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HOUSTON'S BUSINESS SOURCE

VENTURE CAPITAL

CARL NORTON:
MBA, J.D., CPA,
and Maverick

DR. "RED" DUKE:
Character and
Charisma

RESTAURANTS:
The Challenge
of Concept
and Function

Why is this Houston attorney raising the eyebrows of his legal brethren?



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Carl L. Norton is an

extraordinary man. Packing three degrees into his briefcase in the time it takes some to obtain one, Norton has risen to the pinnacle of the legal profession with the same level of energy. Norton's intensity is so evident, it takes on nearly a physical presence in a room.

Described as a "lawyer, accountant, business advisor and quasi-investment banker," Carl Norton wears any number of hats throughout the day. In the process of wearing those hats as managing partner of the growing Houston-based law firm Norton & Blair, he might well be redefining boundaries for legal practitioners in the 1990s.

CARL

How is this Houston attorney raising the eyebrows of his legal brethren? Let me count the ways.

NORTON

BY SCOTT EDWARDS
PHOTOGRAPHY BY TERRY BLACKBURN





“Norton & Blair is attempting to redefine the term ‘major’ law firm. Expanding our services and offering contingency fee arrangements, instead of having a large number of attorneys is a major way for us to compete with the name brands of the legal industry.”



By being involved in an array of corporate finance transactions and offering clients contingency fee arrangements for acquisitions and financings, N&B has rapidly gained the interest of the corporate and venture capital community while raising the eyebrows of their legal brethren.

A Houston resident for the past 17



years, Norton is a former CPA (obtaining the third highest score in the nation on his CPA exam) with roots in Philadelphia and Wall Street who holds both M.B.A. and J.D. degrees. At first blush, one might consider that Norton possesses a curious inclination for the strict regimens and ivory-towered meditations of academia. Instead, Norton is



guiding the members of the firm’s corporate/securities department in pioneering the expansion of the traditional services offered by a corporate legal practice—and he’s found time to become a leading figure in the venture capital industry. The requirements? A vision capable of alternative solutions. Norton is, in fact, an unorthodox, creative innovator.

FUTURE TRENDS: EXPANDED SERVICES, FLEXIBLE FEES.

William Cobb, president of the legal consulting firm, WCCI, Inc., which consults in 55 metropolitan areas, finds Norton’s practice atypical of

THE VENTURE CAPITAL OVERVIEW

Houston venture capitalists are smiling all the way to the “deal” as access to capital remains a difficult path for many companies to cross. As a result, opportunities in venture capital are changing in Houston. Long considered a “risky” source of investment reserved for high-tech deals or start-up companies, venture capital is gaining new respect as a means of funding companies’ financial needs.

Representing both entrepreneurs and venture capitalists, Carl Norton is one man who finds himself in the middle of an increasing number of these deals. In fact, while Norton races from meeting to meeting, he has cultivated a theory that explains the smiles recently seen on venture capitalists’ faces. He calls it the “financing ladder” theory.

Norton, who serves as managing partner of the mid-sized Houston law firm Norton & Blair, describes it this way: “Deals that were traditionally financed through banks - those deals on the commercial bank ‘ladder’ - are being turned away by an extremely conservative lending environment and are now moving over to the top of the venture capital ‘ladder.’ As a result, the quality of venture capital deals has improved dramatically - as have the numbers. In the meantime, deals at the top of the venture capital ladder move down a notch and knock riskier ventures to the bottom rung,” Norton says.

Much of this phenomenon results from the slowdown of deals that are financed through traditional sources - banks, insurance companies and Wall Street. Most companies have traditionally turned to bankers for their financial needs, but commercial lending is at its most conservative stage in years. In fact, Texas banks have made pro-

gressively fewer loans in the last several years. Figures provided by the FDIC show that the amount of commercial and industrial loans has declined from \$35 billion in 1987 to \$25 billion last year.

Team Bank’s Kathy Gamel says the criteria used by most banks to review loans differs from how venture capitalists view deals.

“Banks are much more numbers oriented and the regulatory environment has made it more difficult for banks to loan to start-ups,” says Gamel. “Banks want balance sheets and a three-year history to review. Venture capitalists are more lenient in terms of considering a company’s product or market. Banks want to see marketable collateral rather than assets because a start-up company has no track record.”

Companies that utilize Wall Street as a means of financing are also experiencing their own difficulties. Investment banker Floyd Lankford of Alex



today's corporate practice.

"When someone goes into a deal with him, the greatest distinction is that N&B assumes risk," says Cobb. "Norton's practice fits the client's value system better. Value is added by getting the deal done. If you're not adding value, the client will wonder why you're involved."

Norton believes that offering expanded services and alternative fee arrangements, normally the province of litigators, is a step into the industry's future.

"Norton & Blair is attempting to redefine the term 'major' law firm. Expanding our services and offering contingency fee arrangements, instead of having a large number of attorneys is

a major way for us to compete with the name brands of the legal industry," says Norton. "It's the value added that counts. We sit down and structure a client's deal as opposed to coming in late in the game and just papering it up. The contingency fee arrangement conveys to a client the fact that we are willing to take a risk with him. That makes



us different," Norton concludes.

John Christman, president of Whitestone Products, Inc., a New Jersey-based manufacturer of disposable products, found the contingency fee attractive and Norton's background essential to the \$25 million acquisition of a NYSE company he and Norton engineered. "Carl counseled us beyond



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Brown & Sons in Baltimore regularly visits Houston to review potential deals. "A year ago, the market was seeing a number of initial public offerings designed to raise money for growing companies. Then the Middle East situation hit, oil prices went up, business indicators went down, banks weren't loaning money and the initial supply of public offerings was all but cut off," Lankford remarks.

Norton echoes Lankford's perspective. "Between the war, the banking crisis, the reality of the 'R' word (recession) and the disappearance of junk bonds, the number of public offerings has significantly decreased in the last six to eight months and cut off a source of funds for growing companies. The question becomes one of where a company can find capital," Norton says.

So where are some of the country's estimated six million privately owned companies finding the capital to start-up or expand their businesses?

At least part of the solution is found in venture capital, says Phillip Tuttle of Davis Venture Partners in Houston. "The market forces are at work. Companies are not able to go out and raise capital through traditional sources. Therefore, there are more mature companies involved with venture capital," Tuttle believes. "The track records of these companies are strong. We recently closed a \$6.5 million deal that would have been funded through a bank in the 1980s. Access to the public market all but shut down last year," says Tuttle.

While companies chase their entrepreneurial dreams, the "financing ladder" phenomenon also bolsters the positioning of venture capital funds. "I've seen a significant increase in our venture capital practice," Norton says. "We're doing more deals and our clients are receiving more favorable terms because of the low supply of available dollars from traditional sources. For example, we just repre-

sented a venture capitalist who completed a transaction that a bank would have funded just a year ago."

Norton says that companies are even operating as venture capitalists to attain their financing goals. "The shortage of traditional financing is so noticeable that many companies are operating as venture capitalists. These companies are investing in start-ups and conducting buyouts in their own industry because others can't get the banks to provide equity or loans," Norton remarks.

One of Norton & Blair's clients, Serv-Tech, Inc., a publicly traded Houston-based industrial service and specialized maintenance company, illustrates how companies accomplish this.

"Serv-Tech has recently invested in industry partners to fill the void left by banks. By providing debt and equity financing and taking minority interests in industry related start-ups and existing companies, they build their

the scope of our expectations," says Christman. "He was in the trenches from the very start and structured the deal to the end. Without his guidance, we wouldn't have completed it."

Christman believes that Norton's knowledge of accounting and finance created a distinction from the opposing counsel. "Carl's understanding of the accounting and financial worlds gave us a distinct comfort level at the negotiating table. There was a definite irony in the fact that a major New York law firm simply couldn't keep up with his performance."

A contingency fee arrangement was agreed to between Christman and N&B in which N&B would write off a substantial amount of fees if the transaction failed, or mark up fees if it succeeded. "That's how N&B will assume risk. If the transaction is successful, the firm will also reap the fruits of the client's success," says Cobb.

A MULTI-DISCIPLINED APPROACH

"There are a number of \$10 million to \$100 million revenue companies out there with in-house counsel, but who still need expertise on complicated

financial transactions. I think I foresaw a need for someone like myself who brings a number of disciplines to the table," says the energetic Norton.

"That's when I became interested in representing venture capitalists. I thought my background in accounting, finance and law would offer an attractive commodity to these growth companies."

In late 1982, Norton began courting the venture capital market in Houston. "I sensed that there were quite a few attorneys who didn't understand corporate finance to their client's satisfaction. That still appears to be true too often," said Norton.

Interestingly, Norton offers this comment while the number of Houston area attorneys continues to mushroom. According to the Houston Bar Association, more than 13,000 attorneys practice in Harris County alone. Now with more mergers occurring with out-of-town and out-of-state firms, and more companies expanding their in-house counsel, law firms competitively vie for business.

"My approach differs from the traditional corporate practice in that I'll often be involved in selection of target

companies in acquisitions, due diligence investigations, search for additional capital, and structuring the terms of a deal. Most corporate lawyers don't get involved to this degree."

This strategy is apparently paying off.

Fred Zeidman, president of Houston-based Enterprise Capital, a venture capital company and a leading venture capitalist says, "The seeds have been planted for somewhat of an explosion in Houston's venture capital market in the 1990s. We have a good labor supply, good distribution reputation, a low cost of living, the Texas psyche...and probably no one in Houston has more venture capital work than Carl Norton. He went after the venture capital market in a very giving way in the early 1980s while others ignored it. Now, where there's a deal there's Carl," Zeidman adds.

Norton's practice has developed to the extent that his schedule is often filled with venture capitalists who previously witnessed him in action representing the other side of the deal.

"One of the great things about venture capital work is that it leads to other transactions — public offerings, private
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own operations and provide an opportunity for experienced entrepreneurs. The company is actually operating like a venture capitalist," Norton says.

With six-to-one returns on their investment, John Slack, vice president of finance for Serv-Tech, says the company is comfortable with the methodology and pleased with the results "We're very entrepreneurial and strongly believe in having vested interests in the industry. We're buying service companies - which is really buying people who have the ability to do deals and get the job done. We provide the financial expertise and don't typically get involved with the way they operate. It's a low-risk for us because we go in at a relatively low-level," Slack states.

Most of Houston's venture capital deals shadow the city's economic upswing, diversification and new jobs, says Norton. "Ten years ago, most of the city's venture capital deals were oriented around the energy industry.

Today, the deals involve air courier service companies, tile distributors, medical waste companies and even bicycle distributors."

As a Baltimore "foreigner," Alex Brown's Lankford finds the Texas psyche attractive. "Houston has always been a can-do city. Now, it's one of the few areas of the country doing relatively well. The city's economy has broadened and grown in its attractiveness to investors."

Norton, whose firm hosts a monthly venture capital breakfast, attracts speakers and guests from around the country as word spreads about Houston. In the last three months, speakers have come in from Stamford, Connecticut; Tampa, Florida; and Chicago.

Consensus? Optimism abounds... to a degree. Jim Kozlowski of AMEV Venture Management, a New Jersey-based subsidiary of a \$34 billion Dutch financial services company, was a recent attendee of one of the break-

fasts. Kozlowski thinks Houston's potential is strong but adds that 75 percent of the venture capital money still remains on the East and West coasts. "I'm a firm believer in the opportunities that exist in the Southwest and in Houston. A number of companies that were 'bankable' several years ago are now turning to the venture capital market. I'm now spending three to four days a month in Texas looking at opportunities," says Kozlowski.

While Houston is not a venture capital hotbed like Menola Park, California, the prospects of investment in the area have perhaps never been better as the city continues to buck the national economic slowdown. "Houston continues to rebound, diversify and grow," Tuttle says. "Whether you manage a U.S. pension fund or a European fund, now is the time to invest in Texas."

placements, commercial loans, real estate and even litigation," says Norton.

ENTREPRENEURIAL RESTLESSNESS

Norton has a penchant for doing things differently. "I often do things differently or more aggressively, but that's what makes Houston a great place to do business," explains the 48 year old managing partner who still sets the pace at the office with twelve hour days, six days a week. That philosophy has also helped N&B grow from a small law firm founded in 1982 to a mid-sized innovator with offices in Houston and Austin.

"The firm tries to look for different and better ways to consummate transactions. We try to think in terms of what a client's needs are and how to remain cost-efficient in satisfying those needs," Norton says.

Transactions aside, he organized the "Venture Capital Breakfast Group" five years ago with Ernst & Young, an international accounting firm. These meetings were organized to introduce out-of-state venture capitalists to their local counterparts and assist in creating a greater flow of deals. National firms such as Clayton & Dubilier, Morgan Stanley Venture Capital Fund and Alex. Brown & Sons have presented their strategies at the breakfasts.

Norton has also made a habit of forwarding parts of business plans to financing sources domestically and abroad without expecting a fee — an unheard of practice among many traditional attorneys. But then, what would you expect from a man like Carl Norton?

"I'm not a genius," he hesitates, "but it's not genius that does it. It's working harder and longer. That's what I do, work harder and longer and think in terms of meeting client needs." Norton's eyes project intensity as he adds, "The busiest people get the best work. It's that simple." We at dba feel that highly-motivated genius is probably closer to an accurate description of Carl Norton.

