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Family Venture Capital

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During Some families have thought about providing venture capital, or "seed" money, to family members who are in business for themselves or who are contemplating taking part in the American dream of entrepreneurship. Families that have considered offering such capital are generally pleased with the message it conveys to the family in terms of opportunity and in continuing what, for many, has been a successful venture into the free enterprise system for generations past and present.

Like many good intentions, the challenge is usually in the details. When the family, or family office, begins to develop a plan for providing venture capital, several challenging questions must be answered. Perhaps first and foremost is the question of how to establish a policy that will be consistent and can provide equal opportunity within the family's means.

Other questions that will need to be addressed include the following:

- What are the criteria for approval or rejection of a venture request
- How should expectations be set for the investments? What are realistic expectations?
- What about non-profit ventures? How should expectations differ for profit and for community-based non-profit ventures?
- What about accountability? What happens if the expectations are not met?
- How should the investment be administered within the family or family office? Or should the function be managed outside the family with family guidance at the governance level?
- What role will the family investment vehicle play in the governance and/or management of the venture being financed?
- In the event of a failed investment, what can be done to make sure the unsuccessful entrepreneur remains a welcome contributor to the family?

Many families will attempt to establish policies that mirror those of traditional venture capital firms. Among the conditions for consideration might be the submission of an acceptable business plan, accompanied by realistic financial projections, including cash-flow "burn rate" and break-even to profitability projections. Normally, these would be on a worse-case, best-case, and most-probable-case basis. The plan should also address the repayment of venture financing and expected return on investment to the venture capital provider. Another consideration for approval might include the extent to which the prospective entrepreneur would be wiling to support his/her own venture from both a financial and time-commitment perspective.

The review and approval process is paramount in maintaining fairness in a venture capital environment. Some families have considered engaging outside advisors, such as investment or banking sources, to assist in establishing approval criteria. For these functions, it is best to avoid using advisors who are currently active in managing family assets or providing services to the family. An outside venture capital board might provide a welcome resource for policy development, as well as for the process of managing the family venture investments.

A well-managed venture capital fund within the family can be a most rewarding addition to an already rich legacy in entrepreneurship and participation in the free enterprise system. It can also be a major contributor to the family's efforts in active philanthropy that may offer numerous family members a path to realize their dreams of active involvement in making a difference in their communities.

The Family Business Advisor