

# How does an inventor find an investor or partner? Raising funds to start a company



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TRUE MEDICAL INNOVATIONS are developed usually from addressing the classic “unmet clinical need”; yet, several billion-dollar, blockbuster technologies have been commercialized that simply optimize outcomes, improve procedural profits, and/or decrease risks to the patient. While investing in your own technology certainly shows commitment and encourages others to accept your personal belief, validation from financially sophisticated, third-party investors, together with their deep pockets, often moves the process along more efficiently. Yet, once inventors have that “aha” moment of discovery, it becomes essential for them to quickly assess a few key elements before draining their savings account to support the initial prototype build:

1. Is the discovery simply a product or procedural enhancement, or is it truly worthy of building a company around it?

2. What would it require to generate “proof of concept” and then “clinical validation”—that valuable “first-in-man” assessment?
3. What is the long-term objective of the inventor(s)—licensing income, building equity value, and/or playing a role in the development and commercialization of the technology?

These key questions require answers prior to determining the next steps. In the event that the discovery warrants formation of a company and, therefore, a substantially larger financing requirement, it is then imperative to address the two next big questions: (1) What is the intellectual property (patent) landscape? (2) What is the global market opportunity? A detailed patent search (by a qualified and experienced patent attorney) is designed to inform the inventor whether someone has already filed the elements of their invention and/or if it warrants filing for protection with a new set of marketing claims.

Understanding how a new innovation may affect the global market is critical in not only determining the value of the technology but also in attracting legitimate and sophisticated investors. Market intelligence includes an understanding of potential revenues, requirements for regulatory approval, and the processes of reimbursement/

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payment for each major country. This knowledge also drives critical assumptions in the operating plan and overall budget.

Now that the strategies toward the technology, markets, and intellectual property are well mapped, it is essential to assemble a management team that has the experience and proven track record of moving the business forward from concept to commercialization.

### **IDENTIFYING THE RIGHT INVESTOR**

For the sake of this article, funding from grant sources (ie, National Institutes of Health, Small Business Innovation Research, Defense Advanced Research Projects Agency, etc) will not be considered as “investments,” because such financings do not provide for a liquidated return. In addition, it is very rare to identify and secure an investment commitment that guarantees full funding through commercial success, often defined as achieving positive cash flow (profitability). Conventional financing often includes a sequence of separate classes of funding, each having their own distinct set of terms, conditions, and parameters of valuation. Investors may be segregated into the following groups: (1) family and friends, (2) institutional/venture capital, (3) private equity funds, and (4) strategic/corporate investors. There are exceptions, but each of these groups has certain criteria for their investment—for example, markets, stage of development, investment terms, and timing of possible exit. Nearly all investors, however, will focus on the essentials of markets, intellectual property, and the ability of management to execute on a defined plan.

**Family and friends.** All investors will want to see that the inventor has some “skin in the game” and is willing to invest personal funds in the enterprise. This recognition goes beyond the contribution of intellectual property or intellectual capital. One’s own stake does not need to be the major funding source but should be enough to show commitment before seeking capital from others. Such an investment includes capital contributions from family members and friends, primarily because this is viewed as a personal, gut-wrenching commitment from individuals from whom the inventor cannot hide, and this initial capital is at the greatest risk. There is very little evidence regarding if and when the invention will ever materialize, and there is no guarantee that additional follow-on financing support will be provided.

**Venture capital.** The venture capital industry has evolved greatly over the past decade, with many of

the classic, early stage venture investors either altering their investment strategy to growth-stage funding or departing from the venture business altogether. Those still in the game maintain high expectations of lofty returns while looking to minimize as much risk as possible before committing to what now has often become a staged or “tranche” investment based on the achievement of specific objectives. Venture capital investors will require the inventor/founder to check all the boxes mentioned above (ie, market assessment; patent protection and/or formal assessment of noninfringement; identification of qualified, experienced management; and presentation of a proper operating plan with key milestones and use of proceeds).

**Private equity funds.** Before the downturn of early stage venture funds, private equity funding was considered usually only for market expansion, to provide additional capital for mergers and acquisitions or even a bridge to becoming a public company. Today, several private equity funds are pursuing development-stage investments for the purpose of considering a longer-term “roll-up strategy” (to combine  $\geq 2$  businesses) or to eventually “bolt on” a missing element to advance the market share of an existing portfolio company. Terms and conditions of their investments can be equally as demanding as those of the venture capital investor, but they are often positioned as longer-term investors who will align themselves as partners with the inventor.

**Strategic/corporate investors.** As exciting as it may seem to have an industry giant interested in one’s invention, this is the most challenging investor to consider at this stage of development. Unlike the venture capital investor, whose motives, process, and outcomes are very clear and understandable, the interest from a corporate investor may not be truly aligned with those of the inventor. Endless stories are told about corporate investors who finance, license, or acquire new innovation from inventors or universities only to shelf the technology or shut it down. This possibility may be due to pure economics and strategic issues in the marketplace and often times is not based on the actual merit of advancements in medicine (ie, the good of society). This source of financing should be the inventor’s last resort.

### **PREPARING FOR INVESTMENT**

Once an inventor makes the commitment to advance to the next level of financing, it is imperative that time is spent preparing an

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