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## Helping VCs help themselves

by Olaf de Senerpont Domis [Posted 09:58 EST, 12, Apr 2006](#)

Seasoned venture capitalists know how critical a young startup's management team is to the ultimate success of their investments. Increasingly, VCs are also beginning to recognize their own shortcomings at building cohesive C suites.

How to cope? "We're putting a bunch of guys together in a high-pressure situation and expect them to be a high-performance team," says **Mayfield Fund** managing director David Ladd. "We do use organizational development firms to help develop that."

Indeed, employing management consulting firms is becoming a more common practice in Silicon Valley these days, especially as part of the due diligence process or shortly after venture capitalists have invested. Bill Morin, CEO of New York consultancy **WJM Associates Inc.**, explains why: "Investors might check every nuance and subtlety from a financial point of view but ignore what's really going on with a company's management."

Early-stage companies often have an incomplete cast of managers, notes Ladd. A venture capitalist needs to decide how much work there is to be done to build a team and whether he or she is willing or able to do that, he explains.

"You have to decide whether the people at the top of a startup can handle stress," adds Morin. "Now they'll have investors breathing down their necks, and they'll have to handle the exit strategy kind of management."

The work done by these consultancies, which include WJM, Los Gatos, Calif.-based **Strayer Consulting Group Inc.** and **HRMG Inc.** of Burlingame, Calif., among others, tends to be some variation of a common theme. They step in to help an entrepreneur CEO without a lot of management background who needs a primer about leadership, managing a team and communication.

Often, consultants like Linda Tirado, a co-founder of Strayer Consulting, find that startup CEOs get caught up with pitching the company while seeking funding. Alas, they let that attitude interfere with their communications with investors and the board.

"The startup CEO often is used to sell the company externally, but VCs don't want spin," Tirado says. "VCs want an honest dialogue and transparency and an idea of any problem that might lie ahead. That can become a stumbling block."

Tirado recounts when her services were requested recently by a venture capitalist who, shortly after closing an investment with a young software company, recognized a problem with the CEO (Tirado declined to identify the startup). The company's product did not work as predicted and was "clearly not ready for prime time," as she puts it.

Board members were caught off guard by this, largely because the CEO, who had a strong background in sales and marketing — but not in technology or management — failed to signal any potential problems. "They didn't know how to read the CEO because he had such a happy story for the board despite these problems," Tirado says. "The board was quite disgruntled and ready to eject the CEO."

The chief executive, it turns out, also did not communicate well with the engineering team, which was led by the company's co-founder. A few months of work with Tirado, along with the appointment of a new vice president of engineering, brought the CEO a greater ability to communicate meaningfully with investors and got the startup through what she describes as "a very frightening time."

Management issues, of course, aren't the only challenges a technology startup faces on its growth trajectory. Chief financial officers at two former startups, **Netflix Inc.** and **Salesforce.com Inc.** — both of which

apparently made the right choices with their management teams — recently recounted the challenges they faced getting through their initial public offerings.

Leading online DVD rental service provider Netflix, which debuted in a very challenging public market in 2002, faced looming competition from **Blockbuster Inc.** "We were trying to shoot a window," explained Netflix CFO Barry McCarthy at a recent Silicon Valley gathering.

"If we missed it, we could have gone bankrupt," he said. To please investors, Netflix needed quickly to attain positive cash flow. "We lopped off one-third of our engineers," he said. "Sometimes you need to go [public] as early as possible."

McCarthy added that when a startup mulls going public, it should be careful where it turns for advice. "You can't rely on your board or VCs to answer that question," he said. "They just don't know the capital markets." Even technology boutique banks weren't the place for Netflix to seek advice, McCarthy said, as they lacked power and influence in 2002.

So Netflix turned to **Merrill Lynch & Co.** as its lead underwriter (alongside **Thomas Weisel Partners LLC**, which co-managed the deal). The reason: Merrill's experience with media deals.

Customer relationship management software vendor Salesforce.com's struggle was more about credibility, recalls the company's CFO, Steve Cakebread. The company had done "fairly well" as a private company catering to companies with 50 or fewer employees, but as it tried to expand its customer base to bigger international companies, the dot-com part of the company's name caused some headaches.

"I spent one-third of my time answering calls asking if we'd be in business next week," quips Cakebread. Obviously, he was persuasive, even though he insists his reply to customers and investors was: "We're a dot-com in San Francisco — not to worry."

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