At Stanford, venture capital reaches into the dorm

Investors are seeking out startup ventures earlier than ever, raising new risks

BY SARAH MCBRIDE

STANFORD, CALIFORNIA, DECEMBER 10 2014

At the end of their first year at Stanford University, a half dozen students snagged an apartment-style dormitory on the third floor of Griffin House, overlooking the campus golf course. A little over a year later, in the autumn of 2014, just two were left at Stanford. The others had gone to work on their startups.

They had a big advantage: Fellow roommate Chris Barber, 21, was a budding venture capitalist, already learning about the business of injecting funds into promising new firms. He funded companies run by three of his roommates.

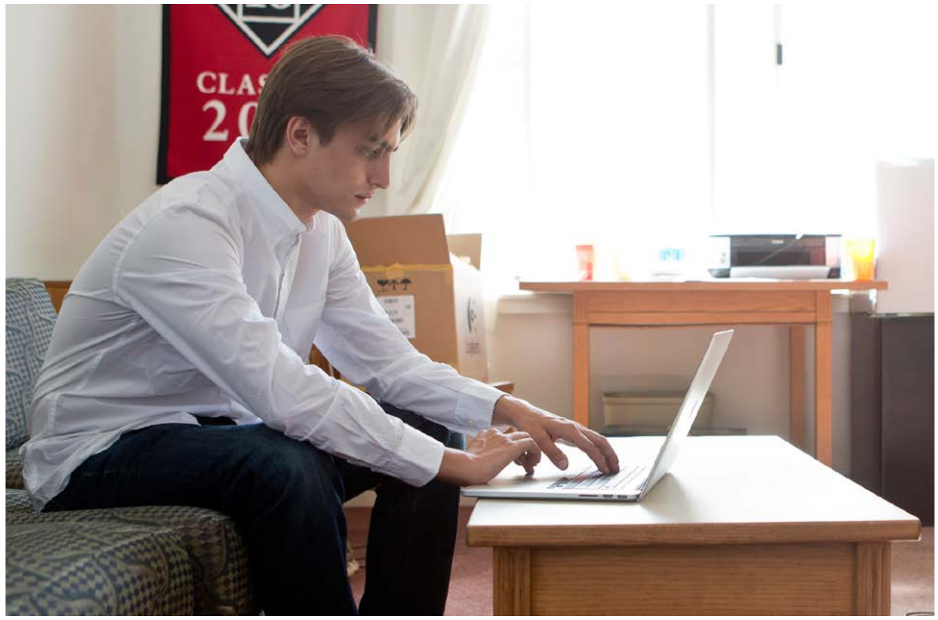
Long one of America's elite universities, Stanford has grown into the leading alma mater, by far, for entrepreneurs receiving early-stage funding from top venture capital firms.

What most outsiders don't see: how early the investment community starts cultivating Stanford students, how committed the students are, and how deeply the VC culture has burrowed its way onto campus.

At Stanford now, venture capitalists are teaching, investing in students' startups, volunteering as mentors, occasionally even visiting the dorms. Professor-turned-VC Balaji Srinivasan visited Griffin House last autumn, shortly before he joined top venture firm Andreessen Horowitz. He was invited to discuss the emerging currency bitcoin.

The dedication can come with a price. Last year social gatherings at the suite, Griffin 304, were rare. A small fridge held mostly soda, not beer. For most of the academic year, Barber was the only roommate with a regular girlfriend. One of his roommates, Jesse Leimgruber, complained that girls drain hours in the late evening, "the most productive time for a startup."

For VCs, the attraction of academia is simple: Some of the hottest tech start-ups are founded by college kids. Student-run firms that met venture capital backers at Stanford include Snapchat, the photo-sharing service. Chief executive Evan



ALWAYS ON: Jesse Leimgruber, CEO of NeoReach, is entirely focused on business. His startup won investment from 21-year-old roommate Chris Barber (on cover). **REUTERS/BECK DIEFENBACH**

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> **Vivek Wadhwa**
> Rock Center for Corporate Governance

Spiegel dropped out two years ago to work on the venture. His first VC backer, Jeremy Liew, is a Stanford alumnus.

Perhaps most famously, Google founders Larry Page and Sergey Brin were Stanford graduate students. They met their first investor through an introduction from Professor David Cheriton, who also ended up investing.

Some on campus find the industry's reach troubling. The students' focus on doing business, they say, distracts from the scholarly mission of college and opens up instructors to potential conflicts of interest. The venture money also provides a temptation to drop out.

"VCs can be a bad influence and are not a good role model for students," says Vivek Wadhwa, a fellow at Stanford's Rock Center for Corporate Governance. Faculty members who aren't venture capitalists counter that VCs provide invaluable real-world insights.

Stanford's graduation rates have dipped somewhat in recent years. Of students who enrolled in 2009, 90 percent had graduated within five years, Stanford said, compared with a five-year graduation rate of 92.2 percent five years earlier. Some students say they are quitting to start companies. Stanford says it doesn't track the reasons students leave.

Reuters asked Stanford President John Hennessy whether there would be a conflict of interest if a Stanford instructor offered a student an implicit incentive, in the form of venture cash, to leave school.

"It's clearly at some level a conflict," says Hennessy. "It's not a direct conflict, but it is a worrisome issue."

Late last year, the university introduced a formal policy to govern faculty investments in student companies. If a faculty member has direct involvement in the student's academic program, the investment

LUMINARY ALUMNI: Sergei Brin, co-founder of Google, and Evan Spiegel, who co-founded Snapchat, both went to Stanford, which had links to their early investors. **REUTERS/STEPHEN LAM, LUCAS JACKSON**

requires approval, including from the vice provost and dean of research.

The new policy states "The strong presumption is that such involvement would constitute a significant conflict of interest that could not be mitigated or managed and that it would therefore not be permitted." It applies only to people with full-time positions.

A Stanford spokeswoman said no requests for approval have been made by faculty members.

Some investor-professors bristle at the notion they are buttressing their portfolios with projects from current students. The vast majority of junior students stick around to earn their degrees, and most don't start companies, they point out. At the School of Engineering, the department that has done the most to welcome venture capitalists in roles such as instructor, adviser or guest lecturer, faculty members say VCs serve a valuable pedagogical purpose.

"If someone wants to go deep, getting a practitioner like a venture capitalist to talk about what they do works," says Tom Byers, an engineering professor and director of the Stanford Technology Ventures Program. "Every instructor invites a venture capitalist into their classroom in that vein."

PLUGGED IN

A career in venture capital normally follows years of entrepreneurial success. Barber, the young Stanford student, got into the game early after a chance encounter at a conference.

The lanky Australian computer science major had been drawn by Stanford's reputation as an entrepreneurial hotbed. But after enrolling in the autumn of 2012, he became disenchanted with the focus on consumer companies he saw among fellow students. Inventions such as smartphone apps struck him as frivolous, relatively easy to get off the ground and creating uncertain value.

Ideas for companies geared to serving businesses, by contrast, seemed to struggle to take flight. Their founders could use an experienced entrepreneur to guide them, he decided, as well as more mutual support.

That summer he crashed a conference given by 500 Startups, a popular program

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for entrepreneurs. At lunch, he found himself sitting next to Matt Mochary, a 46-year-old who started a technology-services company in the 1990s and was now involved in the early-stage funding known as "angel" investing.

Mochary learned Barber was couch-surfing and invited Barber to stay with him and his family. As he got to know Mochary, Barber decided the former technology executive could take on the role of adviser to students who wanted to create business-oriented companies.

"The original idea was to meet a bunch of people students could go work with," says Barber. "To have a network of people." In turn, Barber let Mochary in on the earliest stage of companies imaginable – when they amount to little more than a dorm room bull-session. Mochary offered Barber a deal: The Stanford junior could invest up to $10,000 of Mochary's cash on his own. Larger investments required Mochary's approval. Barber would get 10 percent of any returns.

Barber was to invest in two businesses set up by his room-mates: NeoReach, a marketing firm founded by Leimgruber; and an identity-verification company, BlockScore. Most enterprise startups take

PITCH PERFECT: Stanford students present to a group of visiting venture capitalists during their Technology Entrepreneurship class. **REUTERS/STEPHEN LAM**

at least a couple of years to get off the ground, but he and Mochary say interest from bigger institutional investors in their startups is promising.

By late last year, Barber had convinced Mochary to come coach his classmates. The two launched an informal course, Focus.VC, which they taught from January to April. Mochary presented major concepts such as time management and business development. Barber mastered specialized software and other startup tools, so he could help novice entrepreneurs with specifics like payroll.

At the course's end, many of the students pitched to professionals, including representatives from several top Silicon Valley firms brought in by Mochary. Four of seven companies that presented raised money from investors. Another Focus.VC and Griffin House company, BlockScore, lined up funding days beforehand.

The young entrepreneurs attributed the program's success to the coaching they got and to Mochary's Silicon Valley contacts.

"Every actual problem you'll have, he'll open up his network," says Leimgruber. Mochary put in a good word for him with Founder.org, a seed fund that specializes in student-run startups. It eventually invested, drawn by Mochary's reference and the accomplishments of the founders, said Tony Ayaz, chief revenue officer at Founder.

SHOULD I STAY OR SHOULD I GO?

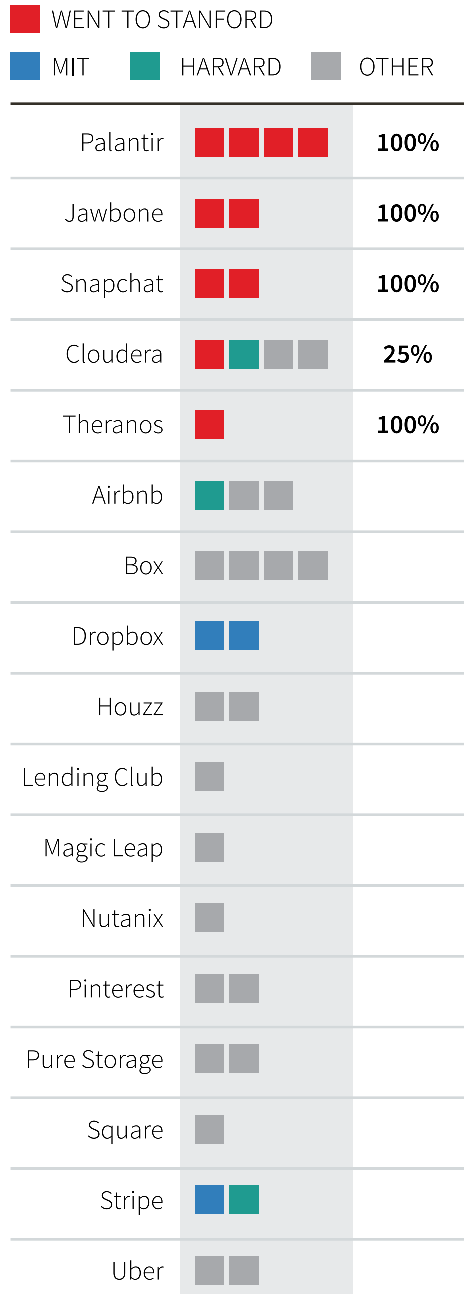
When they weren't in class or working on their startups, the inhabitants of Griffin 304 debated ideas long into the night. "To me, this is so much more fun than going to a party," said BlockScore co-founder Alain Meier. "Because it's lasting."

BlockScore helps financial-services companies verify customer identities. By last April, Meier and his Stanford partner John Backus faced a dilemma. They had to deliver a crucial computer-science assignment at the same time as writing a presentation they'd been invited to make to potential investors through an off-campus program for startups, Plug & Play.

They decided to divide the workload. Backus took a software-writing assignment for the computer-science class and Meier tackled the presentation. They got an A- for

Stanford Ties

Number of founders, and universities attended, at U.S. venture-backed startups in last decade now worth $2 billion or more.



TOTAL **28%**

Source: LinkedIn, company websites
Graphic by Malathi Nayak and Matthew Weber

the computer-science project, and $2 million in venture capital funding from top firms such as Battery Ventures and Khosla Ventures. That's an outcome most student entrepreneurs won't reach for years.

The duo felt compelled to leave Stanford to work full time on the business, which they co-founded with a more experienced entrepreneur. "It just got to a point where it was BlockScore priority, school second," said Meier.

In that decision, they joined another roommate, Ryan Breslow, who had already decided to take advantage of Stanford's leave of absence policy to work on his bitcoin company. (A sixth roommate who was due to share Griffin House had ducked out even before the year started, to work on his alternative energy company.)

When Backus and Meier needed somebody to guarantee the lease on their new apartment, Mochary stepped in. BlockScore invited Barber and Mochary to invest. They also tapped another venture capitalist with close ties to Backus – his father, a partner at New Atlantic Ventures and a Stanford alumnus. The elder Backus says he has mixed feelings about his son's ditching school for a startup.

"The dad part of me says, 'You got into Stanford, now get your degree,'" says Backus Sr. "The VC part of me says, 'You're doing it right.'"

LEAVE OF ABSENCE: The university has a flexible policy which lets students take time out to work on their startups, and return to their studies. **REUTERS/BECK DIEFENBACH**

TEACHER-INVESTORS

Down the hall at Griffin House, Leimgruber was determined to stick to his studies.

The son of a Florida auto-body worker, he and his older brother, PJ, were the first two in the family to go to college. He started the company with PJ and another classmate who did not return to Stanford this semester. The Leimgrubers' mother now works for NeoReach, which helps companies market themselves through word-of-mouth on social media.

"School is my main priority. Always," Leimgruber said in June.

NeoReach eats up around eight hours of his day, he said. Its biggest investor was Founder.org, the fund that specializes in student startups. "They told us to stay in school," Leimgruber said. "That's a key reason we went with them."

In early August, Leimgruber almost quit Stanford. The Valley Fund, a venture-capital firm run by Stanford instructor Alex Gould and partner Steve O'Hara, offered to invest $3 million in his company. Gould has never taught Leimgruber, both say.

Leimgruber thought about taking the money. He felt it would bring an obligation to leave Stanford to focus fully on the business. But he also felt every month in school carries an opportunity cost that could make the difference between developing a company worth millions and one worth billions.

By December, he was "99 percent moving forward" with taking the cash. Either way, Leimgruber now says he won't be coming back to Stanford next semester, but he expects to take advantage of the flexible leave of absence policy and return in the next few years.

That means of the original Griffin House gang, only Barber will return next quarter.

"It's a great outcome," he said about the suite and the accomplishments of his roommates. "If current freshmen or grad students are considering doing something similar, I'd strongly support it."

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