



Stanford eCorner

Defensibility Through Regulatory Constraints

Jim Breyer, Accel Partners; Chris Larsen, Prosper Marketplace

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Larsen and Jim Breyer, Managing Partner at Accel Partners, stress the value of having approval in a regulated industry. This provides an excellent barrier to entry and is very attractive to VCs. Larsen draws on his experience from E-Loan and Prosper in suggesting that while it is cumbersome, if an idea is in the interest of the consumer, it is not difficult to obtain approval.



Transcript

I actually encourage you to look for those industries that have some really tough regulatory hurdles because when you get through them, it really put some distance between people coming around, it's probably two years' lead time. People read about us and say, "Hey, I'm going to start that." versus somebody's companies that are more like products or features which you can do that pretty fast. So those are some of the bigger ones. Yeah. I really want to get to the regulatory issue because in Silicon Valley for all of the virtues of startups here the last three months I was telling Tom Bayers we certainly are seeing now a lot of business plans where it's You Tube meets X, Facebook meets adult entertainment, you name it crazy stuff. But there's just no doubt in a lot of cases we ask people, "Well, what do you think your defensibility is? How much of a lead do you think we have?" And they'll come back and they'll say, "Well, we think we have a two-month lead." And I step back and I say, "It is changing pretty darn fast." And so, that defensibility through regulatory constraints is something that is rarely looked at here in Silicon Valley. I'm struck when I go back to Boston or another parts of the country, we do see more startups and more entrepreneurial ventures where people are looking for discontinuities within the regulatory structure or thinking about taking that on. And maybe talk about that and how you learn from E-LOAN but then you took on a very significant task in terms of having to go state by state on and on and may be take us through how you got comfortable with that and what that is meant from a company point of view? Yeah. I guess a couple of things, one, I think we took a lesson out of the PayPal sort of experience and PayPal I think was famously aggressive in the regulatory strategy, I mean on purpose. And they definitely that's why they won against the city corp.

and some of the other in the eBay kind of version of that. So we're very deliberate about that. We thought, look you know if you get some really good attorneys, we brought on a general counsel right away that was as important as the CTO in our case. So actually brought my general counsel from E-LOAN just a black belt in the area non-better. And he was a real creative legal guy. So regulators won't tell you what you can do and then you can go to the SCC and say "What do you think about this?" Rarely you're going to get a no-action letter especially in these new categories. But what you can hope for is they're not going to shut you down right away. And in many cases, that's good enough. So get some good attorneys, you can get their opinions, arm yourself. You need that to then take to the first question Jim's going to ask "Can you do this?" And again, that's why we have to have that legal regulatory thing fixed first.

I think Jim knows, everybody knows the, yeah, you guys are going to try figure out the technology, right? But can you do the regulatory? That had to come first and I think that was the key lever in getting a good valuation, getting it off the ground as concept, attracting a team. And then I think with somebody who have experience at E-LOAN we had worked a lot with

consumer advocates. The consumer advocates have a big influence on the regulators. At the end of the day, if you're doing something that's good for consumers, regulators will give you a lot more leeway definitely than if you're trying to really push things, screw people especially in financial services where most of the new innovative startups are run by crooks, I mean, these are really, really bad people doing bad things. So if you can introduce something like a PayPal or something that's very positive, that's going to go a long way and you can use that to good benefit.