

Warner tried to spread the wealth

But venture funds failed; management; timing cited

**Jennifer Haberkorn THE WASHINGTON TIMES
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Four of the five venture capital funds set up by former Gov. Mark Warner a decade ago as a way to infuse central, southern and western Virginia with much-needed cash for technology start-up companies have since folded or are in the process of shutting down, failing to spur the economic growth he once championed.

Mr. Warner, a Democrat now considered the front-runner in the U.S. Senate race in Virginia to replace retiring Republican Sen. John W. Warner, no relation, created the funds as a private citizen before his 2001 election as governor. He used his own money - between \$1 million and \$5 million, he says - coupled with investments from university foundations, corporations and individuals from five diverse regions of the commonwealth.

The five venture capital investments were created after Mr. Warner's unsuccessful 1996 Senate campaign, but four of them failed to make much of a return for their investors and closed or are in the process of closing, according to interviews with investors and some fund managers.

A fifth, Envest Ventures, has raised more than \$160 million in three rounds of fundraising but makes only half of its investments in Virginia.

The Virginia delegation waves signs and cheers for Mr. Warner on the final night of the 2004 Democratic National Convention at the Fleet Center in Boston. Critics saw the venture capital funds as a way for Mr. Warner to strengthen his relations in southern and rural areas of Virginia.

Designed to infuse young technology firms with much-needed cash, venture capital investments generally are made by groups of third-parties in exchange for a share in the invested companies. The ventures often are risky because the companies could flop.

The investments "for the most part, did not turn out to be financial successes," said Irving Groves Jr., who co-manages the fund for southern Virginia. "This fund at least found it very difficult to locate

investments that the investment committee felt would be beneficial for the communities and the investors."

Mr. Warner and other investors said the funds floundered because of poor management and poor timing - they were created just before the stock market crashed in 2000, prompting scores of technology companies to fold.

"The idea was the right idea. I'd do it again," Mr. Warner told The Washington Times during an interview last month. "The timing was bad and in certain cases, the execution was bad."

The five funds - Southwest One, Monument Capital Partners, Southside Rising, Envest Ventures and Shenandoah Capital Ventures - targeted different geographic areas around Virginia. Four of the funds - Envest, which focused on the Hampton Roads area, is the exception - have closed or are in the process of closing without returning much of their investments.

For instance, Monument Capital, which started closing down last year, targeted the Richmond area. It raised about \$20 million from investors but returned approximately \$1 million.

"I don't think the fund could have done a whole lot worse," said Ivor Massey Jr., whose family investment group, Triad LC, had invested in Monument Capital.

In the case of Monument Capital, Mr. Warner said, money was invested too quickly and "there were a lot of companies that looked like they were home runs for a while before the whole [technology industry] blew up."

Political gain?

Some Warner critics have said the funds were established to help him in his 2001 run for governor by deepening his ties to southern and rural areas of Virginia, where Democrats previously had not performed well in statewide elections.

One of Mr. Warner's key campaign messages in the senatorial race was "bringing Virginia together, new economy, new opportunities," and he often focused in speeches on the need to bring Virginia up to speed in technology and education. During the campaign, he touted his experience as an entrepreneur and in the high-tech industry as necessary to carry Virginia into the new digital age.

During an 11-day tour in March 2001 to formally announce his candidacy, Mr. Warner said he would bring a businessman's perspective to the challenges of a diverse state and a changing economy and better management to state government.

Mr. Warner told The Times the funds weren't motivated by politics,

adding that the investors were experienced in venture capital and familiar with the risks in investing.

"Was there a goal that I thought Virginia would be better with more venture capital and more entrepreneurial activity in the state? Yes," he said. "But I made it clear to everybody that . . . it was not about job creation, it was about a financial return."

But at least some of the investors were thinking about Mr. Warner's political future.

"We thought it would raise the profile of Mark Warner in this area," said Warner Dalhouse, who helped form and invested in the Southwest One fund. "That was a secondary or even tertiary objective. But most of us had that in the back of our minds."

Mr. Warner was instrumental in finding other investors, according to fund managers. Many of the people interviewed said they have close ties to Mr. Warner or support his 2008 Senate campaign.

Venture capital is typically a risky undertaking: Groups of investors throw significant amounts of money into a pot, which fund managers use to invest in young companies. Participants hope the companies become successful so they see a return on their investment.

The venture capital funds established by Mr. Warner ranged in size from Envest, which has raised more than \$160 million, and Monument Capital at \$20 million, to the smaller funds, which raised between \$3 million and \$7 million each. Venture capital funds are private and not required to file public disclosure documents.

The funds were invested in wide-ranging technology companies, such as an online home-seller, a voice-activated transcribing company and Web site hosts - companies with dot-com names such as iPipe Inc., Homebytes.com and Nueweb Interactive.

Southwest One, which was administered in Blacksburg close to the region's main technology cluster at Virginia Tech, and Southside Rising, which operated out of Roanoke, raised \$5 million to \$7 million each.

Southside has invested about \$5 million and is winding down operations, Mr. Groves said. Southwest One closed last year, Mr. Dalhouse said.

Shenandoah Capital Ventures, the last of the five funds, closed before it raised the full \$5 million it intended to gather, said Richie Wilkins, who helped raise funds for the group.

'It fell apart'

"By the time we got around to [raising money], the tech stocks all

started to crash. When we first started talking about it, it sounded great, but it fell apart," Mr. Wilkins said.

Envest is the only one of the five still going strong today and the only fund to raise a second round of capital. The Virginia Beach-based fund has raised more than \$160 million in capital in three rounds and invested in dozens of companies, according to the group's Web site.

The fund was designed in 2000 to invest in the Hampton Roads area. Since then, Envest's geographic target has expanded outside of Virginia with about half of its companies located primarily on the East Coast.

The fund's first round was one of the country's top performing venture capital funds in 2000, according to Paul Hirschbiel, a founder of Envest.

Creating the regional venture-capital funds throughout the state's rural areas to help business start-ups after the 1996 elections was a key feature in Mr. Warner's effort to portray himself in 2000 as a successful businessman.

Rodney Lamkey Jr./The Washington Times Mr. Warner shares an idea with Jim Webb on his senatorial campaign in 2006. Mr. Warner used donations from university foundations, corporations and individuals to try to help businesses in five diverse regions of the state.

At the time, Mark Rozell, a professor at Catholic University who studies Virginia politics, described the strategy as "brilliant," saying that without having held elected office and without having a public record, Mr. Warner could point to "tangible things he has done for people."

During an October 2001 debate with his Republican gubernatorial challenger, Mark Earley, Mr. Warner said, "I created regional venture capital funds to invest in early stage businesses in southside and southwest Virginia so that young kid in Martinsville doesn't have to pick up and move away.

"We have got to grow the economy in every corner of Virginia, and I will," he said.

In his first television advertisement in March 2001, Mr. Warner was shown visiting different parts of the state while a bluegrass song in the background touted his accomplishments. The song, called "Warner," focused particularly on what he could do to help folks in the rural southside and southwest areas of the state.

His message was simple: Mark Warner would be "the hero of the hills," and it would take a guy who "gets it" to bring prosperity to the region.

Barbara L. Salisbury/The Washington Times Former Virginia Gov. Mark Warner used between \$1 million and \$5 million of his own money to create five venture capital funds. Four of them have closed or are in the process of closing.

An entrepreneur

"What I am is an entrepreneur," he said during a June 2001 stop in Dublin, Va. "An entrepreneur is somebody who can sometimes seize upon a good idea, bring people together, hopefully, then empower a management team to then go out and work on that idea, and then take it into action."

But Mr. Warner argued that the funds were probably not a good political move, telling the Richmond Times Dispatch in 1998 when he set up Southwest One: "If I were doing this for political advantage, I ought to have my head examined. Think about it: I'm taking 75 of the most successful business people from Roanoke to Lee County and putting them in high-risk ventures."

The regional venture capital funds represent a blemish on Mr. Warner's successful business background, which he has touted in previous campaigns. He earned his reported net worth of \$200 million through early involvement in the telecommunications industry, co-founding a cellphone company that became Nextel and establishing Columbia Capital Corp., a nearly 20-year-old Alexandria venture capital firm.

The investment teams that selected the Virginia companies, which included Mr. Warner, were more impressed by "gee whiz" technology than by sound business models, Mr. Massey said. He and other investors also said the funds didn't have strong managers who could help investment companies when they weren't doing well.

It is common for investors to provide temporary help to keep a company - and their investment - afloat.

"The concept was a good one, but it was a victim of execution and timing," said R. Timothy O'Donnell, a Richmond businessman who invested in Monument Capital. "I don't think there's a lot more to it than that."

Virginia didn't have the infrastructure in place in the late 1990s and early 2000s to help young technology companies, said Raymond Smoot, chief operating officer and treasurer of the Virginia Tech Foundation, which committed to investing \$500,000 in Southwest One.

He points to hands-on coaching available today to start-ups in the Virginia Tech Corporate Research Park that didn't exist 10 years ago.

"The environment today is much more supportive," he said.

Many of the companies fizzled because they couldn't find future investors to keep them running. In one case, Monument Capital sued Bonita Software, a Raleigh, N.C., wireless software firm, to try to recoup a \$750,000 investment. It pushed Bonita to file for bankruptcy.

Experient Holdings Inc. and Homebytes.com, other Monument Capital investments, also have filed for bankruptcy. Many of the others, such as iPipe Inc., simply folded as they ran out of money.

But there were some successes.

Luna Innovations Inc. got funding from Envest and Southwest One, according to investors. The molecular technology company, which was previously called Luna Technologies and Luna Analytics, successfully completed its initial public offering in May 2006, trading under the Nasdaq symbol LUNA.

A handful of other companies, including ScholarOne Inc. and BrightPod Inc., also were bought out.

Mr. Warner was already quite familiar with venture capital when he ran against Sen. Warner in 1996 and realized during his travels throughout the state that it wasn't easy for Virginia companies outside of Northern Virginia to find venture capital.

'Where my mouth is'

"I thought I'd put my money where my mouth is," he said of why he set up the funds, adding that he hoped they would encourage technology companies to develop in Virginia.

Many of the areas targeted, specifically in the South and Southwest, had lost thousands of manufacturing jobs in recent years and were hoping to build themselves back up with tech-related companies. For example, Martinsville, a city of 15,000 in southern Virginia, was known in the 1980s for its large-scale sweatshirt and furniture production.

But many of those jobs have since gone overseas, leaving the area now with double-digit unemployment.

Mr. Warner arrives at the inauguration of Tim Kaine as governor of Virginia during a ceremony outside the reconstructed House of Burgesses at Colonial Williamsburg in 2006. Mr. Warner said his funds failed because of poor management and poor timing.

In addition, Virginia's universities were educating students with technology degrees, but many of the students were chasing jobs to Silicon Valley in California because there weren't any in Virginia. Venture capital was needed to bring tech companies to the area, but

most of the limited venture capital in the state was centered in Northern Virginia.

The hope was that the funds would help local technology companies grow, creating jobs to replace the lost employment.

Investors say they put their money into the funds because of Mr. Warner's background, as well as the idea of making a statement that technology companies are welcome in areas such as Martinsville, Shenandoah and Hampton Roads.

"Most of the people who put money into these funds expected they were making a commitment to economic development more so than for personal profit," Mr. Groves said. "Unfortunately, in the case of Southside Rising, that was the case.."

Investors said the funds helped educate budding entrepreneurs about the venture capital process and encouraged them that Virginia has a place for high-tech companies.

"I don't think anybody regrets having done that," Mr. Dalhouse said. "Nobody got rich, but we did create an awakening for the amount of entrepreneurial activities and new innovations out of this area."

Investors say the funds met some of their high expectations and had noble intentions.

"It would have been great if 10 years later, we were the 'Silicon Port' or something," said Mr. Hirschbiel of Envest, playing off the name of Silicon Valley. "But it's unreal to expect that to happen overnight."