

URL: <https://ecorner.stanford.edu/in-brief/vc-case-study-negotiating-with-first-time-founders/>

How should a VC negotiate with an inexperienced or even somewhat naive first-time founder? Should they take advantage of the knowledge asymmetry, or should they educate the founder to make sure the founder knows what to push for? Stanford professor of the practice Tina Seelig and Redpoint Ventures managing director Annie Kadavy explore those questions in this brief case study.



Transcript

- I'm really excited that we're gonna try our first little mini case here.. So let me just tee it up.. So we have a lot of people who are listening who are first time founders or are hoping to be first time founders.. And one of the issues is there is, there is a real difference between the amount of experience you have as an investor and them, when they come in they're naive in a lot of different ways.. So when you are negotiating with a first time founder, a, do you, and we're gonna put up a poll in a second.. Do a, connect them with someone who can help them advocate for themselves and get the best terms? Do you help educate them yourself about the process even if it means that you don't get the best deal? I mean, you might put them in a position where they're gonna ask for more than they could have or would have known to ask.. Or three, do you do everything you can to get the best deal for your firm? So let's put up the first poll and see what our audience thinks.. We're gonna give you 10, 15 seconds to look at this, to see if you connect them with someone, do you educate them or you do everything you can to get the best deal for your firm.. What do you think Annie is going to say? What would you do if you were venture capitalists? Give you just a couple more seconds.. All right, let's see what people say..

Let's look at the results.. Let's see how they gonna show up.. Is it tallying? I don't know.. Well, while we're waiting for the results to show up, let's find out from Annie what she would do.. - I'm like on pins and needles over here, like what will people say? - Pins and needles, like what's gonna happen? Let's see if anybody answered the poll.. The results are sharing, I'm being told that the results are sharing maybe we just can't see them.. - Oh, you and I just can't see them.. - Okay, maybe they'll send me - That's even more exciting.. - a clue in the chat.. So what would you do, Annie? - Okay, I'll go answer first here..

So the answer I give is number two, and the reason for that is that this first negotiation, which is your true first negotiation with the founder and it's your first probably true "hard conversation," it's an important learning experience and a trust building opportunity between the two of you.. And so every negotiation is different.. I have walked away from deals because, for example, a founder is demanding a higher price than I'm comfortable with.. I have negotiated for over the course of one day, over the course of multiple days.. Most other terms in term sheets these days are actually pretty easy to navigate.. We're in a time in history where term sheets tend to be very founder friendly and very consistent across firms and across deals.. And so while I do believe it's my responsibility to help.... Oh, here we go, we can see the results.. - Yeah, yeah.. - All right, an interesting mix that feels like, for me, that feels like success that we framed it up in a way that you-- - Yeah, yeah, exactly..

- Okay, great.. Anyway, coming back to why I say two, I think one, it's the most important conversation you are gonna have to date with this person and so you wanna be able to build trust and I want a founder to be able to ask me a question of, well, why are you motivated to put that into the term sheet? Or why is this the price that you came up with? And vice versa, I wanna be able to ask them, why do you care that this is the board structure that we have as opposed to this or that or the other.. So going to number one, certainly they, any founder can and should, I would recommend, reach out to other founders or even to the law firm that they're working with often becomes a valuable resource to give them some other perspective based on other things they've seen.. And on the flip side, number three, yes, it's my duty, it's my responsibility to get what I would consider a "fair deal." But usually if it's plus or minus, one or \$2 million pre or post here or there, there's going to be some wiggle room that I want to be able to have that conversation in a productive way.. - Yeah, so I'm gonna share the results for those people who are listening to the podcast.. Turns out a very interesting 41% of people said we should definitely try to connect them with someone else who's gonna help them.. 38% so pretty close said you should educate them about what the

terms are and help them kind of get up to speed and 22% said you should do everything to get the best deal.. So it's interesting, my guess is if you went to different VCs you probably would get also different responses to this.. So one of the things that's interesting is when you choose a venture capitals to go to, you might wanna think about how they would answer those questions.. - Yeah, and I also think that how they would answer this question is going to be indicative of how they answer future questions that you work on together about your company..

Then in some sense, none of these are wrong answers but they do represent the person that you're working with...