The Pros and Cons of Different Angel Investment Vehicles

Angels are the Indy 500 racers of the investment world. When great investment opportunities arise, they're the first at the finish line. And like any great racer, a crucial part of the process is choosing the right vehicle. Before you write your first check as an angel investor, you need to decide which investment vehicle will work best for you, as each one has different features and advantages.

Here we will discuss the four most common vehicles investors use, weighing the pros and cons of each so that you can make the most informed decision possible.

Personal Investment:

The most straightforward means of investing is through a direct personal investment. This is the Mercedes AMG of investment vehicles--expensive, but high touch. To make this kind of investment, you meet with the company, sign the purchase agreement, and wire money. Once the company receives your funds, they will counter-sign the purchase agreement and send you a copy. Done!

Personal investments are made through a brokerage or bank account, and it is the most common way for investors to invest. Quick to complete, personal investments have the fewest hassles. That means dealing with fewer investment institutions, fewer forms, and shorter wait times compared to partnerships, trusts, and IRAs (more on these shortly).

However, direct investments usually mean a high minimum investment to participate, which can be an intimidating prospect for beginning investors. Typically the minimums are in the range of $25,000 per check. Implication: to build a diversified portfolio, you will have to shell out a lot of cash! You will also have to manage all of the paperwork and communication with the startup, so if you choose this option, be prepared to be proactive in terms of engaging with the management team.

Syndicates:

Like Tesla's vision of making the electric car a reality for all, syndicates make angel investing accessible for more people. Steadily gaining popularity in the investment world, syndicates lower the minimum investment required from $25,000 to as low as $3,000, allowing you to spread your money over a broad range of startups and thus create a more diverse investment portfolio. Being part of a syndicate also makes it easier for you to participate in future rounds since syndicates often negotiate what is called pro-rata investment rights, which give an investor in a company the right to take part in subsequent rounds of funding.

Propel(x) is a big proponent of this approach and all of the investments on our platform are made through syndicates because it makes angel investing easier and more accessible to investors giving them the same power as larger investors by pooling resources.

Syndicates work differently on different platforms and you should make sure you are aware of the fee structure. Check to see if the syndicate charges an annual management fee and be clear on how much. While Propel(x) does not charge an annual management fee other syndicate management fees can range from 10%-15% one time, upfront. Also, be aware that syndicates also charge a carried interest or a "carry." A carry is a share of the profit of an investment that is paid to the managers of the investment once the startup has a successful exit. Carries can be up to 30%. Propel(x) charges 15%.

Here's a basic example of how a carry works. If you've invested $10,000 in a startup when it had a valuation of $1M (you own 1%) and they have an exit at a $10M valuation your $10,000 investment would now be worth $100,000! This is assuming there were no subsequent funding rounds. This means that you have a profit of $90,000 ($100,000 payout - $10,000 initial investment). In a Propel(x) syndicate you would pay a 15% carry on this $90,000 in profit or $13,500. So Propel(x) would get the distributed cash from the acquirer (or startup), subtract its share of carry and return the rest to investors.

Partnership:

Other investors choose to invest through a partnership. This means you're buying your car with a co-signer. A partnership allows for another level of liability protection. It also opens up the possibility of shifting tax gains and losses to the different parties in the partnership. This can be a useful tool for offsetting gains and losses from other capital investments. However, a partnership can take time to build, and it is easier to use as an investment vehicle if it is already established ahead of time. Again, if you take this approach you'll need to invest the minimum set by the company, which often starts at $10K - $25K depending on the type of startup.

Trusts:

Next is a trust; this is the prized roadster passed down from one generation to the next, hopefully with the brakes and steering intact. Trusts are often used for investments and allow for one generation to protect, control, and pass assets to future generations without invoking the estate tax - a big advantage for high net worth investors. Making an investment through a trust is similar to making a personal investment; but this can take time if the trust is not set up ahead of time. Many of our investors on Propel(x) invest via their trusts. The only difference in the investment process is that the trust is the purchaser and you invest as an entity (vs. as an individual).

IRA:

Lastly is the once rare, but now increasingly common method of using an IRA. The standard benefits of IRAs also apply when they're used to invest in startups. Gains are tax-free until withdrawn, allowing for compounding interest without capital gains taxation (Roth IRAs are currently tax free even when withdrawing). However, using an IRA to invest in a small company or startup often takes a lot of time and effort, and the brokerage fees can be quite high. Most large brokerage houses will not allow investments in startups through an IRA, and the IRA must be transferred to a smaller company that will allow the investment to be made. At Propel(x) we work with various IRA providers to help you make an investment via

Depending on your personal preferences, any one of these methods may be the right investment vehicle for you. But as with any vehicular purchase, we suggest getting some insurance by means of doing your own research before making a final decision and diversifying!

To see companies that are currently fundraising on Propel(x), sign-up free here.

Stay tuned for our next installment, Building a Diversified Startup Portfolio.

(Disclaimer: Each of these options involves complex tax implications. It involves some interpretation and should by no means be considered tax advice. You should always consult a CPA before making a major investment decision.)