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VC Transparency Is The New Black

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When Instagram was bought by Facebook earlier this spring for $1 billion, one question lingering on everyone's minds was how much VC firm Andreessen Horowitz made on the deal. The firm had made an early investment in the photo sharing startup but then bet against it after Instagram's pivot by later by supporting a rival.

A few days after the Facebook-Instagram acquisition was announced, the firm's partner Ben Horowitz took to his blog to not only reveal the back story of the investment in Instagram, but also how much the firm had made off the deal under the terms of the acquisition—$78 million off of a $250,000 investment

Transparency in the VC world is the new black. From the outside, investing terms look like a black box — in goes the company and out comes a cap table. Dialogue that was previously reserved for closed-door, back-office meetings is now taking place in the open public.

For example, take Founders Fund partner Brian Singerman's recent TechCrunch post on "The Paradox of VC Seed Funding." Singerman laid out the brutal economics of seed funding, and concluded that they don't really make sense. In the same post, Andreessen Horowitz's Marc Andreessen left a comment to explain the dynamics of the firm's strategy in seed rounds, and why.

A few weeks ago, TechCrunch founder and CrunchFund partner Michael Arrington admitted publicly on his blog, Uncrunched, that at first he didn't understand the hype around Klout. But at the urging of Kleiner's Chi-Hua Chien, he took another look at the company and decided to invest in Klout's latest round. A few years ago, this was insider gossip — today it's common knowledge.

If you're an entrepreneur, this means that you are more informed than ever about the other side of the investment table. Kleiner Perkins Managing Partner Ted Schlein explains that for the first time the class of entrepreneur is a digital-native vs. digital immigrant. "This is an entire generation of entrepreneurs that have grown up with technology, so the web is their oyster. There is access to so much information."

True Ventures founding venture partner Tony Conrad believes that "the current education of entrepreneurs is unprecedented." With resources like TheFunded, which allows entrepreneurs to rate and review VCs, and AngelList, there is more information and data about the funding world in the current market. VCs and investors realize that they need to be part of this conversation. "Unlike ten years ago, entrepreneurs know what a standard liquidation preference looks like. VCs have learned that you can't put out aggressive terms, because the entrepreneur knows better," says Conrad.

Lightbank partner Paul Lee agrees, explaining that while VCs have been open about deal terms, strategy and more in closed circles; there's been a shift towards openness with the entrepreneurial community.

Schlein believes that the more-informed entrepreneur is a sign of the times. “Consumers are better educated about almost everything they do today, such as buying a car now vs. buying a car ten years ago. There’s an enormous amount of information for the consumer, and the consumer in this case is the entrepreneur.”

So, why the shift towards openness?

Adeo Ressi, the founder of TheFunded and the startup incubator Founder Institute, tells me that transparency in the VC world has been a result of the standardization of deal terms, which are largely founder-friendly. In the past VCs have had wide variety of terms placing the impetus on the entrepreneur to figure out the nuances. Through TheFunded, VentureHacks and other sites, practices like this became more exposed and less effective, which in turn motivates investors to be more open and standardized.

Another reason VCs are more open these days is an increase in competition and a focus on brand building.

“We’re seeing the single largest explosion of angel investors and VCs are being squeezed out of early stage investing,” says Ressi. “VCs and investors have to be transparent and open as a means of differentiating themselves from angel investors.” VCs and investors are using blogs, Twitter and Facebook as a way to distinguish their approach, and build a reputation.

Of course, VCs like Union Square Ventures’ Fred Wilson have been blogging for some time now, but now you’re seeing many more firms and investors taking to blogs to talk about investments, strategy and more. You also see heavy engagement from Andreessen and others on Q&A platform Quora.

Schlein says that the increase in transparency and openness shows the maturing of the marketplace, “Venture itself has only been around for 40 years. There is a realization that this is a service business, and people are going to talk about it and that’s good. At end of day, we will live or die by how good the service is.”

When I hear Schlein describe VC as a “service business”, I’m reminded of the airline industry. Experienced disruptors like Southwest and Virgin America have never really kept their secret sauce a secret. The airline’s co-founder Herb Kelleher spoke openly about how the Southwest team achieved operational excellence. Why wasn’t he worried about exposing his playbook to competitors? Like Schlein, he probably believed that a “service business” wins with world-class execution. It’s less about the creativity, and more about the commitment.

Investors could easily read and mimic Andreessen Horowitz’s strategy and model, but they can’t rip off the team’s execution. Along with transparency comes an obligation to execute flawlessly on openly shared ideas. And that’s a good thing.