Start-up funding: the key role of the finance department

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In this blog series, we are exploring the crucial role the finance department plays in enabling growth within scaling organisations.

Over the course of the series, we will be deep diving on key challenges, the ingredients for a successful finance department and tips for scaling the finance function.

The blogs in the series so far have covered:

- The key challenges and issues that growing companies face when trying to build, run and optimise their finance department.

- The key challenges every growing finance team faces and how to overcome them.

This blog will discuss the expectations from start-ups pre- and post-funding and the vital role the finance department plays in the effective realisation of these objectives and in the overall growth of the company.

A start-up's journey can be a rocky one, made more complicated by the various rounds of external funding that are necessary for growth.

Start-ups seek this funding from external investors to be able to fund their growth journey and it's typically raised through a series of investment rounds from friends, family and business angels at the beginning, and venture capitalists (VC) and private equity (PE) firms in later stages.

These rounds of funding become more onerous for the start-up as the invested capital increases.

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Generally, the VC funding stage is considered pivotal, as it's often the first major, professional round of funding, and indicates that a start-up shows true potential. Attracting interest from VCs and ultimately closing a funding round is a cause for celebration, however, this success also implies the start of a new chapter in the start-up's growth journey.

This chapter brings with it a whole raft of opportunities, but also higher expectations and the need for a step change in reporting on financials and KPIs.

It's therefore imperative the company's finance department is efficiently set up and prepared for scaling up.

Pre-funding: the expectations for a start-up in the run-up to a funding round

For a VC to decide whether to invest in a start-up, they require a wealth of information, including, but not limited to:

- Financial reports, analysis and schedules
- Due diligence supporting commercials/financials
- Future forecasts and plans
- Model projections
- Capitalisation tables
- Term sheets

It's clear to see a significant amount of time and effort is needed to produce these reports and documents, which often require multiple iterations.

The majority of the heavy lifting for these is done by the finance department, a function that is generally already understaffed and over-utilised. The finance department must therefore ensure it is prepared for these increases in demand by having (surge) capacity, skills and tools in place.

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Post-funding: the ongoing expectations for a start-up after a funding round

A common and often underestimated consequence of obtaining a significant investment is that the company must now operate according to more stringent standards, across a variety of dimensions, for example after completing a VC funding round start-ups are often subject to a strictly enforced Shareholder Agreement.

The Shareholder Agreement for professional investors is a lot more complex and difficult to navigate than a simple funding agreement usually used for friends, family and angel investors.

The professional / institutional investor Shareholder Agreement contractually guarantees the investor certain rights such as delivery of financial information, inspection rights, rights of first refusal and observer rights.

> "The Shareholder Agreement for professional investors is a lot more complex and difficult to navigate than a simple funding agreement..."

As part of the Shareholder Agreement, the start-up can be expected to provide the following financial information:

1. Historical annual, quarterly and monthly balance sheet, income and cash flow statements
2. Audited financial statements with year-on-year analysis
3. Capital structure schedule
4. Projections, year-on-year capital budgets and strategic plans
5. Comprehensive tax schedules
6. Schedules for assets, liabilities, expenses and equity

Whilst a start-up does not need a large finance department and a dedicated CFO during the pre-funding stages, the need for a scaled, connected finance team can quickly materialise after funding and once revenue is growing.

An underdeveloped and understaffed finance department could result in a start-up's inability to deliver the aforementioned requirements, thus potentially hindering future growth.

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The challenges and possible solutions VCs see in scaling finance departments at start-ups

Following discussions with technology-focused VC firms, we discovered that an often-underdeveloped area of a start-up is its finance function.

The lack of capability and capacity within the finance department usually comes to light during the pre-funding

due diligence phase, which tends to result in delays in the production of accurate financial data, financial statements and schedules – both forward-facing and historical. This can significantly delay the investment process, and in some cases, lead to its termination.

A start-up's finance department must therefore be prepared for growth.

However, there are certain challenges to growing and expanding this critical function; these challenges relate to leadership, people, and technology. Finding a strong leadership figure (CFO or finance director) with relevant experience is burdensome.

In summary

To conclude, the aforementioned challenges can often be addressed by ensuring that an investment in the finance function (specifically in leadership, people and technology) is made early enough in the company's journey.

This investment should translate into the recruitment of the right profiles and the implementation of adequate and future-proofed systems, processes, and controls. Leveraging a managed service provider to reach these objectives can also enable a company to set up for success and prepare itself for the challenges that arise pre- and post-funding, with a relatively limited budget.

Addressing these challenges will enable the function to set itself up for future success and will save significant costs and time in the long run.

About us

Be | Shaping the Future UK (**Be UK**) is a subsidiary of Be | Shaping the Future, a well-established management and technology consultancy with over 1,900 consultants located across 13 European countries.

We work with the leading financial services organisations to shape their future through our transformation consultancy and advisory services, covering the following sectors:

• Finance
• Cards and payments
• Retail and commercial banking
• Capital markets
• Risk, regulatory and compliance

We take pride in building relationships with our clients and we work collaboratively to drive change for a bigger and better future.

The Finance & CFO Advisory team at **Be UK** is composed of specialists and advisors. Our key service areas include:

• Making finance digital
• Finance data
• Strategic cost reduction

Our **Finance in a Box** service can provide start-ups with a team of finance experts (both in-house and through our offshore managed service provider) to build, run and / or optimise its finance department.

Contact

For more information on how we can help with your ESG, climate and risk initiatives, please get in touch.

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Bash drives change and innovation on behalf of CFOs and senior management across the financial services industry. As a qualified chartered accountant, half of his career has been spent working in the CFO / COO / financial control / product control space. The other half of Bash's career has been spent as a management consultant delivering large-scale strategic, regulatory and transformation programmes for multinational investment banks.

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