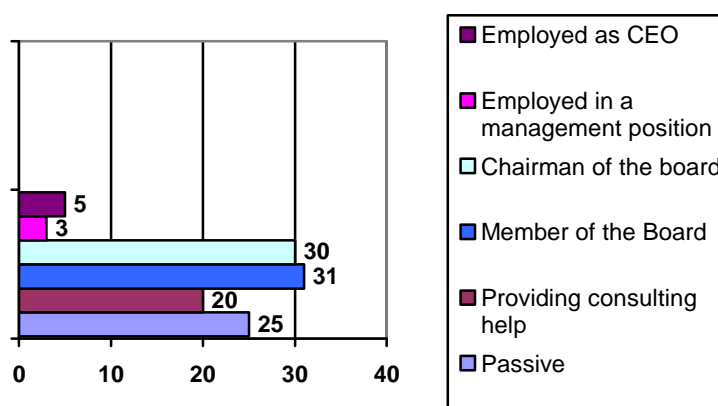
Research shows that, on average, the Business Angel will spend about ten hours a week dealing with the company's affairs. The precise nature of your involvement, however, should be agreed in advance. If you have specific skills to contribute, the company should welcome your involvement; on the other hand, some Business Angels have interfered too much and alienated the executives who are primarily responsible for the success.

The 2002 study on business angels in Denmark⁷⁰ argues that “the investment horizon is 3-6 years on average. During this period the angles act as highly active investors. Forty-two percent of respondents spend 1-1 ½ days a week in each portfolio firm. Their involvement in the firm is mainly as members of the board. But also assisting in design of business plans, attracting other investors and monitoring the financial development in the firms are common activities. The angels are –although to a smaller extent– also engaged in product development”.

Moreover, Sohl and Sommer⁷¹ explain that it took venture capitalists and corporate investors on average five to six months to close a deal in 2001. The average length of time spent by angels considering an investment opportunity had increased for 3 to 4 months from 2000 to 2001.

In 2001 business angels spent an entire extra month or 25% more time on performing due diligence than they did in 2000.

Here are the roles taken by Swedish business angels in the companies they invest in⁷²:



⁷⁰ Kjaergaard Rolf, Napier Glenda, and Nordstrom Borup Jacob, “Business Angels in Denmark”, 2002, p.5.

⁷¹ Sohl Jeffrey E. and Sommer Bruce, “Angel investing: changing strategies during volatile times” p. 22, 23.

⁷² Mansson Nils and Landström Hans, “Business angels in a changing economy”, 2005, p.31.

☀ ***Is there any way I can learn from experienced Business Angels?***

Many BAs organise investor clubs and company presentations that are attended by other Business Angels who are normally willing to talk about their experiences. You might also consider joining a syndicate which is a practical way of putting together larger deals and enables first-time Angels to gain experience with a lesser risk.

III) For the entrepreneur looking for equity capital

☀ ***What are the essential assets of a project?***⁷³

In order to draw the attention of a business angel, a project should preferably have the following characteristics:

- Be documented on a realistic financial plan;
- Include a clear marketing and market penetration strategy;
- Rely on a product that can be sold rather than one that is agreeable;
- Be supported by a managerial team of undeniable competence;
- Present an exit route for business angels based on a realistic evaluation of the company at the time of the exit.

☀ ***How can I get the right valuation for my company?***⁷⁴

- **Know your sector:** do what the investors do? Research the public and private companies in your sector that compete with you and are similar to you. Understand their valuations, what drives their performance and price, how both the IPO and trade sale markets value these companies;
- **Know your metrics:** from public company filings, industry reports, press releases of competing companies and industry associations, understand how companies like yours are measured. What metrics are used to measure and signal performance? What are some industry averages and ranges? How does your company compare? If the metrics currently used don't really apply to your company, which ones are you suggesting that will signal performance, and why?
- **Develop a valuation range:** you want to begin to develop a range of valuations for your company, based on both the sector and metric information you've evaluated so far. You will also need to educate yourself about what the "going rate" valuations are in your market. Talk with other entrepreneurs and advisors about current valuations, and keep up with IPO and acquisition valuations in your local market. You should decide where within that range you would feel like you got a good valuation. This helps you have a number in your head when you meet with the investor.
- **Build your case:** Conduct your own valuation analysis of your company and be ready to present a well researched and factual argument about your company valuation. Incorporate specific comparable valuations and performance metrics into your case, as well as company-specific factors that can justify a higher valuation, including:
 - A strong and experienced management team (most important);
 - The existence of other investors who are interested in / bidding on the deal

⁷³ C2 Ventures Investor Pulse UK Angel Attitude Survey, « A qualitative survey into UK Business Angel attitudes, preferences and views in 2002 and 2003», p.20.

⁷⁴ Mulcahy Diane, "Venturing forward – A practical guide to raising equity capital in Ireland", Oak Tree Press, 2005, p.38-10.

- Being in a “hot” sector or market
 - Strong IPO or trade sale markets with high valuations
 - Having paying customers
 - A strong sale pipeline to support revenue and growth projections
 - Intellectual property ownership or other competitive advantage/barrier to entry.
 - Value killers are all the opposite. Other common value depressors are:
 - A hairy deal
 - An over-priced earlier round
 - Difficult early investors and board members.
- **Negotiate:** While the old adage “you get what you negotiate” applies here, there are factors beyond your negotiating skill that will influence your ability to obtain higher valuation. There are several factors that can increase your negotiating leverage:
 - General interest from more than one investor
 - General interest from more than one investor
 - General interest from more than one investor (it is hard to emphasize this enough)
 - If you are a serial entrepreneur, your credibility is your currency and you will have better negotiating outcomes than a first-time founder.
 - Raising capital early, before you need it, give you negotiating leverage, since you have the advantage and ability to walk away from a mediocre deal and the time to create other alternatives.

No matter how strong and compelling and airtight your case is, you will ultimately only get a valuation that an investor is willing to pay. In general, equity investing is, and will remain, a buyer’s market. Nonetheless, doing your homework and preparing to argue for the best valuation you can justify will help you avoid you can justify will help you avoid a mis-priced round, impress investors, and contribute to your financing strategy.

What does it take to impress an angel?

Because angels invest their own money, they are usually careful when they look at an investment. The factors that can make them confident are:⁷⁵

- Something they understand, ideally a business from an industry they’ve been associated with;
- Something they are passionate about – angels can always leave their money in the bank, so an investment has to interest them;
- Management they trust, respect and like;
- Something they can bring added value to;
- Deals that don’t require huge sums of money – or additional rounds of angel money.

The latest study in Wales⁷⁶ underlined the following factors influencing the angels’ ability to invest (1 having the least effect, and 5 the most effect:

⁷⁵ www.inc.com/articles/2001/03/22375.html

⁷⁶ Hurcombe Ray, Davies Leanna, and Marriott Neil, “Business Angels in Wales: putting some boundaries on our ignorance”, 2005, p.28.

Insufficient quality deal flow	4.02
Insufficient deal flow	2.80
Insufficient available time to work with investee companies	2.79
Insufficient available time to evaluate opportunities	2.63
Narrow investment criteria	2.49
Insufficient available invest funds	2.38
Insufficient experience in business angel type investments	2.11
Other	1.67

But remember, chances of raising equity finance are relatively, as shows the study conducted by Envestors illustrating what happens to business plans presented to investors⁷⁷:

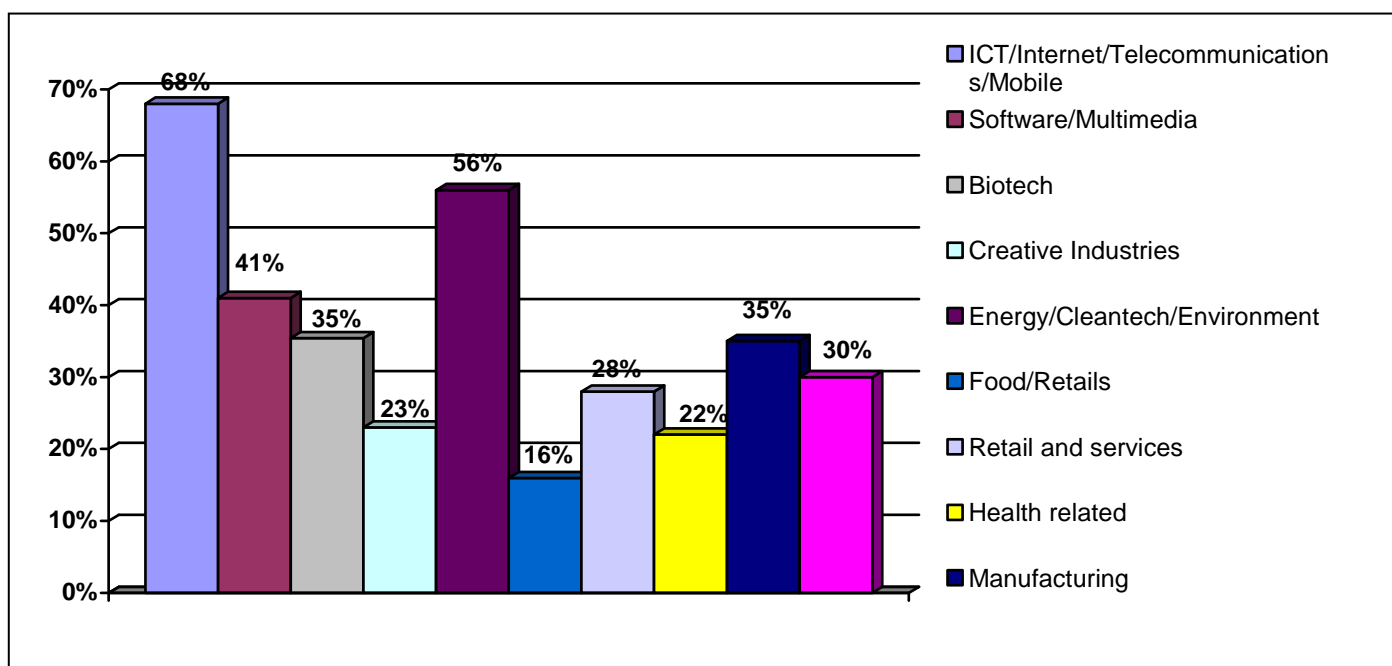
- 60% are rejected after a 30 minute review;
- 25% are rejected after a 3 hour appraisal;
- 10% are rejected after a full day evaluation:
- 3% re rejected following failed negotiations;
- 2% succeed in raising funds.

Also, Dragons' Den is a well known UK BBC TV programme, where private individuals (Dragons) back young business with high potential. Although the programme is a fiction of the real world of business angels investing, it showcases how business raise money from private investors, and good examples of pitching of business ideas.

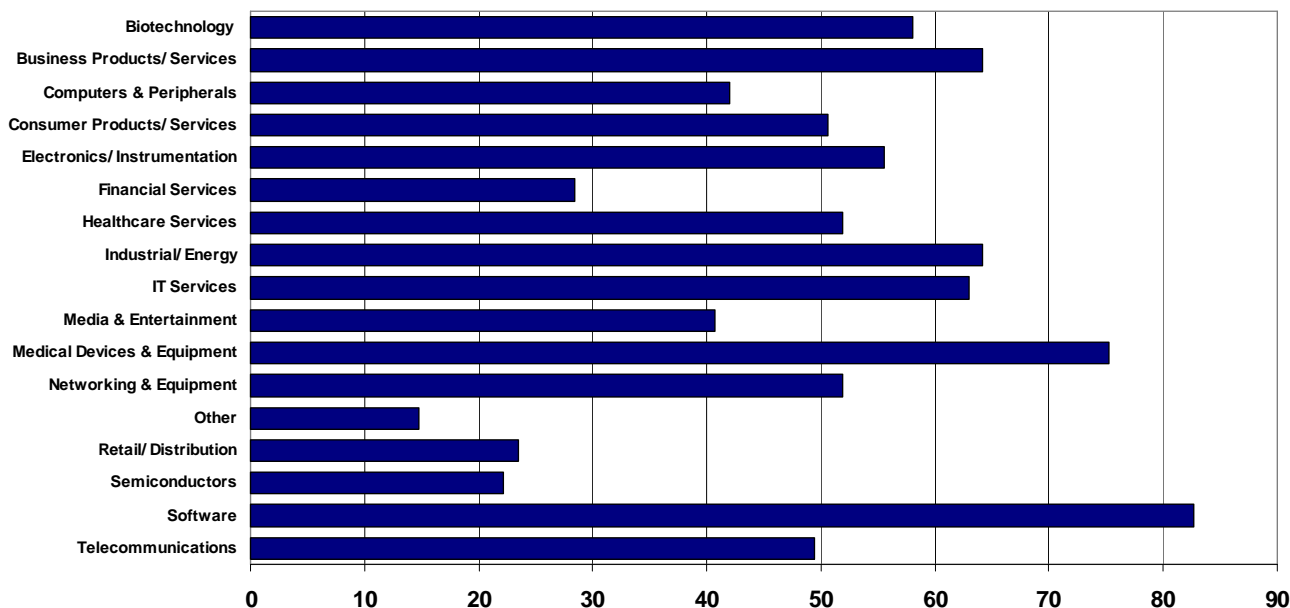
Through the critical review of this show, the newly published "Dragons or Angels" book reveals the ways business angels are looking for companies to invest in, and use their money and expertise to transform them⁷⁸.

What type of company do business angels invest in?

The table below indicates the percentage of networks that invested in each of the sectors out of total networks replying to the question: *Sectors of investment of the deals concluded through the networks in 2007, in 2008*⁷⁹.



In comparison, here is the data from the Angel Capital Association Confidence Survey⁸⁰



What amount of money can I raise from Business Angels?

Generally between 25,000€ and 250,000€, and up to 400,000€ in the UK - although the sums can be higher, in which case they will often concern a syndicate of investors. Often, the injection of cash by Business Angels enables the company to leverage substantial funds from other sources.

Will I need to sell shares in my business?

You must be willing to sell a percentage of the issued share capital in exchange for funding. This will provide a strong capital base and, if you choose the right investor, valuable additional skills and experience. To ensure that your interests are protected, you should seek professional advice when structuring your deal.

Do I need to pay the business angel for the time they spend working on my business?

This is something to be negotiated between the company and the investor and will often depend on other elements in the deal. However, as the Business Angel will be holding equity, their principal concern will not be with earning fees or salary but with the long-term success of the company. Sometimes Angels may feel that the company must recognise the value of their time and make a charge, although this is often deferred until the company is profit.

How can I expect a business angel to help me?

Again, this should be defined in the initial agreement. Business angels are typically successful business people in their own right and research has shown that they can contribute strategic advice, marketing, finance and accounting skills as well as networking (especially with potential customers and other sources of finance).

⁸⁰ ACA Angel Group Confidence Survey – Investment preference 2007-2008

🌟 **How much does it cost to raise finance?**

According to Envestors, here are the things to keep in mind when raising finance⁸¹:

- Be investment ready before marketing your opportunity to investors to make sure you have collected all the necessary legal, financial and market information;
- Allow around £5.000 to pay for all the legal fees associated with closing an investment deal;
- If you are raising bank debt you will have to pay arrangement fees of around 1% of the amount;
- Most investment funds will require you to pay monitoring fees once the funds are in place.

🌟 **How long does it take to conclude a business angel agreement?**

It can take up to 12 - 15 weeks to raise equity funding and finalise the legals. However, research shows that funds are usually transferred within one month of a first meeting.

🌟 **How to close a deal?**

Closing an investment deal will require extensive legal documentation, which can include the following elements⁸²:

- ✓ Shareholders Agreement, which sets out the relationship between the shareholders. This covers areas such as who should be the directors, non-compete undertakings and any other matters which the shareholders wish to keep private.
- ✓ Subscription Agreement/Investment Agreement, (sometimes combined with the shareholders agreement) which sets out the terms of the 'share subscription', including pre-conditions for the investment (e.g. the current owners to sign service agreements, the transfer of all intellectual property and goodwill to the company and confirmation of bank finance), warranties about the existing business and any options or bonuses to be awarded to the managers.
- ✓ Service Agreement, i.e. the employment contracts with the managers/directors, incorporating non-compete restrictions.
- ✓ Disclosure Letter, making disclosures against the warranties in the Subscription Agreement.
- ✓ Employment Contracts, with more junior managers and staff.
- ✓ Other contracts, for key suppliers or customers.
- ✓ Memorandum, which sets out the formal powers of the company (e.g. to borrow money, to carry on its business) and the company's authorised share capital.
- ✓ Articles of Association, dealing with the company's internal regulations (e.g. proceedings at shareholders and board meetings) as well as incorporating shareholder rights (voting, dividend etc) and minority protection. Articles are publicly available from Companies House.
- ✓ Share Options, usually under the Enterprise Management Incentive (EMI) scheme.

In the framework of the EASY project (Early Stage Investors for High Growth Business) a series of tools and common procedures have been developed to support international deal- structuring and new quality standards for BANs and Seed Funds.

These tools, which are set out in the EASY Toolkit, include:

⁸¹ Envestors, "A simple guide to raising finance up to £2m", p.11.

⁸² « A guide to investing as a business angel », www.envestors.co.uk

- International investment readiness diagnostic and good practice model
- Model for selection and profiling of international business propositions
- Cross-border business valuation tool
- Due diligence checklist for transnational deal structuring
- Transnational deal tracking platform
- Quality standards framework.

For more information visit: <http://www.earlystageinvestors.org/>

🌟 ***How to structure and execute a trade sale in a professional way?***

Roland Koo⁸³ summarises the Golden Rules for the entrepreneur:

- Create value
- Get the consent of shareholders
- Involve the management
- Do not forget your business in the deal making phase
- Always have alternatives
- Allocate enough resources
- Be proactive and control the process
- Work fast with a high level of discipline
- Think strategic and win/win.

🌟 ***How can I evaluate the benefit of a BA involvement in my business?***⁸⁴

You can ask yourself the following questions:

1. To what type of situation/issues have the angels brought the most expertise and assistance;
2. What value have they added? Have they provided introductions and referrals to investors, customers or suppliers? Or are they just a source of capital?
3. How have they behaved when the business has not gone according to plan or the company has missed its projections?
4. Did the company need follow-on capital and did the investor provide it?
5. Have they been supporting in later rounds of financing? Do they participate in follow-on rounds?
6. Are they active or passive investors? To what level are they involved in the company's operations? Or the company's board?
7. Would you work with this angel again?

⁸³ Koo Roland, Executive Director, Austriamicrosystems AG. Presentation made during the 4X4 Forum on Entrepreneurship held in Louvain-la-Neuve, Belgium, on 18/19-11-03.

⁸⁴ Mulcahy Diane, "Venturing forward – A practical guide to raising equity capital in Ireland", Oak Tree Press, 2005, p.97.

• **What is the secret of the deal chemistry?**

A deal between an entrepreneur and a business angel is possible if and only if they share a minimum set of values when it comes to the business project and if their interpersonal relationship is based on mutual trust.

According to a business angel, the preconditions of deal success generally include:

- Cooperation: will he (the business angel) become a real member of the management team?
- Commitment: can the team implement the business plan?
- Competence of the management team
- Charisma: will the BA be able to transfer his know how and not to impose it?
- Chemistry: Does the BA believe that he will co-operate with the entrepreneur?

The typical entrepreneur's expectations of a business angel's contribution include:

- Chemistry: does the entrepreneur believe he will co-operate with the BA?
- Competence: what is the complementary management knowledge that the BA will bring to the entrepreneur?
- Conditions of the BA participation: share of responsibility, modalities of the involvement, objectives...
- Contacts: How can the network of contacts of the BA benefit the entrepreneur?
- Flexibility: with regards to the business plan for example, and ability to listen.

According to a survey made by Venture Capital Report (UK) and Oxford University (UK) with a sample of 500 BA, their main criteria for assessing a proposal are:

- Impression of the management team;
- Experience and understanding of the sector;
- Projected profitability;
- Business plan content and presentation;
- Attractive return on investment;
- Location.

 ***How can I get more information?***

You can visit the European Trade Association for Business Angels, Seed Funds and other Early Stage Market Players website at www.eban.org or contact the EBAN Secretariat:

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