

The Art of

the Deal—

How VCs Choose Entrepreneurs

For more than a decade, academic research has postulated the way entrepreneurs and venture capitalists interact. But has financial contracting theory borne any resemblance to what happens in the real world? Using data provided by a pool of successful VCs that include GSB alumni, **Steven N. Kaplan** and **Per Stromberg** have come up with two studies that answer the question. **By Patricia Briske** **Photos by Kevin Weinstein**

For years, financial contracting theories have focused on the way both sides should act. In many instances, however, the theories went awry because they didn't have a clear understanding of actual practice. Kaplan, Neubauer Family Professor of Entrepreneurship and Finance, and Stromberg, associate professor of finance, looked at the contractual agreements between VCs and entrepreneurs, then at the players themselves and how they interact.

After reviewing more than two hundred agreements between actual principals and investors, the researchers have written a detailed description of the interactions and have made progress toward explaining them. "There's a perception among entrepreneurs that VCs are stealing your company," Kaplan said. "But they're not. The way contracts are set up is that they state, 'If the entrepreneur delivers what's promised, the entrepreneur will do well.' If that's what happens, the VC will leave you alone."

Gerald Gallagher, '69, agreed with their conclusion. "We don't want entrepreneurs to feel abused, to get two years down the road and say, 'Hey, this isn't fair.' As a VC, you're building a base for a long-term relationship," he said. A general partner at Oak Investment Partners in Minneapolis,

Gallagher is among the VCs who are familiar with Kaplan and Stromberg's research.

Guy Nohra, '89, a general partner with Alta Partners in San Francisco who read the studies, echoed the sentiment. "The savvy entrepreneur will understand it's a necessary evil to give up control, meaning to give up more than 50 percent of the company. There's a saying: 'You can own 100 percent of zero or 10 percent of \$1 billion. You choose.'"

The wide variety of agreements that were struck was one feature of the business that Kaplan and Stromberg didn't expect to find. "The richness of the contracts surprised us," Kaplan said. It also surprised the investors who had provided the data for the research. "The investors each did things in a particular way, and they didn't realize others did it very differently," Kaplan said.

Put It in Writing

Kaplan and Stromberg's first paper, "Financial Contracting Theory Meets the Real World: An Empirical Analysis of Venture Capital Contracts," studied 213 contracts in 119 companies financed by 14 venture capital firms. Each VC turned over the agreements signed during each round of financing and, when possible, the entrepreneur's business plan, internal analyses of the investment, and data on subsequent performance.

What the researchers discovered was that each round of funding allows VCs to allocate various rights separately, based on observable measures of performance. "In general, board rights, voting rights, and liquidation rights are allocated such that

if the firm performs poorly, the VCs obtain full control," Kaplan and Stromberg wrote. "As performance improves, the entrepreneur retains or obtains more control rights. If the firm performs very well, the VCs retain their cash flow rights but relinquish most of their control and liquidation rights."

They also noted that VCs commonly include noncompete clauses and vesting provisions in the agreement to make it more costly for the entrepreneur to leave the firm. And, Kaplan and Stromberg discovered, when VCs have voting rights and a board majority, they're more likely to release funds based on performance milestones.

VCs ask a lot, but they bring much more to the table than a standard investor does. "VCs add value beyond what regular investors can do," Kaplan said. "When it comes to advising and monitoring the CEO, the VC will be more involved than a banker."

This increased involvement sometimes means educating the entrepreneurs. Gallagher

be very careful about not interfering with management—even if they ask you to."

Kaplan also pointed out that investors have very specific ways of participating. "VCs get different securities—convertible preferred stock versus common stock, which is what entrepreneurs get. They also have rights to control the board. But if things go well, the special rights go away. If they don't, the VCs can exert their power."

Character Counts

In their second paper, "Characteristics, Contracts, and Actions: Evidence from Venture Capitalist Analyses," Kaplan and Stromberg analyzed investment memoranda from 11 venture capital partnerships in 67 companies to describe the characteristics and risks that VCs consider in actual deals. VCs provided the researchers with the investment memorandum—from brief two-page write-ups to detailed descriptions—that the entire partnership group used to decide whether



Per Stromberg (left) and Steven Kaplan based their research on actual contracts between venture capitalists and entrepreneurs, many of them GSB alumni.

"There's a perception among entrepreneurs that VCs are stealing your company."

—Steven N. Kaplan

recalled an instance in which an entrepreneur discussed merger and acquisition possibilities with someone outside the firm before talking to the board of directors about it. "On a fairly regular basis, the CEO will do something without consulting the board because it's his first time through," he said.

And it's not uncommon for a venture capitalist to be the one who draws the line between acting as a board member and acting as a manager. "Other than when you're dealing with a governance issue, the VC should serve as a consultant, giving an opinion," Gallagher said. "But you have to

to make the investment. Most start-ups were in information technology and software, but the sample also included biotechnology, telecommunications, health care, and retail ventures. The researchers took note of how the data came into play when VCs set up the financial contracts and how the investors monitored the firms over time.

Kaplan and Stromberg found that VCs evaluated the opportunity and also considered the management team. "They ask, 'Does the entrepreneur have a good idea? Is there a big market? Does the business model make sense? Can they beat the competition?'"

Will the customers buy it? That's the opportunity," Kaplan said.

When it comes to the management team, however, Kaplan and Stromberg said entrepreneurs often meet with potential investors even when their team is short a few members. "When investors go to meet with them, they find out the team is not complete," Stromberg said. And in their paper, they write, "VCs play a large role in shaping and recruiting the senior management team. In at least half of the investments, the VC expects to play an important role in recruiting management."

Gallagher agreed. "We're frequently involved in helping the CEO pick the senior people," he said. "Experienced VCs should know about selecting people because we've had a lot of experience."

VCs also have certain expectations of the entrepreneur at the helm. Stromberg said, "You look to see how much experience he or she has, whether they're focused. You look for frugality because you don't want to give

researchers tracked the success of this sample of 67 firms, Kaplan said, "A fourth of them have gone public, another fourth have been liquidated, and on about half of them, the jury's still out. But," he pointed out, "you wouldn't expect everyone to succeed." Still, studying successful companies has value, Kaplan and Stromberg wrote. "If anything, a bias toward more successful VCs would be helpful because we are more likely to have identified the methods used by sophisticated, value-maximizing principals."

What Makes a Good Entrepreneur

"[Good entrepreneurs have] a lot of experience in that industry. They've been a successful entrepreneur before," Kaplan said. "Having a complete team is important; so if you've got one good person, can you fill it out?"

Having a good grasp of the financial situation is equally important, Stromberg added. "Frugality and being able to realistically budget and forecast is pretty important." That

"The inability [of entrepreneurs] to forecast financial progress is a relatively common complaint of VCs."—Per Stromberg

\$2 million to someone who's going to go off and just waste it."

When it comes time to draft the contractual agreement, the more uncertainty VCs face, the greater control they seek in the venture. "One problem arises when the investor doesn't know what the entrepreneur is thinking," Kaplan said. "That's known as adverse selection. The other problem is that after he's given the entrepreneur some money, the VC doesn't know what the guy's doing with it. That's called moral hazard."

How these decisions play out in the long run is hard to say, though. When the

quality is often absent, he said. "The inability to forecast financial progress is a relatively common complaint of VCs."

When it comes to personality traits and abilities among entrepreneurs, Gallagher looks for four specific qualities. "They'll need intelligence because, unlike corporate CEOs, entrepreneurs won't be surrounded by experienced staff and will often be dealing with stuff they've never seen before. Resourcefulness is important because an entrepreneur may have a great idea but not have the time or capital. They have to be open-minded because they may have to deal with

situations that are different than they'd anticipated; for example, the competition may be tougher than they thought. They have to search for ways to improve their company regardless of the source of the idea, and that includes what their competitors are doing. And they'll have to have an inner self-confidence, because the whole team will draw strength from that," Gallagher said.

"If an entrepreneur isn't open-minded, we usually have to replace that person."

Nohra listed similar qualities. "A good entrepreneur is motivated, aggressive, very bright, and focused. But," he cautioned, "those same qualities can work against you, too. For instance, stubbornness—misguided motivation—is not good when you're wrong. And the odds are so stacked against you, you almost have to be unrealistically optimistic."

Kaplan and Stromberg came up with their own ideas of what makes an entrepreneur successful. "VCs are going to do a lot of due diligence," Kaplan said. "And you'd better have a management team made up of the right people who can do what they say they're going to do. In terms of the opportunity, you've got to nail down answers to questions like, 'Is it a big enough market to be attractive? Is it something customers are going to buy?'"

The research also gives entrepreneurs a strong sense of what to expect in a contract. "It helps if you can look at them in a rational way. In one instance, we had a guy who was negotiating with venture capitalists. Before he read our paper, he thought, 'This is awful. How can they do this? It's outrageous,'" Kaplan recalled. "Then he read our paper and said, 'OK, now I understand why they're doing that; it makes sense. And here's where I can negotiate.' Or, 'There's nothing I can do; this is the way it is.'"

Stromberg said, "Entrepreneurs can also say, 'Here's where I'm getting a particularly bad deal, compared to the average guy.'"

GSB students have access to the research if they take Kaplan's course, Entrepreneurial Finance and Private Equity. "I teach how to evaluate the deal, which is based on paper number two. I also go over how you should negotiate the contract, and that's based on paper number one. I hand them out," Kaplan said. Teaching also gave Kaplan access to the venture capitalists who ultimately provided the data for the research.

Kaplan and Stromberg's next step is to see how their theories hold up internationally. They collected data from companies in 16 countries. "The U.S. clearly has been at the maximum in terms of entrepreneurial activity and venture capital. Is that because of the legal environment or the tax situation? Can you write similar contracts in other countries,

Faculty Work is Available Online

- For research on the Internet's effect on commerce by Austan D. Goolsbee, professor of economics, go to gsbadg.uchicago.edu/vitae.htm.
- For work on strategies and innovation, particularly in high-tech industries, by Toby Stuart, Fred G. Steingraber—A.T. Kearney Professor of Organizations and Strategy, go to gsbwww.uchicago.edu/fac/toby.stuart/research/.
- For additional research by Kaplan, go to gsbwww.uchicago.edu/fac/steven.kaplan/research/.

For additional research by Stromberg, go to gsbwww.uchicago.edu/fac/per.stromberg/research/.

or are there impediments? If you can, then you predict there will be more entrepreneurship," Kaplan said.

Regardless of all the variables—the kind of start-up, the experience of the entrepreneur, the contingencies in the contract—every agreement comes down to the same thing, Kaplan said.

"All you need is two people to agree." ■

A WINNING VENTURE

\$7 MILLION POLSKY GIFT GIVES CHICAGO GSB AN ENTREPRENEURIAL EDGE



Entrepreneurs, Present and Future: The GSB has given an edge to (from left) **Michael P. Polsky, '87**, as well as New Venture Challenge participants **Jeremy Graff, Peter Stratil, David Knoepfle**, and **Linda Zabors, '02**.

By Patricia Briske with Amy Rust

The Maroon Biotech team wasted no time getting down to business at the New Venture Challenge. They had 35 minutes to convince a panel of seasoned venture capitalists that they deserved \$20,000 in seed money for a new drug, and the competition was intense.

The group of students from the GSB, the Law School, and the Pritzker School of Medicine wanted funding to create Poloxafuse, which could be used to heal cell membranes in patients who had suffered a stroke or heart attack. “We’re not the first ones to discover the drug, but we’ll combine it with a proprietary product,” explained GSB student **David Knoepfle**. In 15 minutes, he described the debut of a similar drug and why it failed, the market for Maroon Biotech’s product, and why it would take \$5 million to bring Poloxafuse to the patients who need

it. Its inventor, **Rafael Lee, M.D.**, of the University of Chicago Hospitals, and Maroon Biotech chairman **Richard Egen** sat silently nearby.

Then the questioning began. “How far along are you in formulation?” asked **Karen Kerr, Ph.D. '95** (physical chemistry), managing director of ARCH Venture Partners.

“What’s your strategy for convincing the payer that this is a worthwhile thing?” asked **John Oxaal, '81**, partner at Sevin Rosen Funds. Other pointed questions followed about marketing rights and winning FDA approval.

Being able to field such tough questions is the key to winning the New Venture Challenge. For students with an eye on entrepreneurship, the annual business plan competition sponsored by **Edward L. Kaplan, '70**, founder of Zebra Technologies, is the culmination of at least half a school year’s work. The courses, lab sessions, and leadership programs had prepared them for this moment. “There’s a big difference between the first presentation we ever made in class and what we did today,” **Knoepfle** said. “The transformation is worth the cost of tuition.”

The New Venture Challenge is one piece of the entrepreneurship program. Chicago GSB is taking its newest—and biggest—step toward training tomorrow’s entrepreneurs by establishing the **Michael P. Polsky Center for Entrepreneurship**. Named for **Michael P. Polsky, '87**, founder of Invenergy, the center will help the GSB forge a future in the study, teaching, and practice of entrepreneurship.

The center is made possible in part through a \$7 million gift from Polsky, which brings the GSB closer to its campaign goal of \$15 million for entrepreneurship. The endowment provides the financial security to keep existing programs in place and explore new programs, said dean **Edward A. Snyder**.

Photo credits: (left to right) Kevin Weinstein, Nathan Mandell, Nathan Mandell

“This generous gift gives the GSB the backing to offer students both the latest research from top faculty and real-world experience in entrepreneurship that is unmatched by any other business school,” he said.

Entrepreneurial Edge

Establishing the Michael P. Polsky Center for Entrepreneurship marks a crucial step in the entrepreneurship program’s expansion, bringing together the kinds of resources and services that centers like the Kilts Center for Marketing afford their students and faculty.

Since 1998, the GSB’s entrepreneurship program has offered students

coursework that gives them a practical foundation, opportunities for real-world experience, and a network of successful alumni who guide them—and sometimes offer financial backing.

The program’s strength lies in its faculty, which includes top entrepreneurial researchers as well as practitioners. **Steven N. Kaplan**, Neubauer Family Professor of Entrepreneurship and Finance, is faculty director. He’s known for his insightful research, but it’s Kaplan’s work in the classroom that earned him a place on *Business-Week’s* list of top entrepreneurial faculty in 1995. **James Schragger**, clinical professor of entrepreneurship, also made the list. Students value the fact

that he works in the field heading up boards of directors, advising start-ups, and advising entrepreneurs.

The Entrepreneurial Finance and Private Equity class is the bedrock of the curriculum. “It’s a case-based course oriented toward things that are useful in the real world,” Kaplan said. “We give students the frameworks and analytical tools to think about start-ups in the case-oriented courses.”

Another popular course is New Venture Strategy, which Schragger teaches. Students come up with fresh business prospects, then research, develop, and present the venture to their classmates. The course is unique to Chicago GSB, Schragger said. “We’ve viewed entrepreneurial strategy as a separate discipline for a long time. Small businesses play in a different strategy arena than existing large businesses,” he said.

GSB students on the Maroon Biotech team were glad to take Commercializing Innovation with clinical professor of entrepreneurship **Scott Meadow** because of his 20-year career in venture capital. Drawing upon

cases from actual companies, students “look at how the skills of marketing, manufacturing, strategy, and organizational behavior can be used within an entrepreneurial environment—particularly within the context of finite cash,” he said. Meadow invited former colleagues to talk to the class, and the presentations were popular. “If we looked at a business plan, we could actually talk to the person who wrote it because Scott would bring them in,” said **Jeremy Graff**, another GSB student on the Maroon Biotech team.

Serious Study and Plenty of Practice

The entrepreneurship program offers students not only theory, but also a chance to apply it. The New Venture and Small Enterprise Lab and Private Equity/Venture Capital Lab place students at Chicago-area start-ups or private equity firms for course credit. “Often, [the work] is strategy related,” said **Ellen Rudnick, ’73**, clinical professor of entrepreneurship and executive director of the program. “Sometimes



Nathan Mandell

Solid Stewardship: Leadership at the GSB’s entrepreneurship program reflects both top research and real-world experience, from **Steven Kaplan** (right), faculty director and professor, to **Ellen Rudnick, ’73**, clinical professor and executive director.

it’s helping to raise capital. Sometimes it’s helping assess the market and the competition.”

Students in the Private Equity Lab work individually in a kind of intern capacity. “When you get out in the world and have to apply these things, they don’t always work the way you think they’re going to work,” Rudnick

pointed out. Students also attend weekly lectures on deal structures, portfolio management, and due diligence, among other topics, which give them a chance to network while they learn. “They’ll use the class as a way of asking if there’s anybody who might be interested in looking at the same deal,” she said.

“When you get out in the world and have to apply these things, they don’t always work the way you think they’re going to work.” —Ellen Rudnick

In Good Company

Chicago GSB alumni have launched successful enterprises in a variety of fields.

* *New Venture Challenge* participant

Peter Ahn, ’79, chairman and CEO
Block Sportswear
Leading U.S. big and tall clothing manufacturer



Matthew Gibson

Barbara L. Bowles, ’71, chairman and CEO
The Kenwood Group
Mutual fund targeting mid-cap investments

Henry “Chip” Appelbaum, ’99, vice president, corporate development
Source Precision Medicine
High-precision molecular tracking of disease and therapy

Jerrold B. Carrington, ’87, general partner
Inroads Capital Partners
Venture capital firm

Francis N. Cavalier, ’81 (XP-46), retired vice chairman and chief operating officer
McCluer Corporation
Provides consulting, architecture, engineering, and construction services worldwide

John G. Chirapurath, ’01, vice president, marketing, and cofounder
*** Sarvega Wireless**
Enables companies to create, deploy, and manage wireless applications

Brian Coe, ’99, CEO
LithoLink
Metabolic testing and disease management for kidney stone patients

Jake Crampton, ’98, founder
*** MedSpeed**
Transportation services for the health care industry



GSB Publications file photo

Robert C. Davidson Jr., ’69, chairman and CEO
Surface Protection Industries
Manufacturer and marketer of paint and specialty coatings

Gerald R. Gallagher, ’69, general partner
Oak Investment Partners
Venture capital firm



Bill Burrougham

Kathryn Gould, ’78, general partner
Foundation Capital
Venture capital firm investing in high-tech start-ups

For more experience, some GSB first-years spend the summer working at emerging entrepreneurial companies or private equity firms through internships supported by the George and Kathryn Gould Family Fund and the Kauffman Center for Entrepreneurial Leadership, among others.

Some students opt for a different path. Maroon Biotech's Graff chose to spend the summer at Pfizer in New York City to hone his knowledge of the pharmaceutical industry, a path Meadow recommended. "About 15 years ago, you could be a generalist. But VCs are becoming more specialized," Graff said. "It's better if you have solid industry experience."

For some students, internships change their career path in unexpected ways. "Oftentimes, I have students come back from their summer internship experience saying, 'You know, I need some more experience before I go out there and do it on my own,'" Rudnick said. "They recognize how really difficult it is to be an entrepreneur."



An Eye for the Best: Zebra Technologies founder and CEO Edward Kaplan, '70 (center), sponsors the New Venture Challenge. During a brief cocktail reception before the awards were announced, he spoke with his son, Alan Kaplan (left), and GSB student Jay Malin of Symphony Design, one of eight teams in the finals.

The Real Deal

There's nothing like making a pitch to make a student feel like an entrepreneur. In order to compete in the New Venture Challenge, a team has to include at least one GSB student. Many enter during their second year of business school, but Knoepfle and Graff were first-year students last spring when they submitted

Maroon Biotech's plan, competing in the first round with 58 other teams. Thirty plans advanced to a second round, and students whose plans were accepted for competition could enroll in the course Special Topics in Entrepreneurship. There, they would get advice from venture capitalists, private investors, and established entrepreneurs who serve

as class mentors. "The exposure you get to venture capitalists is something you couldn't get in the outside world," said Graff.

Only eight teams made it to the New Venture Challenge finals; *Chicago GSB* selected Maroon Biotech at random to follow through the competition. This year, proposals ranged from devices that track pets to devices that track remote assets, such as tamper-sensitive material shipped by rail. For the first time, judges added a separate "lightning round" for another five teams that didn't make the finals. Each got three minutes to present its ideas, and with the eight finalists, they would split \$50,000 in prize money.

Despite the stakes, everyone agreed that winning isn't everything. "The students have to do all the groundwork for starting a business, and that's extremely valuable," Kaplan said. "When they do start a business or invest in one, they'll know exactly what to do and what not to do."

After the Maroon Biotech team finished its presentation, judges heard from Ocuity, which intends



Voice of Experience: Judge William Mulligan, '79, (left) said the business competition mirrored the real-world experience of pitching VCs. That's why part of the preparation includes coaching from Waverly Deutsch, adjunct assistant professor of entrepreneurship (right), among others.



to become "the leading provider of tracking and monitoring capabilities for remote assets," and InfoUnity, which pledged to provide customers with "information technology market research that is quarterly, quantitative, and consistent."

Out in the hallway at Gleacher Center, Maroon Biotech members let out a collective sigh of relief

when their presentation was over. "This was a new level of intensity," said Edgar Ho, a third-year law student who sought out Maroon Biotech after learning about the proposal on the GSB Web site.

William Mulligan, '79, managing director at Primus Venture Partners, was among the 17 judges who heard Maroon Biotech's pitch. "This was

Timothy Hoeksema, '77 (XP-39), chairman, CEO, and president *Midwest Express Airlines*
Airline headquartered in Milwaukee



GSB Publications file photo

Edward Kaplan, '71, chairman and CEO *Zebra Technologies*
Manufacturer of thermal transfer bar code printers



Matthew Gibson

Dennis J. Keller, '68, chairman and CEO *DeVry*; founder, *DeVry Institutes, Keller Graduate School of Management,*



Jim Warych

Joseph D. Mansueto, A.B. '78, M.B.A. '80, chairman and CEO *Morningstar*
Mutual fund research firm



Matthew Gibson

Joseph Neubauer, '65, chairman and CEO *ARAMARK Corporation*
World's third-largest food service provider



Photo courtesy of Oberweis

James D. Oberweis, XP-45 ('80), president *Oberweis Asset Management*
High-growth equity investing for institutional clients

Sol Kanthack, '00, president and cofounder *Brightroom*
Internet-based photography business



Matthew Gibson

Kenneth Kaufman, '76, managing partner *Kaufman Hall & Associates*
Provides financial advisory services and software to health care organizations

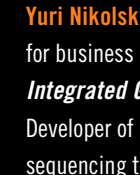
Center for Corporate Education, and Becker Conviser Professional Review

Joel Krauss, '74, founder *Fred Belmont, '75,* founder *Omnitech*
Strategy and marketing consulting firm focused on the technology industries



Matthew Gibson

Robert C. McCormack, '68, founding partner *Trident Capital*
Venture capital firm specializing in Internet and information technology



Matthew Gibson

Yuri Nikolsky, '99, vice president for business development *Integrated Genomics*
Developer of microbial genome sequencing technologies



Kathleen Weinstien

Louise O'Sullivan, XP-44 ('80), cofounder and president *Prime Advantage*
Supplier of sourcing services, logistics management, and e-commerce technology to industrial manufacturers



Kevin Weinstein

Specialist in the Field: Student **Jeremy Graff** said his experience in the pharmaceutical industry gives him an edge in entrepreneurship.

very much like what they would have faced if they came to our firm," he said.

Regardless of which teams would emerge as winners, Rudnick said each one had taken an enormous step toward creating a real company. "To even make it to the finals, each team had to be selected by three out of five judges. In the real world, it only takes one person to fund you.

"The exposure you get to venture capitalists is something you couldn't get in the outside world." —Jeremy Graff, entrepreneurship student

"I've had judges come up to me today looking for teams that hadn't made the finals, saying, 'Where's that plan? I thought it was good.'"

Waiting for judges to select the winners, Maroon Biotech members kept their thoughts upbeat. "To make finals in a group where there's such strong competition, that really says something," Knoepfle said. Graff agreed. "Regardless of how this turns out, you know there's something there with your company."

It took the judges less than an hour to pick the top business prospects. When Kaplan stepped to the podium, the first one he named was Maroon Biotech, which had won third place

and \$5,000 in start-up money. Second-place winner Advanced Chromatography Systems garnered \$10,000 to "develop innovative liquid separation technologies." Ocuity took the \$20,000 first-place award. The top three winners also won free legal services from Altheimer & Gray, and the other five teams each received \$2,000 for their participation, Kaplan said. Each of the five teams that competed in the lightning round received \$1,000.

The Ocuity team was elated. **Gurinder Dhillon**, a weekend student, said he thought the concrete nature of their business plan appealed to the judges. "After the dot-com world burst, people became interested in



Nathan Mandell

A Promising Venture: First-place winners in the New Venture Challenge were Ocuity team members (from left) weekend student **Gurinder Dhillon**, **Linda Zabors**, '02, and CEO **Mary Koelle**. "VCs have been more receptive to talking with us," Dhillon said after the competition. Weekend student **Vinay Pande** is not pictured.

ideas that were more solid," he said. "And there's a real need for asset tracking in the rail industry, which has fallen behind the trucking industry where these devices have already been implemented." Also, Dhillon noted, the September 11 attacks have boosted business for many firms that provide security.

The prize money was welcome, but the honor of winning meant more, students said. "It's in our presentation materials now, and it definitely gets attention," said **Linda Zabors**, who was a second-year student during the New Venture Challenge.

Members of Maroon Biotech agreed. "It was tough competition," Graff said. "It gives you credibility when you rattle off the names of the judges you presented to. Getting third place is incredible validation from such experienced VCs." Having Ho of the law school and **Peter Stratil** of the Pritzker School of Medicine

on their team was an advantage, he added. "They brought different perspectives," Graff said.

Over the summer, team members would continue to work on the project in their spare time, looking for a CEO and applying for grants to fund the \$5 million in necessary research, and taking advantage of the free legal advice from Altheimer & Gray. The scope of the project means Poloxafuse may not make it to market for a couple of years, but Maroon Biotech members are committed to going as far as they can.

And the New Venture Challenge may have hooked them for good on a career in entrepreneurship. "I saw three businesses besides ours that I'd be willing to invest in," said Knoepfle. "Some of the New Venture Challenge's biggest success stories have been the ones that didn't win." ■

Winning Teams from the New Venture Challenge 2002

First Place: Ocuity
GSB students: Linda Zabors, '02; and Gurinder Dhillon and Vinay Pande, weekend students
Other team member: Mary Koelle, CEO
Description: The company designs, manufactures, and supports asset-tracking equipment for transporting hazardous materials and tamper-sensitive shipments.

Second Place: Advanced Chromatography Systems
GSB students: Samuel Nickerson, Christopher Pattinson, and Robert Benson, now second-year students in the full-time program

Other team members: Seth Snyder and James Franck, both of Argonne National Laboratories
Description: The company develops liquid separation techniques for industrial processing. ACS's first product, SepraStack, is a patent-pending system that can reduce operation costs and improve manufacturing capacity.

Third Place: Maroon Biotech
GSB students: Jeremy Graff, David Knoepfle, now second-year students in the full-time program

Other team members: Edgar Ho, J.D. '02; Peter Stratil, Pritzker School of Medicine student and now first-year GSB student; Raphael Lee, M.D., University of Chicago Hospitals; and Richard Egen, chairman
Description: Maroon Biotech is commercializing Poloxafuse, a drug to treat injuries and diseases linked to cellular membrane damage. A similar drug was too strong; Poloxafuse will enable the healing agent to be delivered in smaller doses.

Joel M. Stern, '64, managing partner and CEO **Stern Stewart & Company**
 Corporate finance advisory services

Philip Summe, '96, general partner **Gabriel Venture Partners**
 Venture capitalists working in communications and networking, information technology, and Internet industries

Robert Taylor, '90, (left), chairman and former president and CEO **Joseph Beatty, '89**, former vice president and chief financial officer **Focal Communication Corporation**
 Telecommunications firm

John W. Van Dyke Jr., '69, president **Dakota Water Systems**
 Water treatment products and systems

Arthur Velasquez, '67, chairman, president, and CEO **Azteca Foods**
 Producer of tortillas, salad shells, and chips

POLSKY'S ENTREPRENEURIAL EXPERIENCE EMERGED IN U.S.

“When you start a company, your chances of success are best in an area where you have deep knowledge.” —Michael P. Polsky

When he was growing up in Ukraine under Soviet rule, Michael P. Polsky's options seemed very limited. Certainly nothing hinted that he would make a career in the United States as an entrepreneur.

“After high school, I tried to get into the university, but it was not easy, particularly because I was Jewish. It was possible for me to get into technical school, however, which was OK since I liked math and physics.”

At Kiev Polytechnic Institute, he discovered an interest in thermodynamics. He earned a degree in mechanical engineering. “I was lucky. It was a good education that was in line with western education,” he said.

Polsky, 52, began his career designing power plants in Ukraine in 1973. Despite perestroika, “it was still the classic Soviet Union situation—very political, no freedom,

no opportunities.” In 1976, he and his wife immigrated to the United States, where he landed a job in Ann Arbor, Michigan, working on power plant design for Bechtel Power. In 1978, Polsky was hired by Brown Boveri in St. Cloud, Minnesota, to work on gas turbines. “I was an application engineer, and that’s when I got more exposure to the business side, doing things like economic analysis,” he said.

In 1980, Polsky joined Fluor/Daniel in Chicago as a supervising engineer. “Profound changes were going on in the energy field in the early 1980s. The laws had changed, and there was an opportunity for private people to generate energy. I was fascinated. I tried to push Fluor into owning and operating power plants. Then I started looking for opportunities to do it on my own.”

In 1982, he enrolled in the GSB's evening program, where he sharpened his entrepreneurial skills. He earned his M.B.A. in 1987, but by 1985, he was ready to launch Indeck Energy Services in Buffalo Grove, Illinois, with a partner. Indeck built power plants on the East Coast with backing from investors. During his tenure, *Inc.* magazine rated it one of the 100 fastest-growing companies nationwide.

Polsky attributes the success of his first venture to his expertise in the power industry, his business acumen, his hard work, and being in the right place at the right time. “When you start a company, your chances of success are best in an area where you have deep knowledge and you’re not relying on someone else to explain things to you,” Polsky said.

In 1990, he created Polsky Energy and tackled the mercurial energy market on his own as an owner and operator of power plants across the country. “In 1996, we won a bid to build a large plant in Wisconsin,” he said. “At that point, we were one of the most significant power plant developers in the United States.” In 1999, he changed the name to SkyGen, and a year later, he sold



Expertise in Engineering and Entrepreneurship: Michael P. Polsky, '87, attributed his success in owning and operating utilities to his strong educational background in both thermodynamics and business.

the firm to Calpine. “It was the right time to exit, which is important because energy is a very cyclical market,” he said. Polsky stayed on as a member of the board, but about six months later, he was ready to start another company. “By nature, I was more interested in working on my own,” he said.

He started Invenergy in 2000. “I shifted my focus to acquisitions. I’m more of a financial player now,” he said.

His success has enabled him to give \$7 million to create the Michael P. Polsky

Center for Entrepreneurship. “The GSB has been very beneficial for me,” he said. “The M.B.A. has given me a complete package as an entrepreneur. Your chances for success increase exponentially when you have all the skills. There’s nothing better than understanding it all yourself.”—P.B.

Entrepreneurial Gifts Give GSB an Edge

Several alumni and friends of the school have supported entrepreneurship at Chicago GSB. Listed below are those who made gifts of \$50,000 or more.

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