Management 425 Course Pack
Brad Leve

Chapter 4
Defining Venture Capital

I was born in 1966, the year Digital Equipment went public. Digital Equipment was one of the first venture-backed initial public offerings (IPOs). Digital Equipment helped propel the venture capital market. Many of the most successful companies in the world were started with venture capital. Before Starbucks went public, it raised $30 million in 1990 through a private placement. Starbucks now has revenue in excess of $17 billion. Private placements (equity or debt) grew in popularity. According to Allen, Brealey, and Myers, "In 1980 private placements accounted for about one-fifth of all new corporate debt issues, but by 1989 this proportion had expanded to almost one-half."[1] Alex. Brown helped many emerging growth companies raise money with venture capital. Investors would line up for Alex. Brown IPOs like small children on the beach in Avalon, New Jersey, on a hot summer day waiting for ice cream. The allure of venture capital for investors is simply high returns:

> Part of the attraction of venture capital investing lies in the optionlike character of individual investments. Downside losses cannot exceed the amount invested. Upside gains can multiply the original stake manifold. The combination of limited downside and substantial upside produces an investor-friendly, positively skewed distribution of outcomes.[2]

Alex. Brown Private Equity Group, for example, from June 30, 1991, to June 30, 1997, had an average internal rate of return of +33.31% versus DJIA +21.3%, venture capital funds +21.0%, S&P 500 +9.8%, Russell 2000 +17.7%, and T-Bills +4.6%.[3]

At the time, I introduced many of the most successful private placements to Alex. Brown. For example, I brought in a company called CDNow (arguably the first business-to-consumer company) as well as placed tens of millions in deals with high-net-worth clients looking to diversify. CDNow raised $10 million in August 1997. Private placements are simply a private round of financing for a company led by an investment firm or bank. Private placements are generally purchased by institutions such as venture firms and high-net-worth individuals. The investments are a minimum of $100,000 to $500,000 and illiquid. Private equity — unlike the other alternatives — where an investor can become liquid in a reasonably short period if not immediately—are illiquid for a long time.

In the 1990s the only thing better than a hot IPO was receiving shares before the company went public: pre-IPO shares. Private placements were the hot ticket of the alternatives world. They were the vehicle that allowed access to pre-IPO shares. Wealthy clients could not get enough. I remember advising one client in particular to invest in one of the best private placements ever. In February 1999, I recommended Cobalt Networks, which was priced at $3.70 per share with a minimum of $3 million to invest. Cobalt went public in November 1999 at a price of $22. The stock reached a high of $158. The Dow Jones News Wire reported this IPO to be the third-best IPO ever. Putting aside any kind of lockup, this investment hypothetically would have been worth $117,567,567.51. Cobalt Networks was a high-risk, high-return investment. Even the name of the company was alluring. Surfers have a term that can be used to describe such a lucrative investment: *amped.* Amped means getting excited while surfing or really looking forward to surf.

There are few things in life as exhilarating as watching an investment you made go public be such a screaming success. Right before a company goes public, the underwriters have a clear idea of how "hot" the IPO is or if it will be mediocre. A lackluster IPO is frequently referred to as a dog. A hot IPO, on the other hand, will be oversubscribed, such as the Boston Beer Company, another hot IPO I introduced to Alex. Brown. Even if you hated the taste of beer or Samuel Adams, one appreciated the buildup before the IPO as more and more investors wanted a finite amount of shares. The venture capitalists that funded the company did quite well. The Boston Beer Company was the lead microbrewery to go public in September 1995, and no other microbrewers were public at the time. A hot IPO like the Boston Beer Company will typically open "up" and keep on going. Because of its success, other microbreweries went public, such as Pete's Brewery Co., maker of Pete's Wicked Ale. Watching a company go public is exciting. The rush is tantamount to driving 150 miles per hour in a Porsche or winning the lottery. Adrenaline courses through your veins. Your heart races. Your palms sweat. You can even feel faint not knowing where the stock will close the first day.

Because Alex. Brown was ranked the number-one firm for taking venture-backed IPOs public, I had exposure to a lot of venture capital funds. There are certain venture funds an investor would want to avoid like the plague, whereas others are like running into Taylor Swift in an airport (assuming you like country music). I helped run a small $30 million venture fund for partners of Alex. Brown called Momentum. The fund had many success stories derived from investments in fast-growing health-care and technology companies. For example, we invested in the first Linux company called Andover.net, which ultimately became part of VA Linux. We contributed to a private round of funding (totaling $7 million) on November 1, 1998, for Andover.net, which eventually led to an IPO on December 8, 1999, and was worth $82,800,000. The first-day return on Andover.net when it went public was + 252.08%. Andover.net was then acquired by VA Linux Systems on February 3, 2000, for a total of $950,000,000.

Personally, I have invested in many fast-growing companies. A good money manager will taste his own cooking. I have never recommended a security or company that I would not purchase myself. The best money managers are invested in their own funds. Advisers and managers that do not put their own money where they invest others' money typically do not have as good performance. While I experienced many success stories, I also invested in a few companies that made going camping with Freddy Krueger or Jason Voorhees look like a good time; I have invested in both good and bad companies. Anyone investing in venture capital should study the waves and examine whether they are entering or leaving at a good time. Often the worst of times presents the best of times to invest in venture capital. Venture capital is high risk, high reward, and should be carefully studied. Investing blindly in venture capital is ill-advised. An investor should not be in the dark. As James Joyce said in *A Portrait of the Artist as a Young Man,* "He saw the sea of waves, long dark waves rising and falling, dark under the moonless night."[4] Do not surf in the dark.

While venture investing is not for the faint of heart and many things can go askew, the rewards are quite compelling. Benchmark Capital's $6.7 million investment in eBay mushroomed into $6.7 billion or a 1,000-times return, qualifying it as "the valley's best-performing venture investment ever."[5] Then came Google. Andy Bechtolsheim, a founder of Sun Microsystems who invested in early-stage companies, helped start Google with $100,000.[6] On September 7, 1998, Google Inc. was finally incorporated. Sequoia Capital and Kleiner Perkins Caulfield and Byers funded a $25 million round at a valuation of $100 million in June 1999.[7] On April 29, 2004, Google filed an S—1, the formal public offering document for an IPO, and stated that they would sell $2,718,281,828 worth of shares. On December 10, 2007, Google's market capitalization was $173.6 billion.

Venture capital can go one of two ways: up or down. One either makes a lot of money or loses it. Over time, returns of venture capital are quite compelling. If one chooses to add venture capital to a portfolio, it is prudent to really do your homework. Google was not the first search engine. There were many search engines at the time, such as Lycos, Infoseek, and AltaVista. However, not all search engines use the same algorithm, and none were as successful as Google. Venture capital investors need to be careful as to the sector they choose but also selective among the companies in that particular area. The industries in which venture capital is invested covers primarily technology, consumer, media, health care, environmental, and transportation. A me-too or copycat company is not the same as the original or leader of the pack. Venture capital is one of the most challenging of all the alternative investments but is by far the most lucrative.

Defining Venture Capital

According to Wright and Robbie, "Venture capital is typically defined as the investment by professional investors of long-term, unquoted, risk equity finance in new firms where the primary reward is in an eventual capital gain, supplemented by dividend yield."[8] Generally, there are two groups involved with venture capital: general partners and limited partners. The general partner manages the fund, and the limited partners are the investors. Venture capital involves early-stage investing in the equity of privately owned companies with the potential for rapid growth. Venture funds require accredited investors. Federal securities laws define the term *accredited investor* in Rule 501 of Regulation D as follows:

1. a bank, insurance company, registered investment company, business development company, or small business investment company;

2. an employee benefit plan, within the meaning of the Employee Retirement Income Security Act, if a bank, insurance company, or registered investment adviser makes the investment decisions, or if the

plan has total assets in excess of $5 million;

3. a charitable organization, corporation, or partnership with assets exceeding $5 million;
4. a director, executive officer, or general partner of the company selling the securities;
5. a business in which all the equity owners are accredited investors;
6. a natural person who has individual net worth, or joint net worth with the person's spouse, that exceeds $1 million at the time of the purchase;
7. a natural person with income exceeding $200,000 in each of the two most recent years or joint income with a spouse exceeding $300,000 for those years and a reasonable expectation of the same income level in the current year; or
8. a trust with assets in excess of $5 million, not formed to acquire the securities offered, whose purchases a sophisticated person makes.[9]

Venture capital is one of a number of investment strategies under the private equity umbrella. Within the venture capital space, investors can encounter companies that are just beginning and require seed capital. Venture capital entails investing mainly in early (but can also involve later-stage) growth companies that are private.

Parents, friends, college roommates, or neighbors might initially "seed" a company or help form it. They are also commonly referred to as "angel" investors. Angel investors typically provide seed capital to get the ball rolling or put money into start-ups with the hope of the investment turning into a fast-growing, profitable company down the road. Investors who prefer early-stage investing are most commonly known as angel investors. *Early Stage VC* or *start-up* refers to a company that is newly formed, analogous to a builder framing a house, whereas seed investing might be compared with the cement or foundation being poured. Venture financing in start-ups typically is devoted to a product or for designing a prototype. As a company grows, it requires additional funds.

Growing companies can consume tremendous amounts of capital. Venture capital firms will most likely then enter the picture to invest in mezzanine or expansion rounds. In some cases the investment takes the form of a loan or might even include an “equity kicker” or some other component in order to entice an investor. As the company continues to grow and nears an IPO, it will often require more capital. Late-stage investing, as this is known, is popular among investors because much of the risk is diminished. There are also opportunities between venture rounds called bridge rounds, in which an investor puts money in to help ensure that the company has enough capital to get to the next round. Private equity is a

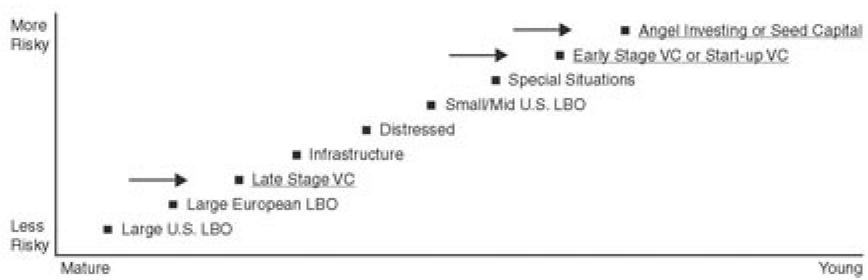

Figure 4.1 Private Equity Spectrum (Venture Capital)

Source: Author.

broad-based alternative asset class comprising a number of different areas, as seen in Figure 4.1.

Venture capital is illiquid and involves equity in private companies or ones not publicly traded on an exchange. Private equity strategies might include leveraged buyout, distressed investments, mezzanine capital, and growth capital. Venture capital can be viewed as a component of private equity. A general partner runs the venture fund, and limited partners invest in the fund. Venture capital is invested in limited partnerships that are usually 10 years in duration. The companies are neither mature nor traded on any stock exchange. Venture capital seeks companies that show promising new technologies or concepts that are not necessarily proven. Funds are raised either using bonds or equity. Private placements are “the direct sale of bonds to lenders by the debtor company, bypassing an underwriter for the offering.”[10] Private placements can also involve equity that is sold to high-net-worth investors, companies, or institutions, such as venture capital firms. Venture capital firms take a stake in these companies by purchasing equity in the company. Normally, there is a lead investor who contributes the most money but also helps dictate the terms. Companies typically raise between $10 million to $80 million and use the money for expansion, development, or going public.

One fallacy about investing in venture capital is that an investor cannot buy into great companies in bad markets. When the going gets tough, Americans get innovative. “Americans are adept at finding opportunity in adversity.”[11] Some of the best companies in America were started in the worst of economic times:

> History shows that great companies are often built during bad times. In 1939, at the tail end of the Great Depression, two engineers started Hewlett-Packard in a garage in Northern California. Silicon Valley itself was largely created during the nasty recession of the mid-1970s. During that decade, entrepreneurs laid the groundwork for the boom of the 1980s, building companies that pioneered three new industries: Atari in the video game business, Apple in personal computers, and Genentech biotechnology.[12]

Many great companies were built using venture capital. Venture capital plays a vital role in the U.S. economy, funding the launch and success of a variety of industries inspired by innovations in technology, transportation, and pharmaceuticals, among others. The direct role of venture capital investment has gone to research and development expenses, and, more important, to hiring hundreds of thousands of new personnel to oversee those roles. That is, venture capital creates jobs. Jobs get eliminated in both good times and, especially, bad times. However, venture capital helps fill the void. According to the *Economist,*“Even in boom times, 15% of American jobs disappear each year. Their places are taken by new ones created by start-ups and expansions. This dynamism remains evident [in a post-recession world]—the most crushing economic conditions most businesses have encountered.”[13] In the first decade of the twenty-first century, tens of millions of Americans were either starting or running small businesses:

> The annual study by Babson College and London Business School, released Thursday, covers 34 countries with a combined labor force of 566 million. It is the largest annual measure of entrepreneurial activity worldwide. Babson, based in Wellesley, Mass., is seen as a leader in the study of small businesses. The study estimates that 73 million adults are

either starting a new business now or managing a young business they own.[14]

Many of these businesses require some form of outside funding, and contrary to what one would think, the overwhelming amount of funds for venture capital comes from individuals, not venture firms. according to *Investor's Business Daily's* study of the Babson report, "Fewer than one in 10,000 new startups get their initial funding from venture capitalists."[15] Friends, neighbors, family, colleagues, relatives, and former classmates are typical investors in venture capital. In fact, according to *the same* report, 99.9% of start-ups rely on funding from everyday investors, who have collectively contributed about $105 billion (versus $20.4 billion from venture capital firms) to help get new businesses of the ground.[16] The bulk of financing (on average about $50,000 to start a business) is from entrepreneurs themselves.

Venture Capital and Entrepreneurs

Venture capital is based on investing in fast-growing companies run by entrepreneurs. Robert E. Wright notes, "At its most basic level, financial history is the story of the competition between different means of linking the savings of investors to the spending of entrepreneurs."[17] If you have a great concept, you will need someone competent and driven to build on that idea and turn it into a company. Companies that are immensely successful were built by entrepreneurs. McDonald's was built by Ray Kroc. "Under his leadership, the company exploded from one store in the mid-1950s to more than 8,300 locations at the time of his death in January 1984.... From its IPO in April 1965 to when Kroc died, shares surged 1,014%."[18]

According to the Edward Williams and Albert Wapier in *Essentials of Entrepreneurship,*"All [entrepreneurs] have common roots in economics, economic/growth, and the creation of wealth.... The origin English word *entrepreneur* comes from the French word *entreprendre,* which can be translated to mean 'to do something' or 'to undertake'."[19] An entrepreneur is a creative, hard-working, charitable, motivated individual with an idea for a unique product or service that he or she turns into a viable growth company that will improve the lives of others and add to society. The definition of an entrepreneur varies widely:

> To an economist, an entrepreneur is one who brings resources, labor, materials, and other assets into combinations that make their value greater than before, and also one who introduces changes, innovations, and new order. To a psychologist, such a person is typically one driven by certain forces—needs to obtain or attain something, to experiment, to accomplish, or perhaps to escape authority of others… To a Communist philosopher, the entrepreneur may be a predator, one who usurps resources and exploits the labor of others. The same person is seen by a capitalist philosopher as one who creates wealth for others as well, who finds better ways to utilize resources and reduce waste, and who produces jobs others are glad to get.[20]

Many successful entrepreneurs give back to society either with foundations or other philanthropic giving. Table 4.1 provides a chart of philanthropic entrepreneurs.

Table 4.1 Philanthropic Entrepreneurs

Name	Background	Causes	Estimated Lifetime Giving (millions)	Net Worth (millions)	Giving as a % of Net Worth
Bill and Melinda Gates	Microsoft cofounder	Global health and development, education	$40,780	$59,000	48%
Gordon and Betty Moore	Intel cofounder	Environment, science San Francisco Bay area	7,404	4,500	165
Alfred Mann	Medica devices	Biomedical education and research	1,735	2,200	79
Ted Turner	CNN founder	Environment	1,500	2,300	65
Larry Ellison	Oracle CEO	Research on aging and diseases	808	26,000	3
Jeff Skoll	Founding president of eBay	Social entrepreneurs	744	3,500	21
Bernard Marcus	Home Depot cofounder	Jewish causes, health, free enterprise, children	700	2,000	35
Pierre Omidyar	eBay chairman and founder	Unleashing human potential	657	8,900	7
Irwin Jacobs	Qualcomm cofounder	Education, arts	627	1,600	39
Thomas Siebel	Siebel Systems founder	Education, meth prevention Meth Project, community	386	1,900	20

Source: "The 50 Top American Philanthropists," *BusinessWeek*, 2008; "The 50 Top American Philanthropists," *BusinessWeek*, 2009. Used with permission.

True entrepreneurs are heroes. Many have made huge sacrifices (financial, personal, emotional, and familial) to build their dreams. The reward for an entrepreneur should be great because it is no easy feat:

> In sharp contrast, an IPO is the pinnacle of a long chain of new money invested in a highly risky venture. It typically begins with an entrepreneur tapping into personal savings to develop an idea. Later, the entrepreneur persuades wealthy private investors or even a venture capitalist that the business has intriguing growth prospects, and they seed the startup with somewhere between $100,000 and $1 million. The money can come from

> the traditional venture-capital industry, which is made up of more than 500 venture-capital funds that invest between $3 billion and $4 billion a year in some 3,000 companies or the invisible venture-capital industry, drawn from some 2 million self-made high-net-worth individuals who conservatively invest between $10 billion and $20 billion a year in more than 30,000 ventures.[21]

The companies that entrepreneurs build create jobs. A total of 243,421 employees from Apple, Microsoft, Yahoo, Oracle, and Google alone would be unemployed in 2009 if the entrepreneurs behind them could not have raised capital when they were in their infancy:

> Over the past 60 years the money and the expertise provided by venture firms has led to the creation of thousands of companies, including Intel, Genentech, FedEx, and Google. A study by the National Venture Capital Assn. found that US venture-backed companies generated 10 million jobs and 18% of the nation's gross domestic product from 1970 to 2005.[22]

Venture capital helps companies grow into large-cap companies, which employ millions of people in a variety of industries. Joseph Schumpeter viewed entrepreneurs as agents of historical change. Venture capital gets deployed into a number of industries. However, technology is one of the biggest, and, not surprisingly, a huge source of jobs in the United States. Figure 4.2 is a chart of the number of employees at various technology companies.

When one includes other sectors in addition to technology, such as health care, venture capital creates a massive number of jobs. Guy Fraser-Sampson reports: "Research suggests that even by the end of 2000,

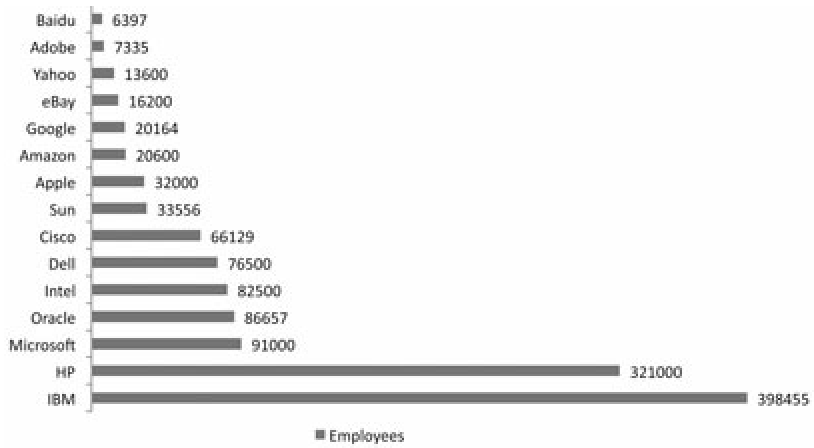

Figure 4.2 Number of Employees at Major Technology Companies

Source: Royal Pingdom, "The Size of IBM Makes Microsoft and Google Look Like Tiny Startups," http://royal.pingdom.com/2009/05/04/ibms-size-makes-microsoft-and-google-look-like-tiny-startups/, accessed May 4, 2009. Used with permission.

venture capital had directly created about 8 million new jobs in the USA (roughly equivalent to one job for every $36,000 of investment), and that if one added into the mix the jobs created indirectly in supporting and related businesses then the total rose to a staggering 27 million."[23] Whether the economy is good or bad, entrepreneurs are building companies and, in turn, hiring. Many talented and terrific employees lost jobs in a variety of industries when the market crashed. Recessions lay off workers, who then become marketable and sought after by entrepreneurs. Recruiting talented employees becomes easy, as well as obtaining office space. Americans, for the most part, are hard working and industrious:

> Such is the nature of human beings to strive to get more output from a given amount of input. All people want to be productive so that they can enjoy more wealth and more leisure. Not all people, however, have access to institutions that make increased levels of productivity possible. The mere desire to be more efficient is insufficient to drive productivity to higher levels because efficiency comes with start-up costs. Those costs will eventually be repaid many times over, but the initial cost of

> increased productivity is often a barrier that thwarts the introduction of innovations or reforms.[24]

The American culture admires those who work hard and are successful with their endeavors as opposed to those who are idle and complacent. The *Economist* reports: "A Pew poll released on May 21st found that 76% of Americans agree that the country's strength is 'mostly based on the success of American business' and 90% admire people who get rich by working hard."[25] Many successful companies were created during challenging times in the United States:

> Since its inception after World War II, venture capital has had a little-known but profound impact on the U.S. and world economy. It has played a catalytic role in the entrepreneurial process: fundamental value creation that triggers and sustains economic growth and renewal. In terms of job creation, innovative products and services, competitive vibrancy, and the dissemination of the entrepreneurial spirit, its contributions have been staggering.[26]

Five of America's Top Entrepreneurial Companies

1. **Zippo Manufacturing Co.** Zippo Manufacturing Company was founded in 1932 by George G. Blaisdell. Zippo has flourished from a $10-a-month room over a garage with two employees in the early twentieth century to a multimillion dollar business that employs 570 people based in Bradford, Pennsylvania, along with an office in London and a joint venture company in Paris that generates revenues upward of $155 million.[27] Zippo lighters are sold in more than 120 countries and have become a household name. The firm expects to sell its 500 millionth Zippo in 2010.

2. **Kraft Cheese.** Kraft Foods, Inc. was founded in Chicago in 1903 by James Lewis Kraft. "With just $65 in capital, a rented wagon pulled by a horse named Paddy and a never-say-die attitude, Kraft, 29, started a business peddling unpackaged cheese wholesale to local merchants."[28]

Kraft's first year was a nightmare, and he went $3,000 into debt. Now the Kraft brand is the largest food and beverage company in the United States and the second largest in the world, after Nestlé. Kraft's 2008 revenues were $42.201 billion and net income was $2.901 billion for 2008.

3. **Goodyear.** Goodyear would not be possible without Charles Goodyear's vulcanization process, which was developed in 1839. Before vulcanization, rubber products could not withstand hot and cold weather. Goodyear's process could be one of the most significant developments of the nineteenth century. Charles Goodyear was determined to succeed and even spent time in debtor's prison. His accomplishment paved the way for tires and life rafts as well as a plethora of other products that revolutionized the industry.[29]

4. **Eli Lilly.** Eli Lilly founded Eli Lilly and Company and fought for the north in the American Civil War. Eli's company was founded in 1876 and primarily focused on the manufacturing of drugs. He then marketed them wholesale to different pharmacies across the nation. Two medical advances he pioneered were the creation of gelatin capsules that hold medicine fruit flavoring for liquid medicines. Today, Eli Lilly and Co. is the tenth-largest pharmaceutical company in the world with a market cap of $38.56B.[30]

5. **Smith & Wesson.** Smith & Wesson was founded in 1852 in Norwich, Connecticut, by gunsmiths Horace Smith and Daniel B. Wesson. Their aim was to produce a "lever action repeating pistol that could use a fully self-contained cartridge." After two financial setbacks, one of which forced them to sell their venture to Winchester in 1854, they created "the first successful fully self-contained cartridge revolver available in the world."[31] With their patents, Smith & Wesson grasped market superiority and emerged as the world leader in handgun manufacturing.

There are quite a few examples of entrepreneurial companies in the United States, as discussed in the sidebar below:

Venture Capital and National Security

Venture capital plays a large role in the national security of the United States. The United States was an innocent bystander to the diabolical terrorist event on September 11, 2001, but venture capital has helped prevent further attacks from happening. Besides making the United States the leader worldwide in medical and technology advances, venture capital has also assisted the U.S. government with security. Long before September 11th, the Central Intelligence Agency (CIA) set up its own venture firm known as In-Q-Tel. The fear was that the United States was falling behind with the Internet and national security. "'For many years, our intelligence technical capabilities were the standard of the world,' U.S. Senator Bob Graham (D. Florida), chairman of the Senate Select Committee on Intelligence, told reporters on the day of the attacks. 'We have fallen behind, and we need to close the gap and reassert our leadership.'"[32]

Originally, In-Q-Tel was set up as a nonprofit by the CIA in 1999 with an annual budget of $30 million to improve its Web prowess. The focus of the fund was "Information organization, access management, search, link analysis, Internet privacy, self-protecting data, threat detection, location information."[33] An example of a company that In-Q-Tel invested in was SafeWeb, which allows one to roam the Internet without a trace. Another high-tech company the CIA invested in is called Stratify. "Stratify is among a handful of companies that can find important tidbits of 'unstructured data' — information scattered throughout organizations in word-processing files, e-mails and databases, for example—and put them together in a way that makes sense."[34] In-Q-Tel's investment in Stratify fostered the development of technology that the government felt would directly aid them in the War on Terror.

The former head of Alex. Brown, A. B. "Buzzy" Krongard, was appointed executive director and helped with the CIA's information technology. Table 4.2 provides a list of companies that the In-Q-Tel invested in for the CIA.

Not surprisingly, security investing became even more popular following September 11th for national security as Thompson's Venture Economics showed:

> Indeed, while security accounts for just a slice of overall venture capital, the pace of investing in the sector is up 50% since 1998, Venture Economics data show. Security accounted for about 5%, or $1.2 billion,

of $21.2 billion total venture-capital investing in 2002.[35]

Table 4.2 In-Q-Tel's Investments

Company	Product	$ Amount
SafeWeb	Software that allows users to browse Web sites without being detected	$1.0 million
Intelliseek	Software for searching across multiple, disparate sources and managing search results	$1.4 million
Mohomine	Software for managing unstructured data	<$1.0 million
Graviton	Wireless and sensor technology that monitors and adjusts remote functions	$1.0 million
Open GIS Consortium	Develops standards for presenting geographical information on the Web	$1.1 million
MediaSnap	Security software that controls access to individual documents	$1.3 million
Digital Data Development*	Identifies potentially fraudulent	Undisclosed
SRA International	Advanced search engine that mines data	Undisclosed
Twisted Systems	Software for sharing and archiving information	$350,000
Science Applications International Corporation	Software that repels denial-of-service attacks and shores up security	$3 million
Browse3D	Software for visualizing linked Web pages	Undisclosed
TecSec	Strong encryption software	$55,000
TruSecure	Internet security services	$500,000

*A subsidiary of Systems Research and Development.

Source: Justin Hibbard, "Mission Possible," *Red Herring* (December 10, 2001).

From 1999 until 2007, the CIA venture fund reviewed thousands of business plans and invested hundreds of millions of dollars:

> Since In-Q-Tel was founded in 1999, the firm has reviewed more than 6,300 business plans for everything from identity recognition software to nano-sized electronic circuits. Many proposals come in via its Web site. In-Q-Tel has put about $200 million into more than 100 companies, beating traditional VC investors to technologies such as the mapping software that's become Google Earth.[36]

A critic might fret about taxpayer dollars going toward a government venture fund, but the government has actually had quite a few home runs with its investments (besides keeping the United States in the forefront of

Table 4.3 In-Q-Tel Successes

Company (technology)	Date
@Last Software (3-D modeling)	Jul–04
Decru (data production)	Aug–01
Keyhole (3-D Earth satellite visualization)	Feb–03
Mohomine (text search tool)	Apr–01
Spotfire (information management)	Sep–01
SRD-NORA (data mining)	Jan–01
Visual Sciences (visual data analysis)	Mar–04

Source: Kameiz Foroohar, "Spy Funds," *Bloomberg Markets*, December 2007.

national security). The CIA's foray into venture capital has been profitable, ultimately saved taxpayers money, and protected the United States.

Although the U.S. government has made many terrible investments, the CIA had many companies that filed IPOs or were acquired. Table 4.3 shows a number of In-Q-Tel success stories. Astute venture capital investors would note that 9/11 was going to develop or create a new area of focus for venture capital firms. War usually leads to increased defense spending (public or private companies), and the malicious attack on U.S. soil would most likely result in increased military spending. Hundreds of successful security and defense companies were started. For example, In-Q-Tel partnered with Kleiner Perkins to invest $12.5 million into Arc-Sight, a security management software company. On September 1, 2007, ArcSight, Inc. filed an S—1 to sell shares in a $74 million initial public offering.