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Playing Chicken

Once again, Craig, Rex, and Dean found themselves seated around the old maple table. It had moved. Our new offices were just north of town in a group of five office buildings collectively called Hollymead.

What the three had before them was unbelievable. The final tally from the private funding round showed that not only had we moved back a safe distance from the edge of the abyss, we had actually brought in more cash than we had hoped to raise during the failed IPO. Putting the achievement in perspective, Dean pointed out that we had raised more private equity capital than any dot-com ever—this was one for the record books.

As the three men formally closed the funding round, setting the stage for a new run at an IPO, they reviewed the last few months like a tailback reviewing the instant replay of his ninety-five-yard touchdown run. They felt proud, exhausted, exhilarated, and motivated, all at the same time. They were victorious, for the moment, but the game was far from over.

It had not been easy. As far back as Christmas Eve, the Paul Allen investment, a gargantuan $50 million influx of capital, had looked imminent. Then Rafe Durn and Frank Flowers had squabbled over who would have what preemptive rights, and they had demanded warrants to sweeten the deal in the event Value America failed to attain a public market valuation of at least $600 million during 1999. What had happened to the good old days, just a short time back, when a $300 million valuation had seemed wildly optimistic?

The problems had been ironed out, finally, and the money had at last begun to flow into Value America's coffers, and not just from Paul Allen. Fred Smith and Federal Express had each contributed $5 million. Global Crossing's founders, Rafe Durn's friends Don Tarpin and Gary Winnick, invested $10 million. And the employees and friends of the company had given millions more. It was immensely gratifying because all of the "loans" made in the first sixty days after the failed IPO had been voluntarily converted to equity. The folks who knew us best believed in us.

The world was finally starting to take notice. Retail Week had proclaimed that Value America was one of the world's most innovative retailers….

Tucked in a lush pocket of country where east coast bustle fades into quiet green hills, Craig Winn has assembled an Internet company whose chief strategists profess no special love for the Web. Hundreds of miles north, in New York, or a continent away in California, entrepreneurs run themselves ragged trying to wring money from the ether-world. Though it's a simpler pace of life in Charlottesville, executives at Value America, too, burn their days in double time. Others talk of customer acquisition costs and focus-group findings, but the architects of Value America use a different vocabulary. They aspire to nothing less than building the world's next retail revolution….

It is Winn's enthusiasm that fuels his team's 12-hour shifts. "He appeals to my intellect," said Phil Ramsey, VP of Direct Response Marketing. A year ago, Ramsey was capping a successful consulting career. "Now I'm hooked," Ramsey said. Others followed Winn from California where he worked closely with the original Price Club team that pioneered the warehouse-store concept.

Ken Power, SVP and Creative Director, met Winn four years ago. He produces the folksy newspaper ads that make Value America the one Internet company able to make traditional marketing tactics work online. Power's copy and style extends into the company's Web store. Its logical layout, plain-English descriptions, and copious illustrations lend an approachable air.

"People never really buy anything until they trust someone," Ramsey said. "We want to make our mark doing what other retailers can't. We're a one-stop shop." An analyst at the IPO Monitor said, "You've got to take WalMart and put it on the Web." Or Price Club, as the case may be….

Richard Gerhardt, Value America's President of Consumer Products, and Price Club staffer at the time, said, "Winn convinced manufacturers they could eliminate costs by supplying Price Club with great products that could be sold to consumers at a low overhead. This same model persists at Value America today." The firm takes possession of inventory only while it's en route to customers. Manufacturers coordinate the deliveries. In return, brands pay fees for online listings and multimedia product presentations. "This was a unique opportunity for us," said Chuck Gangi, Sales Manager for Targus. "They're unlike any other Internet retailer. With Value America, we're all part of the same team."

"Retail is in need of repair," Winn said earlier this year. "Almost every manufacturer of consequence views their retail customers as their enemy." Value America is Winn's bid to flip-flop the retail channel, selling the best quality merchandise in the store with the lowest overhead.

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As We continued our quest for dot-com's holy grail, the initial public offering, our due diligence efforts proceeded apace. The investment bankers, lawyers, and auditors had been busy collecting risk factors. Generally, we didn't mind, because they were like cheap insurance—"You can't say you weren't warned." But this was getting silly. They seemed to be writing risk factors on everything they could think of, real or imagined. It got to the point where some of the risk factors were simply untrue.

Bill Hunt had found himself at the epicenter of one risk factor controversy that irked Craig no end. Bill had addressed a group of footwear and stocking manufacturers, and during the course of his speech he had made what appeared to be a "forward-looking statement"—a bad thing, the lawyers had declared, according to their view of SEC regulations.

In reality, all Bill had done was say we were filing a registration statement (correct), and that we had grown faster than the Web itself (correct again). He referenced a recent USA Today article that said Internet use was doubling every ninety days. Our first IPO's red herring had proclaimed that we were tripling every ninety days. Unfortunately, his speech was picked up and reported in the Dow Jones News. So the lawyers accused him of hyping the stock.

He had done no such thing. The SEC ruled that it was perfectly proper to share positive new developments with business partners like Bill's hosiery brands. In fact, to refrain from doing so would have constituted a breach of fiduciary duty to our investors: one was expected to "sell" one's company to potential allies. They even had a term for the acceptable behavior: "puffery." Being of a business mind, the SEC knows nothing happens until somebody sells something. Our lawyers didn't care. They crafted a risk factor that maligned the truth and embarrassed Bill.

Companies are strongly discouraged from hyping their public offerings in the media, especially in the days leading up to an IPO. An overly favorable or inaccurate newspaper or magazine article can derail a stock offering before it gets started. The technical term for the offense is "gun jumping." The SEC wants the company's merits to be judged strictly upon what was published in the S1, red herring, and prospectus—a devilishly hard thing for us to achieve, considering we were up to our ears in the information age. This was why the February issue of Chief Executive magazine caused such a stir.

Chief Executive didn't have a very large circulation, only 30,000 or so. You couldn't even walk up to a newsstand and buy a copy. You had to be a mover or shaker in the business world, a top executive of a large corporation, to get it. Naturally, when Craig told the lawyers about the impending article, their here-comes-trouble meters pegged.

Craig insisted that the article had not been written to support the upcoming IPO. In fact, he had been having discussions with Arnold Pollard, the Chief Executive of Chief Executive, since the previous April. Arnie was intrigued with Craig and the company he had founded. They had become good friends by this time. But it wasn't until Pollard's staff asked if they could come and take a few photographs that Craig knew that they were planning an important story. At Pollard's suggestion, the photographs were taken in Craig's elegant home, with his wife and his dog.

He figured he dare not wait until the issue was actually published to find out if it were accurate and devoid of hype. He asked Arnie to let him preview the text. "I won't ask you to change anything editorially," he said, "but a misstatement could sink our IPO."

"The piece is going to press in twenty-four hours, Craig," Arnie said. "It's going to be our February cover story, the first time we've ever devoted our cover to such a young firm. So, if we've gotten the facts wrong, we'll make corrections. Otherwise…."

The story was spectacular. Its tone was so positive, Craig's pulse raced as he devoured every word. Based upon his experience with the media, he just knew there had to be a time bomb ticking away in there somewhere, but he couldn't find it. The story was provocative and entertaining, yet truthful.

The magazine went to press as written, and all hell broke loose. The story at first blush made Value America look too good to be true—inspired leadership, revolutionary business plan, bright prospects, friends in high places. Underwriters' counsel demanded that the IPO be pulled. This had to be hype, they charged. But closer examination revealed what Craig already knew—the story was precisely accurate, verifiable, and totally consistent with the statements contained in the S1. There was no hype, no forward-looking statements, nothing at which to point an accusing finger. The lawyers didn't care. They wanted blood. The story at the heart of the controversy said, in part:

At first glance, the story sounds familiar: a young, energetic, tech-savvy entrepreneur starts up a company on a wing and a prayer, with a fascinating premise and a dream of becoming the next Gates. The company chugs along, announcing strategic alliances and releasing new products until it either secures a place as leader of a niche—or fades off quietly into cyber-oblivion. But if you think you've heard Value America's story before, you may want to think again; this online retailing company isn't just another Internet.com. After all, it isn't every day the CEO of an e-commerce start-up secures some $120 million in private placement from some of the world's most noteworthy investors.

Some of those who now own pieces of Value America (which has also just filed with the SEC to go public with 5 million shares of common stock): FDX's Fred Smith (he and his company are in for $5 million each), Microsoft co-founder Paul Allen (he has a total of $65 million invested through his company, Vulcan Ventures), Gary Winnick, CEO of Pacific Capital Partners and co-chairman of Global Crossing, Don Tarpin, co-chairman of Global Crossing, and the respective principles of both the Carlyle Group and CIBC/Oppenheimer. Organized labor, oddly enough, has invested a total exceeding $20 million. And all of this was accomplished without help from investment bankers. That means no fees to pay out—which, in turn, means a whole lot of cash to play with.

Not that Winn will have trouble finding ways to spend it; competing for share of the online wallet requires constant reinventing, developing, and evolving. The virtual retail world is a space in which all is new—or at least most things are. In fact, Winn's company is built on a business plan he wrote some 20 years ago. Back then, Winn was working as a representative helping retailing legend Sol Price. Winn's job was to convince brands to partner with Price, but it wasn't an easy sell.

To increase the vendors' comfort level, Winn explained that retailing had historically undergone periodic revolutions, that the Price Club represented the latest of such shifts, and that they shouldn't miss out on being part of it. It was a reasonably effective pitch, but some brands wanted to know more. "They said, 'If you're so smart, tell us about the next retail revolution,'" recalls Winn. He painted a futuristic picture of multimedia product presentations and direct shipments from manufacturers that eliminated the need for inventory sitting on retailers' shelves. And he liked what he heard himself saying. "I decided that while this idea was fresh, I might as well write the business plan."

The missing ingredient was the technology that would make it possible. So Winn worked as a manufacturers rep, and then founded Dynasty, a lighting manufacturer that he eventually sold. In the meantime, PCs proliferated and the Web arrived, making Winn's old business plan feasible. In 1996, he and partner Rex Scatena incorporated Value America, and since have been working to revolutionize retail.

But so, too, have thousands of other companies that have taken to the Web. Entrepreneurs are trying out new business models to see what will make money in the new and rapidly evolving medium. Winn's vision, then, is just one of many vying for the attention of customers and investors. But his approach is one of relentless logic, methodically ticking off point after point, while tempering his arguments with considerable personal charm and enthusiasm. In short, he makes a powerful pitch—one that has convinced a large number of high-profile backers of his model's merits. So impressed was Fred Smith, in fact, that he will serve on Value America's board—his only other board besides that of his own company.

Winn says that the Value America business model stands out from the Internet crowd because of a handful of key factors starting with scale. Rather than one or two types of products, the company offers goods from more than 1,000 brands in 20 industries—everything from computers and jewelry to coffee and Post-it notes.

Another critical element of the model is an emphasis on well-known brands, such as Panasonic, HP, Amana, and GE. Winn says that the trust engendered by such brands is important in a medium where people can't touch the merchandise, and where a lingering suspicion of Internet security and legitimacy keeps many from buying on-line. To support the sale of branded, higher-end goods, Value America gives customers a wealth of product information in the form of multimedia presentations that describe features and strengths in detail.

Value America has also bucked Net tradition in its approach to advertising. The company has focused heavily on traditional vehicles, such as newspapers. The company's ads, which are often humorous, are created by an in-house advertising staff. "It's our biggest expense area, so it better be a core competency, right?" says Winn. "That's especially true if you want to have a unique voice."

Value America is based on an "inventory-less" model. The company is essentially a conduit between consumer and manufacturer; it has no warehouses, and owns products only while they are on their way to consumers. The company has created sophisticated systems that will seamlessly take orders online and pass them electronically to the brands. The result, he says, is "what we believe to be the first totally electronic and automated link between supply and demand.

"We are in the business of creating friction-free capitalism," he adds. While the most efficient retailers operate at 18-to-22 percent total overhead as a percentage of revenue, he says, "We have designed Value America to run ultimately at 5 percent." The approach, he adds, is "very much like being a bank. A bank typically makes a 3 percent spread on your assets. We are margining other people's assets."

Such efficiencies, as well as the relationships Value America has with manufacturers, were key to attracting Paul Allen's Vulcan Ventures firm, says Vulcan president Frank Flowers. "It's clear to me that the challenge in on-line retailing is to keep your infrastructure costs as low as possible. Any time you can deliver customers directly to manufacturers and allow the manufacturers to ship products to customers directly; you have eliminated a significant amount of risk from the business model. So the appeal of the Value America story is its finely tuned back end, as much as anything else."

In the following interview, Winn talks with CE about the merits of Value America's business model, and the travails of creating a business on the Internet.

Q. Why is having a broad range of products so important to your business model?

A. We're convinced the consumer isn't going to learn to navigate and bookmark hundreds of sites or share personal and financial information on a wide scale. So we're comprehensive. Most everything you need for home or work can be found in one place. The other reason is the stunning amount of capital that is necessary to build a brand in e-commerce. If you're applying those promotional dollars to a single category, it would be difficult to ever be profitable.

Q. That approach means you've had to establish relationships with a great many manufacturers. Has that been difficult?

A. It's the hardest thing we do. Every brand relationship started with a "no." Some told us no many times. Because we are selling the best brands, they have the most to lose. They risk alienating their existing distribution channel or losing the lead position with our new emerging channel. So to have gone from over 1,000 noes to 1,000 yeses is pretty remarkable.

Q. Your focus on traditional advertising vehicles was unusual for a Web-based company. What was your reasoning?

A. E-commerce revenues had been driven through fixed-cost agreements with portals that provided a “click here” button. We believed that the same amount of dollars spent in traditional advertising would drive more revenue. It could create a whole new voice, a new image if the advertising was as information-rich and brand-centric as the store. That’s impossible with a “click here” button.

Q. How will Value America evolve—and what are some possibilities for expansion?

A. We can create custom stores in almost any way that you can slice the people and products. For example, there are about 1,000 major charities in the U.S., and one of our strategies is to form alliances with them. Our biggest budget item is advertising. With these custom stores, we eliminate that cost.

Q. Are you troubled by the fact that PC penetration seems to be stalled at 40%?

A. No. We began Value America only when I became convinced that convergence was going to become a reality. TV and phone penetration are in the 99th percentile.

Q. What happens when somebody else says they think they can do this better?

A. I say, “Come on down!” Every day is a battle. And thank God the challenges are enormous. Otherwise, any idiot could do this. If I knew when I started this company what I know now, I never would have done it. I’ve spent 25 years preparing to do specifically what we’re doing. I understand manufacturers and how to build relationships with them. I understand and love technology. I’ve been the middleman between manufacturer and retailer. And even with all of that—and hiring the brightest team of people and having backers with deep pockets—this is awesomely difficult.

Q. Have you found leading an Internet company to be different from leading a more traditional organization?

A. Yes. The biggest difference is the enormity of the dollars required to promote it. I have spent 90 percent of my time raising capital. Yes, there is a lot of capital available, but there are tens of thousands of people with wonderful ideas chasing it. Second, everything you do, you have to build yourself. Typically, when you start a business, the one thing you don’t have to worry about is financial and accounting systems. But there is no accounting system you can buy for an e-commerce inventory-less model. You have to build it. And, this is the one space where patience is not rewarded. You have to be willing to go out to sea and fire your guns while you are still laying the keel. It’s an environment where you must constantly be aggressive, where time moves in dog years.

Q. How did you manage to land Fred Smith?

A. Actually, Fred Smith—who I view as the Babe Ruth of business, a real world-class entrepreneur—called me out of the blue and left a voicemail saying, “I have been studying Value America and it is my opinion that it is the best business model I have ever seen.” Now, in my opinion the best business model is Federal Express. So to have Fred Smith call and say that—that’s some pretty powerful stuff.”

In the end, after several days of intense investigation, the underwriter’s attorneys couldn’t find a single inaccurate nuance. The Chief Executive cover story remains the definitive published account of Value America.

To be helpful, Craig encouraged the lawyers to diminish their perceived liability by writing another risk factor. It seemed to work for everything else. He even offered to write it himself with a little help from Caise. In carefully worded legalese, they "asked" investors to ignore the February cover story. They warned that even though the article mentioned that Fred Smith and Paul Allen, founders of two of the world's largest and most innovative companies, had invested in Value America, this "should not be construed as an endorsement of our company." How these investments should be characterized, if not an endorsement, was left to the imagination of the reader.

What is perhaps most amazing, however, is that within a year's time so much would change at Value America, and within the dot-com world, that another business periodical would actually reuse the photographs of Craig found in the Chief Executive story without his permission to create an entirely different and false characterization. But more on that later.

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a thousand brands and counting; we were not the same store we had been even six months before. We had more departments, and more depth within each department. The store layout that had served us well when we had fewer brands had begun to show the strain. So we hired a talented young Web designer as the new Creative Director for the store. I no longer had the time for such indulgences. My ad team and I were too busy composing ads for what had become one of the world's largest dot-com ad campaigns.

Interestingly, Paul Allen's only point of disagreement with our store in those heady days was the look of our homepage. He preferred what had become the standard approach, with links to everything under the sun arranged under tabs. We resisted this look, because it tended to look cluttered, confusing, and frankly, cheap. But there was far too much content in the store now for our old ultra-clean look. The compromise featured a gateway to each department, arranged in a checkerboard pattern of icons. It was handsome and scalable: as we added departments, we simply added more icons. Other key navigation and shopping features were handled neatly around the edges.

Glenda Dorchak, who considered herself to be in charge of everything, was proud as a peacock. Never mind that until the new designer started working with Craig her plan had been a catastrophe. She had tried to remake the store in her image: cold and clinical. Graphic suicide.

The compromise, however, failed in subtle ways, easy to miss. In some places, we lost ground. Craig noticed the shift, but few others did. Unfortunately, he was too busy closing the private equity rounds and reenergizing the IPO to steer the new creative team around all the inherent deficiencies in their new format.

So in the push to become more streamlined, the store ceased being polite: the page where we thanked customers for their last purchase and gave them the opportunity to comment was gone. We ceased being caring: the blue "genie," our visual metaphor for in-store help, was gone, as was my good-natured tutorial. The rich repository of information about the hows and whys of the store was jettisoned—it didn't fit the new, more clinical style. We ceased being fun: all the humor was sucked out of our presentations. We ceased being helpful: our thoughtful, well-reasoned explanations were gone, replaced with regurgitated ad patter. Craig was sick about it, but he couldn't put Humpty Dumpty back together again, not without shooting down all the queen's horses and all the queen's men.

One change was not so subtle, nor were its negative implications. From day one, our product presentations had been central to attracting brands, achieving factory authorization, and forming brand partnerships. When a shopper entered a product category, their shopping experience started with the presentation and then moved on to the purchasing panel (a page that was never more than one click away). Glenda, however, could see no value in the presentations, so she changed the order and made them an option. A tiny eyeglass icon led shoppers to them, but it was easy to miss, and easier still to ignore.

Even if Glenda didn't understand brand dynamics, the brands did. Almost immediately, the flow of capital from brand partners slowed to a trickle, magically transforming our corporate gold mine into an expensive white elephant. If Glenda had finished high school, she probably would have learned that every action has an equal and opposite reaction. Before the store was even open for business, Rex, Bill, and Craig had brought in many times more presentation revenue (at eighty percent gross margin) than General Dorchak's whole ill-managed army of merchants ever did.

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"I've got a bad feeling, Rex." Craig was slumped in a chair, rubbing his forehead and contemplating the impending IPO. "You know how we missed the summer window—the party was over before we showed up. Well, sure as shootin', we're heading directly into another round of dot-com jitters."

"You may be right. But, on the bright side, it looks like we did nineteen million in sales in Q4, a gain of four million over Q3, despite the fact we were too broke to advertise. The Series C round is finally closed, and we raised something like seventy-five million. The auditors are almost done screwing around, and we're about to re-file our S1 with the SEC. Unless something really bad happens, we'll be out there in four or five weeks. Think positive, Craig," Rex said brightly. "No more glitches."

Craig rose and smiled hopefully. "No more glitches."

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Dean looked pale as a ghost. He grabbed Rex as he passed his office. Entering Craig's, Dean turned and closed the door. Uh oh, Craig thought.

"What?" he asked, not really wanting to know.

"How much was the ad budget for Q4?" Dean asked rhetorically.

Craig didn't have to look it up. "Three million. Six if the funding came through."

"Try sixteen. Glenda's overspent her budget by ten million dollars."

"Are you sure?" Rex asked. Stupid question. Dean had been over the numbers a dozen times. There was no mistake.

"I don't believe it," Craig lied. "She just ignored the constraints? We were sinking, and she spent money like a drunken sailor?"

"Well," Rex offered, "that explains how we were able to do nineteen million. She burned sixteen mil doing it! Hell, I thought this was the one thing she was supposed to be good at."

"Piss-poor ratio, that's for sure," Craig spat out. "Where was she advertising? Bus benches? Magazines? Get her in here!"

"It's not true," a watery-eyed Glenda cried when Dean appraised her of the problem. "It can't be," she protested. "Sixteen million? No way. Your numbers are wrong." She didn't like Dean very much. The feeling was mutual. "I'll straighten this out," she announced.

You do that.

It was a surreal episode. The problem, for once in our lives, wasn't the money. We had enough to propel all but the most gluttonous into the stratosphere. It was now a question of integrity and the merits of our business. Our analyst's models for the coming year had been based on a logical progression from the previous quarter. To have torched $16 million against a budget of $6 million could lead investors to one of only two conclusions. Either we were lying scumbags, as FedEx's CFO had assumed, or we were unaware of what was happening in our own company, incompetent buffoons. Investors never factored in treachery.

When Glenda returned, she tried to downplay the disaster. At first she announced triumphantly that she had found a $100,000 error. Dean called her on it. All the records were reexamined. With nowhere to hide, she eventually admitted that $16 million had indeed been torched. Then, true to form, she proposed misallocating some of her overindulgence into Q1 as a way to repudiate responsibility. Unethical, if not illegal.

"No thank you," was Craig's response.

Dorchak was never willing to accept blame. When the inquisition was over, she stormed out of his office vowing to find the responsible party. A mirror, Craig thought, might be helpful.

Cornered, Glenda did what any red-blooded American girl would do (she's Canadian, but who's counting). She lashed out at the most convenient target, in this case the soft-spoken Derick Roberts, whose job it had been to place our ads in accordance with Glenda's directives. Derick, a seasoned advertising professional, had been doing precisely that ever since Phil Ramsey had been dismissed from the job for questioning the appropriateness of overpaying Business Week.

Derick was in his office chatting with Doug Purvis, our photographer, when Glenda walked in. Ignoring Doug, she told Derick, "Sometimes a lieutenant has to fall on his sword for his general," or words to that effect, and fired him summarily, claiming it had all been his fault. She then turned to Doug and cooed, "I understand it's your birthday." Without warning, she grabbed him by the cheeks and kissed him full on the lips.

She hadn't fooled anybody except the bewildered Roberts and the nearly neutered Purvis. Craig reinstated Derick to his original job, but neither man was ever the same. Both had sacrificially invested their time and money when we had needed it most, and had been kicked in the balls for their efforts. As a company, it was not our finest hour.

As the extent of the damage became clear, Dean angrily observed, "Our first IPO failed, and against incredible odds we've earned a second chance. But when the bankers find out about this, they're going to cancel the second one, sure as hell. We're dead men walking." He shook his head.

Craig looked up, wild eyed. "You're probably right, Dean. We're as good as dead—you can't cover up a ten million dollar mistake. But before they start throwing dirt on us, I've got one last idea. I don't know if it'll work, but we might as well go down fighting."

“Well, whatever you do, the funeral starts in two hours,” Dean replied. “That’s when the conference call with Dale Dandridge is scheduled. We’re supposed to go over our IPO model—you know, the one that doesn’t make sense any more. We need a miracle. Again.”

Alone in his office, Craig reflected it’s not about history. It’s about the future, about meeting and exceeding expectations. It had always been his policy to under-promise and over-deliver. People liked pleasant surprises more than disappointments, of course, but the investment community seemed to like pleasant surprises even more than they did dead-on predictive accuracy. The answer to the present conundrum, then, was to tweak the model for 1999 to predict greater expenses and smaller revenues—in other words, lower expectations, especially in the first half. In so doing, Glenda’s Q4 disaster wouldn’t look so glaringly out of place.

In the two hours he had available, Winn lowered the coming year’s revenue projection from $175 to $150 million. He increased expenses, especially advertising. This would serve to make the pitiful performance of Q4 blend into a logical, believable scenario. Craig pulled his calculator out, got a sharp pencil, and a clean pad of paper. He created a new model, a detailed assumption page, and a presentation strategy.

Without a second to spare, Dean came back to his office and sat at the antique table. He dialed Dandridge’s number on the speakerphone as he instructed his assistant to fax Dale the new handwritten assessment. As the CFO sat, the CEO delivered his spiel. They held their breath.

“I’m glad you’ve done this,” Dandridge exclaimed. “You guys were growing so fast, it was, frankly, unbelievable. This new scenario makes much more sense. It’s more credible, an easier sell. As a matter of fact, it makes so much sense, instead of getting you three to four times forward revenues, I’ll be able to get you five. Let’s see. That’s a gain of $150 million. We’ll file the IPO at $625 million. How does that sound?”

Both men sat there looking like they’d been slapped silly with the good fairy’s favorite wand. In curtailing expectations in a last ditch effort to save the company, they had actually increased our valuation by $150 million. Dean grinned and shook his head in admiration. “I think I have just witnessed the most incredible financial turn of fortune since some guy talked FedEx into changing their mind. Two hours ago we were dead. Now we’re worth more than ever. It’s a pleasure to serve with you, sir!”

There were few people who could appreciate the magnitude of what had happened like Dean. But Craig simply smiled and said, “I’ve given the shareholders their money’s worth today. I think I’m going to go home now.”

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The very moment we had raised the money we needed to survive, the founders turned their attention to ridding themselves of their incompetent, blackmailing President. They’d hired Russell Reynolds to find a COO so they could in due course torch the wicked witch.

“It isn’t happening,” Rex grumbled.

Craig, too, was perplexed. “We’ve engaged the biggest executive search firm around, and they’ve come up empty handed.”

“Maybe it’s the field—dot-coms are just too new. They can’t find anybody who’s experienced that can make the transition to our world.”

“I dunno. We’re really just a retailer in a new venue. I can’t believe it—looks like we’re on our own again.”

It was an issue on which Craig and Rex were divided. With the specter of Dynasty’s funeral pyre ever before him, Craig was convinced that as an entrepreneur/founder, he needed to turn over the reins of the company to a professional manager before it got too big—preferably as the company went public. Rex thought more of Craig’s management abilities than Craig did; he wanted him to stay in the saddle a while longer. But they were on common ground when it came to Dorchak. She had managed to hang onto her job only because circumstances had prevented them from firing her. Ever since the unpleasant episode a few weeks after her arrival, the company had either been looking down the barrel of an IPO, as we were now, or had been desperately broke.

She still looked fine on paper, talked the talk, had all the right moves. Only a handful of people knew she was poison. But our founders knew, and that was enough. They felt there was no way they could ethically go public with an insecure, conniving President unless there was a solid plan in place to jettison her sorry butt.

“I know who I’d like to have, if we could get him,” Craig said.

“Who?”

“A guy I’ve known for years, Byron Peters. He’s the COO at Price Costco. He’s an experienced retail pro, knows operations, and he’s familiar with Sol Price’s way of thinking. He’s a known quantity.”

“Okay. Anybody else? We ought to be looking at several candidates.”

“You remember Tom Morgan, the COO at USOP?”

“He was there the day we played golf with John Ledecky, right?” Rex had a good memory for golf trivia.

“He’s running an office supplies distributor. The category is important to us, so it’s a pretty good fit. I got to know one of his execs pretty well, a do-nothing Harvard MBA named Tom Starnes. He loves Morgan. I asked Motley about him. He said he’s got a decent reputation. ’Course, people tend to say nice things about guys who buy their products.”

“Well, then. Let’s try ’em both.”

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Professional managers expect employment contracts detailing their convoluted compensation packages, options, golden parachutes, and the rest. Value America, however, was a bit more democratic. We used a “one-size-fits-all” approach. Everybody from Craig and Rex on down signed the same exact agreement. It was supposed to be the company’s first line of defense against the debilitating “every man for himself” philosophy so prevalent in corporate America. It is perhaps telling that one of Glenda’s demands the previous September had been to get her own customized employment contract. After the fact, mind you.

For months now, Glenda’s lawyers had been negotiating with our Justin Caise over contractual minutia, and still there was no signed agreement. At issue was her severance package—especially if we elected to dismiss her unceremoniously, or just demote her, pull her fangs, so to speak.

Glenda saw herself as the very picture of altruistic patience to have worked so long without a special contract granting her every whim. It was so unprofessional not to have one. So as the due diligence for the second IPO moved into its final week, she saw her chance to rectify matters.

As part of every IPO's due diligence, each officer is interviewed by counsel. They typically ask benign questions; it's boilerplate sort of stuff, but a necessary part of the process. One by one, they had checked off the boxes next to the names of the officers—all save one. Dorchak always seemed to be unavailable. The lawyers began to smell a rat, and called Craig. "You have a problem," they said. No kidding, Craig thought.

Now that she had garnered the desired attention, Glenda turned up conspicuously absent. She had confirmed her first blackmail by writing Craig a letter, and she did so again. Glenda informed the company that she would not be coming to work until she got a new contract, saying, "Before I move further, I want to come to an agreement on my personal matters, as outlined under separate cover. I cannot proceed..." unless I'm given everything I want, she implored.

Her showing up absent on the eve of an IPO caused jitters amongst those who are easily spooked. The practitioners of IPOs are universally allergic to the slightest sign of trouble. Was Dorchak aware our S1 couldn't be filed until she complied? Was she aware that she was putting employees and shareholders in peril for her own personal and selfish gain? Of course. Why do you think I chose this particular time?

A thoroughly disgusted Justin Caise and an utterly perturbed Rex Scatena spent hour after grueling hour with Glenda's lawyers, hammering out a contract she would sign. It was a watershed moment, the first self-centered legal document ever crafted on behalf of Value America. It would not be the last.

The only things Justin and Rex made sure not to give up were the right to hire someone over Glenda and to be able to fire her for cause without penalty. In the end, the contract was signed, the final interview was conducted, and the S1 was filed. Dorchak had magnanimously allowed the company she worked for to continue living.

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"Peters says he's interested," Craig told Rex, "but he's worried about losing his Price Costco stock options. His lawyer is overly fastidious, too."

Rex sighed. The process could take months. "What about Morgan?"

"I'm thinking we could bring him in as Chief Operating Officer, distance ourselves from Dorchak, and promote him to CEO after the IPO."

But Morgan wouldn't stoop to interview for anybody's COO position. "I'm the CEO of a Fortune 500 company," he proclaimed. "It'd be beneath me." He didn't mention that under his leadership, USOP was rushing headlong toward its new status as a Fortune 5000 company, splintered into impotent fragments of its former self and ultimately into bankruptcy. And he didn't mention that the only reason he was at USOP was that Ledecky had recruited him out of a lackluster twenty-year career in auto parts and office supplies, where all he'd had to do to "make it" was show up to work and accept responsibility for absolutely nothing.

So Craig suggested Tom could come in as CEO instead. This would be problematical at the IPO since he'd have none of the credibility only time and performance provide. The advantage for Tom would be that his stock option strike price would be set pre-IPO, a million-dollar advantage. Craig explained that an offer had been made to Byron Peters some time ago, but that negotiations were moving slowly. Tom, naturally, figured he had better move fast if he wanted to get his share of dot-com gold.

As part of the process, Craig called Fred Smith, seeking his advice about vacating the office of CEO. Fred complimented Craig as lavishly as he had ever been praised, saying, "This reminds me of me. I've always tried to hire the best COOs in the country. There's no limit to what a man can achieve if he is able to recognize his strengths and weaknesses. You're decision here is not unlike that made by some of history's great leaders."

"Fred, I'm told you've met one of the guys we're considering. His name is Tom Morgan, from USOP."

"Yeah, I think so," Smith replied. "We tried to buy one of their companies, Mail Boxes Etcetera. Morgan flew a leg with us on one of my planes. If he's the same guy I'm thinking about, he seems okay, kinda quiet, meat and potatoes. Could be a good fit for you."

Craig questioned, "Mind if I have him give you a call?"

"That'd be fine," Fred agreed.

Unbeknownst to Rex and Craig, Morgan was doing a little soul searching of his own. He called his spiritual advisor first, Mr. Goose Godfrey. Godfrey, who was paid handsomely for his counsel, put Morgan in touch with Dan Case and Gerry Roche. Dan, AOL's Steve Case's older brother, was CEO of H&Q, the technology investment banker. Roche was CEO of the giant headhunting firm Heidrick & Struggles. Both told Tom that the dot-com world was hot. If it didn't work out with Value America, they could always find him another job. So Morgan used the number Craig had provided and called Fred Smith. Fred was, as usual, passionate, articulate, and sincere in his praise of both Craig Winn and his company.

The final interview was conducted at Craig's home. Morgan was pleasant and polished. Craig was pleased with Tom's preoccupation with his faith and family. And he certainly looked professional, a picture of suave sartorial perfection. The founders liked what they saw (or thought they saw). Moreover, they desperately wanted to solve their Dorchak problem.

Craig explained that he had promised himself he would resign as CEO as soon as the company had grown large enough, and that time, he felt, had come. Tom took it all in, nodding knowingly.

Rex explained that Glenda Dorchak had to go. Tom, he said, must come up to speed on sales and advertising quickly. It was imperative that the firm's dependence on her be eliminated and that she become relegated to a minor role, or better yet, to the unemployment line. Morgan was told about Glenda's blackmail schemes and her willful disregard for budgetary restraint. Tom took it all in, nodding knowingly.

Rex spoke again. "The last thing we need from you is inspiration, Tom," he said. "In the person of Craig Winn, we have all we need of that. He's a charismatic, visionary leader. The best thing that can happen is for you to do your job, manage the company, keep the pieces tied together, running smoothly. Free Craig up to do what he does, forming relationships, being out in front selling the merits of this thing to new partners and brands. Frankly, there's no one who can do it better. If you can work that way, the future's bright."

Tom took it all in, nodding knowingly.

Morgan said he was ready to leave USOP to join Value America. He said he would need a special employment contract, of course, a huge compensation package, stock options, and a partridge in a pear tree. He also said that he wanted to give his old firm plenty of notice so as not to leave them in a lurch. They, however, told him he could leave tomorrow.

For Byron Peters, it was better late than never. He joined our burgeoning executive team at a level equivalent to Glenda's, with his own shiny new contract. His had to be better than Tom's, which had to be better than Glenda's. Craig and Rex were so intent on removing Dorchak's stain, they agreed to pay Peters $10 million out of their own pockets to cover potential losses on his Costco options should a particular set of adverse circumstances occur. The incident serves to demonstrate their resolve to clean up their mess.

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Craig was not known for being a trend follower, but this one held promise. It had become chic to exclude company executives from boards of directors, the theory being that you could get input from your own team any time you wanted it. This left more room for prestigious board appointments from outside the company, appointments that bore the potential for strategic partnerships of immense value.

Rex was by this time no longer President of the company. With the advent of Tom Morgan as CEO, Craig too would be leaving his managerial role behind. They became merely Chairman and Vice Chairman of the board, co-founders and the company's two largest shareholders, still owning sixty-two percent of the stock between them after the dilution of past investment rounds. But a Chairman is little more than a parliamentarian, with no more influence than any other board member.

Dorchak's initial blackmail had landed her a seat on the board, and as long as there were other insiders serving, she couldn't be forced off without sending up pre-IPO red flags. But if we went to an all-outside board, she'd be history. Craig and Rex approached Johnson and Motley, explaining the situation. Both graciously sacrificed their positions in the interests of removing Dorchak. She wasn't happy about it, but she was gone. One down, one to go.

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Fortunately, Internet stocks had recovered, but déjà vu was starting to raise its ugly head. The market was showing signs of dot-com jitters. Amazon had stirred things up by doing the largest convertible debt deal in history—a $1.2 billion anchor. It had made a lot of folks nervous. Craig was convinced that if we didn't get our IPO on the road soon, we would find ourselves rowing up another waterfall.

This was where it had all started to unravel the last time we had tried to take our company public. The S1 was done, the SEC's comments had all been resolved, and the teach-ins for the sales force had been scheduled. They were to begin at Robertson Stephens, starting as before with a one-on-one preview for analyst Dale Dandridge.

At the conclusion of the new road show presentation, Dandridge rose, shook his head, and smiled. "I'd give that one a nine-point-five, gentlemen. It's probably a ten, but I've never given a ten. Don't change a thing."

The reaction they got from the Robertson Stephens sales force was roughly the same. Craig was happy and bewildered at the same time. We were the same company they had all but spit on six months before. Now all of a sudden we were God's gift to yuppies. Go figure.

As strained as our working relationship with Robbie Stephens had become, we were joined at the hip with them, for better or worse—like a marriage gone bad. Once a company selects its auditors and its lead underwriters, it's virtually impossible to change them—the Street automatically assumes there's a problem the firm is trying to conceal.

This was not necessarily true with the other support players. In our darkest days, Volpe Brown Whelan had stood by us—Mark McNay and Andrea Williams had been instrumental in helping to arrange capital, but Hambrecht & Quist had done nothing. As much as Craig and company loved H&Q's analyst, Suzzi Maupin, there was no way we were going to go into this IPO without rewarding Volpe for their tireless support.

"Suzzi," Craig explained to the H&Q analyst, "this is the right thing to do." Doing the right thing was important to Craig, even if it was out of step with the rest of the business world. "We're not going to shortchange Volpe Brown. They've been so supportive I can't in good conscience give them less than thirty-five percent of the deal. I have to give the lead house forty. That leaves a maximum of fifteen percent for H&Q, with Robinson-Humphrey getting only ten. Your work as an analyst is superb, Suzzi, but your investment bankers have been no help at all. They didn't show up. I don't even know their names. If you can't accept fifteen percent, it'll be a no go. I'm sorry."

The analyst sighed. "You're right. Everything you've said is true. But my firm won't accept fifteen. We're going to have to bow out, regrettably."

It was regrettable, Craig reflected, but in the end, good was rewarded. The final tally was Robertson Stephens forty-four percent, Volpe Brown thirty-nine, Robinson-Humphrey fifteen, and E*Trade two. It was the first time E*Trade was listed as part of an IPO syndicate. One detail down. A hundred to go.

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It was beginning to look like a classroom exercise in chaos theory. The Series C investment round had closed weeks previously. It was history. Who would have thought that in amongst that $75 million, a bad penny would come back and haunt us?

The Series C warrants indemnified investors if the company didn't increase in value, or if it failed to go public in a timely fashion. There was a "trigger price," below which there would be monetary consequences for us. But our value had passed that point some time back, making the warrants meaningless, like a man who had outlived the term of his life insurance.

The auditors couldn't come to terms with their possible non-cash consequence, so they hadn't released the Reds for printing. But in order to get out on the road, we had to have the Reds. Time was now our enemy.

Bentley Hollis, Robbie Stephens' syndicate manager, brought things to a head. He told Craig that he was unwilling to set the road show appointments without the Reds. For his part, Craig could envision the whole thing coming unglued again if he didn't force the issue. So he instigated a game of chicken.

"Bentley," he said, "the last time we tried this, your firm cost us big time. I don't like the way the market's acting. I'll get the Reds. You set the road show appointments."

"Alright. I'll set the appointments, but if the Reds aren't here by Tuesday, I'm going to cancel them."

Hollis would only flinch if Craig couldn't deliver. Like the bumper sticker said, "Get in. Sit down. Hold on. Shut up."

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"Stay away from that man. He's dangerously unbalanced."

They were talking about Craig Winn, skiing down a Utah slope with a cell phone glued to his ear. Yelling.

Craig and Rex had come to the conclusion that it was silly to fly all the way back to Virginia from San Francisco, only to turn around three days later and fly back to the west coast to begin the road show. Since their kids were enjoying an early spring break, they met their families in Deer Valley to get a little skiing in before commencing the exhausting ordeal.

As usual, what had seemed like a simple solution to Craig had been a problem for the unimaginative auditors. If we took the company public now, our valuation would void the warrants, so he told the auditors to pick the worst possible number they could conjure up, and publish that in the Reds. Then, if the warrants, through some unforeseen twist of fate, did come into play, their impact would be less than they announced. Everyone would be happy. The auditors, being sticklers for detail, balked.

That explains why Craig was yelling into his cell phone. He was "negotiating" with PwC's Frank Noblock. "Listen to me, Frank," Craig threatened. "Dean Johnson is at the printer's. If you don't do this, my next call will be to him, and I'm going to tell him to print the Reds without your opinion. The fact that it's never been done before won't stop us."

"You can't do that!"

"Oh, yes we can. And we will. Either you act responsibly and choose the worst possible number for the non-cash consequences of the warrants—which aren't going to be exercised anyway because our valuation is already above their trigger price—or you'll go down as the first accounting firm in history that allowed Reds to be printed without an opinion. It's your call."

The Reds were printed. In the "Financial Pages" section, on page F-2 (following the seventy-seven-page body of prospectus material), the opinion of PricewaterhouseCoopers LLP appeared: "In our opinion, the accompanying balance sheets and related statements of operations…present fairly, in all material respects, the financial position of Value America…." Upon pages F-19 through F-21 appeared Point #12: "Subsequent Events," explaining in arcane accounting mumbo jumbo the ramifications of the Series C warrants. There is no extant evidence suggesting any investor ever read these pages, and far less to indicate that they might have been understood.

Craig had won his second game of chicken.

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"Those Reds aren't going anywhere."

Tuesday was approaching like a freight train. The Reds were edging their way toward the presses, but we had another battle on our hands. The Reds said, "Over a thousand brands have chosen to partner with us." We had actually printed the names of over five hundred of them. You couldn't buy that kind of credibility with all the tea in China. You had to earn it. There was just one problem. The underwriters' counsel found the number incredible. As in "not to be believed."

The problem was exacerbated by the fact that we couldn't just go to technology and ask the geeks to print us out a comprehensive list of our brands. There was no central repository where they were all listed together, nor should there have been. There were overlaps from department to department. There were esoteric issues concerning what constituted a brand, as opposed to a supplier or a manufacturer. The lawyers wanted proof, or the whole thing was toast.

Craig once again found himself yelling into a cellular telephone in a public place. This time it was in Robert Redford's Zoom Restaurant in Park City. They wanted proof. We would supply proof.

Dean enlisted his lieutenant, Tracey Wingfield, Richard Gerhardt, Andy Rod, and Isaac Saltzberg's Marketing group to do a physical inventory of brands. They worked for the better part of the night, reviewing the logo pages and putting the names on a master list. They checked the departments we'd created for firms that had brands in several categories, like HP, (with Colorado, DeskJet, LaserJet, OfficeJet, ScanJet, SureStore, Brio, LXPro Servers, Pavilion, Vectra, PhotoSmart, CopyJet, and DeskWriter). The ordeal came to be known as "The Night of a Thousand Brands."

The lawyers never did find out exactly how many brands we had in the store that night. When the documented list got well past a thousand, they backed down. But we continued counting. Gerhardt gave Craig the final tally. It was thirty-three pages long and contained the names of over 1,500 brands, all of which were in the store. Craig had won his third game of chicken. But this one came around for another go, squawking, with feathers flying. Some lawyers don't know when they're licked.

They took issue with the Red's overleaf, a page I had designed showing seventy major brand logos and a heading that read, "We're Known by the Company We Keep." Underwriters' counsel told Craig we couldn't show this brand logo page without the express written consent of each and every brand. "But that'll take weeks. Besides, we have other store pages with logos in the S-1," he protested.

"Yes," they said, "but those pages are actually in the store."

"Thank you," Craig said. Within the hour, we had Web-enabled the simulated page and put it up live in the store. Craig provided the lawyers with the URL, so they could see it for themselves. They were not amused.

Chicken, game number four: Winner, Mr. Winn.

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Naturally, in order to take a company public, you have to have the blessing of its board of directors. The step was supposed to be a fait accompli. Who would have thought the bad penny would show up again?

Rafe Durn had a problem with the way the auditors had described the Series C investments. He thought it might pose a tax problem for his investors. Dean reminded him that PricewaterhouseCoopers had come up with the formula. “And, as I recall, Coopers was the firm you relied upon when you questioned our policies back in ’97. Besides, there’s no time to change it now. The road show appointments are set.”

Durn stood firm. “I don’t care. I’m voting no until they’re rewritten.”

Dean called Craig in desperation. He had had it with Rafe Durn.

Craig calmed his trusted CFO and told him he would handle Rafe. Craig and Rex were sharing a beer in the Deer Valley Lodge after a day of cell-phone skiing. “Dean, have Tracey call each board member. Set up a conference call for nine o’clock eastern—that’s seven o’clock mountain time. Get some rest. I’ll get us through this.”

They picked up separate phones in the condo that night. As predicted, everyone supported the IPO except Rafe Durn. For the fifth time in three days, Craig found himself playing chicken. “Rafe,” he said, “I’ve done everything I can do to take our company public. Right now we’re as ready as we’ll ever be. The market is receptive, but it won’t hold. Last time, your delays cost us. I’m not going to let that happen again.”

Laying down ultimatums wasn’t Craig’s style. He knew that if you gave an adversary no room to maneuver, the situation could easily blow up in your face. He had learned that the hard way back in his days with The Winn Company. It hadn’t been pretty. And yet, almost against his will, he found himself pushing Rafe Durn into a corner, giving him no way out.

“We’ve been down this road before, Rafe,” he spat out the words. “I offered you the keys to the company. Well, I’m doing it again. You can either say ‘yes’ and give us a unanimous decision tonight so we can start the road show on Wednesday, or you can show up in Charlottesville and start running the company.”

There was an unbearable silence. Somebody coughed. Durn finally spoke. “Alright, Craig,” he said. “You’ve got my vote.”

With a collective sigh, the final board meeting for Value America as a private company was concluded. As farewells were uttered, someone said, “Go out there and do us proud, guys!”

“That’s the plan,” Craig said as he jumped from the frying pan into a raging fire.