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tried anything new."
- Albert Einstein

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Child Entrepreneur David Koretz, Now CEO Of Mykonos Software (Part 1)

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Sramana Mitra: David, let's start at the beginning of your story. What is the genesis of your entrepreneurial roots?

David Koretz: I grew up in Rochester, New York. Like a lot of entrepreneurs, my journey started earlier, more informally than it did formally. My parents owned a small insurance and commercial collection agency. They worked together all day, so when they came home they would still talk business, especially around the table. I was either not going to pay attention at the dinner table or I had to learn how to understand business.

My grandfather had built a company from scratch that ultimately became the largest manufacturer of socks in the country. He did that out of the **Empire State Building** in New York. I ended up having **entrepreneurial influences very young**. As a result, when I was seven I started selling sea shells at the edge of my driveway. My grandfather ended up FedEx shipping me a contract to supply the sea shells and split the profit with me. I reviewed the contract and tore it up and then called him to tell him that I was not going to split the profit and that I would rather go to Florida to get my own sea shells. I always had those types of lessons pushed on me from the time I was very young.

When I was in fourth grade I started a business where I sold candy to students. Pretty soon I ended up not having enough room for my books, so I left them at home. My entire locker was filled with candy. I then started renting my neighbors' lockers. Eventually I hired other students, so I had a whole bunch of students working for me. I ended up hiring my sisters' friends to drive me to the wholesale club because they were old enough to have a license. I made about \$250 in cash a day.

Sramana Mitra: What did you do with the money?

David Koretz: There was nothing to do. I was too young to have any real purpose, so I would just save it. My parents came home one day and found a stash of \$15,000 in cash that I had stockpiled from my candy business in my room when she was putting clothes away. She was panicking trying to figure out why I had that much cash. Eventually I got caught, and the principle did not share my entrepreneurial views and threatened to suspend me.

I ended up starting my first real business when I was 14. I had always been very interested in technology, and for me business was a way to get into some of the technologies that I was excited about. The first technology I really got excited about was **home automation**. There was a technology that would allow you to call your house. When you called, you could tell the house when you were coming home and it would adjust the lights for you. It was cool and could **drop your power consumption by 50%**.

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Sramana Mitra: How did you learn about home automation and energy efficiency at the age of 14?

David Koretz: I used to read trade journals such as CES Today and Asian Trade Sources. I signed up for some journals as a distributor, and it allowed me to see all of the latest technologies coming out of Asia for the U.S. market. It was a paid-for precursor to what became Alibaba. Buyers used to scour those magazines and trade journals hoping to find that one interesting product that nobody else had.

I started finding products that I felt would do well in the U.S. market with minor adjustments. I started contacting those companies to see if they would give me distributor or license rights to that product for the U.S. market. A bunch of them agreed, and by the end of the first year 15 companies had given me **exclusive rights to the U.S. marketplace**. I always asked for a sample so I could validate the product. I would play with it, and if it was cool and the technology worked the way it was supposed to I would ask them for the rights.

Sramana Mitra: Did they know you were 14 years old?

David Koretz: No, none of them did. Eventually some of them figured it out.

Sramana Mitra: Whom was the contract between?

David Koretz: I had created a company and that company would make the agreements with the other countries.

Sramana Mitra: Did you focus only on home automation?

David Koretz: No, I started out in consumer electronics. I started in **home automation** because I found that product very interesting.

Sramana Mitra: What did you do once you had distribution rights to a product?

David Koretz: I would serve as the distributor and sell it to consumer electronics stores like **CompUSA, Fry's** and others. I did that until I was 17 years old.

Sramana Mitra: How many distribution deals did you achieve with that company?

David Koretz: The first year I did 15 distribution deals. We did \$226,000 in revenue, and I made about \$26,000 off it. The next year we did \$2.4 million in revenue. We had 35 distribution deals at that time. The following year we did \$14.2 million in revenue and had 60 distributors.

A year and a half before that I really got into **home automation**. It was driven by small electrical pulses that would go through your home network. The flaw is that most Americans do not live in standalone homes, especially early adopters. They live in apartments. They live in multiunit dwellings where the home network was not a perfect loop, and the products would not work in apartment buildings. Additionally, even in the event you had a standalone home, there would be cases where the signals never reached the other end.

I partnered and cofunded development of the first wireless home automation system. That system was effectively using mesh networking systems. It took every device and made it a receiver and a repeater, so they would also broadcast them. Mesh networks are not very efficient, but on a small network like ours it was a good thing. That allowed us to build a system with no size limitations.

The home automation technology we developed really powered our sales. My last year we did \$110 million in sales, and I ended up selling the company in 1997. That was an interesting time because it was in the middle of the Asian financial crisis. There was massive currency devaluation. We would sell to companies and they would tell us they were selling at cost minus seven. That was normal. The government would fund large companies with loans, but the small companies just went under. We watched 110 manufactures drop down to 20 manufacturers in just 18 months.

Sramana Mitra: Why did someone buy the company, given the market dynamics?

David Koretz: It was not specific to us because it was a macro problem. The guys selling at cost minus four had done it for years, and they had strong loans from their governments. If you stopped selling for three or four years you were not going to be able to re-enter the business. Most governments felt that it was the cost of doing business.

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Sramana Mitra: You navigated a sizable business from 14 to 18 years of age. Did you parents get involved in it?

David Koretz: My parents and my grandfather were not involved and that was intentional on my part. I went to high school on various schedules. It was not official, but I just did it. From 8 to 5 I could **deal with U.S. distributors. I basically attended each class once a week. I don't think my parents really understood how little I was going. I was dealing with Asian companies and had the 12-hour time difference.**

I would typically work from 9 at night until in the morning and then sleep for two hours. I would then go to high school or work with the U.S. companies. I would then flip so that I could attend other high school classes.

Sramana Mitra: What was the actual work you were doing?

David Koretz: The first element of that work was a constant vigilance to find new manufacturers. Once you get a product you have to assume that it will commoditize in 12 months. Once people realize how good a product sells, they will hand a copy of the product to a larger manufacturer and ask them to make 50,000 units which meant we could no longer compete on cost.

The second part of the job was **selling to U.S. buyers.** I would put together distribution deals. I did a lot of phone and fax work. Email was not as big yet. The third part of the business was managing the logistics to get product from that part of the world to the U.S. efficiently.

Sramana Mitra: Where you involved in that process?

David Koretz: If you take a product **FOB Hong Kong**, most distributors do not understand how to take a product and get it into the U.S. market. You have to deal with customs, freight forwarders, and insurance regulations. I managed all of that. I hired customs agents, freight forwarders, and had to keep my eye on that entire work flow. If I bought a 40-foot shipping container and it came to port in New Jersey and I would have to split that container among my various customers. I would then have to truck ship all of the customer shipments from that container in New Jersey.

Sramana Mitra: Did you have any employees?

David Koretz: I just had a few. It is not an employee-heavy business. It was about deal-making and orchestrating. I only had a handful of people even when I reached \$100 million in sales. I was not inventorying product, which helped a lot.

Sramana Mitra: So you were 17 years old with a \$100 million business that only had 4 or 5 employees and you decided to sell it?

David Koretz: Yes. Once we had the right contracts in place I started getting a lot of offers to buy the company. They would always try to figure out if they could work a deal around me, but if they were not able to do that they would pick up the phone and call me. They usually wanted to just purchase a contract. I had 125 contracts, but they were not even. There were roughly five contracts that were worth 60% of the business.

If I had the U.S. locked up then other companies would sign with that same manufacturer for the rights to Canada. Then they would create another company to **import the product from Canada**, so they essentially bought from their own company.

Sramana Mitra: How much did you sell the company for?

David Koretz: I sold it for mid-seven figures. Margins at that time in the industry were 0.25%, but we were at 1.4% because we played the 12-month anomaly of identifying products ahead of their time.

Sramana Mitra: The valuation of that type of business is always on earnings?

David Koretz: Always.

Sramana Mitra: So you were now 17 years old with a nice stash of cash. What came next?

David Koretz: I had gone to college at night while I was running that business. I went to Rochester Institute of Technology from 6 to 10 at night four nights a week. I wanted to go to business school and signed up for Babson College. Before I went there, I sold my company and started another business with a friend doing website development. I sold that business back to my partner and started a third company. We got **VC financing** right after I got to Babson.

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Sramana Mitra: What was the concept behind the business you founded just as you went to Babson?

David Koretz: It was an information sales business. It was a Dun and Bradstreet and Axiom type of company. At the time all of those products were all offline products and we were going to take them online.

Sramana Mitra: Did you stay at Babson?

David Koretz: No, I packed everything up and left. Technically I am probably a second-semester freshman there. This was 1998 and I stopped going to class so I could write the business plan and get venture funding. I was funded by **Tom Golisano**, whom I had met when I was 14. I was doing an introductions occupation class in my high school and my teacher gave me a professor at RIT who taught business. I told my teacher I did not want someone who taught business, I wanted someone who did business, so I asked to shadow Tom. I ended up calling him every day for 40 days until I was finally able to get through and spend a day with him as part of a shadowing program.

Sramana Mitra: How much money did you raise while you were at Babson?

David Koretz: I raised \$275,000. We did two things that nobody had done before. We built the first online engine that allowed you to input a metropolitan statistical area and some classification codes and it returned data in real time. We had a licensing deal with Axiom, and we put an **overlay of NAICS data** which made us the first **NAICS compatible sales system**. We charged on a cost-per-lead model. We flat rated that model to make it small business compatible.

Second, we took it a step further. They would update the databases by shipping 6,000 phonebooks to Asia where they were input manually for six cents an hour and sent back on CD-ROM. Sometimes you can have 30% error rates with those databases which is very high for sales and marketing. We built a **product called Persephone**, after the Greek goddess of the harvest, which went out and scoured the entire web.

Sramana Mitra: That sounds a lot like what Intarka did. That company was venture funded and was one that I founded in 1998.

David Koretz: Small world! There were only a handful of companies doing that. Were you scouring the NetSol database?

Sramana Mitra: No, we were scouring the Internet. We had AI algorithms to do the work for us.

David Koretz: We also built AI algorithms, and we took the NetSol database and scoured off of them. We used hundreds of threads so we could pull into the database quicker. On the other end the challenge was knowing if the data was better or worse than what we already had. That is when we started using **AI to do qualitative analysis** based on what we had. Those pieces of technology were sold off separately to different companies, but it led to another good exit.

Sramana Mitra: When did you sell?

David Koretz: We sold in March 1999. In August I started **BlueTie**, which is a SaaS company. I believed that applications were going to shift to the cloud. We were the first company to see that email collaboration did not makes sense inside of small company offices. We built an **alternative to Exchange Server** from the ground up. We were the first app that could do drag and click, double click, and really make the Web environment feel like a desktop experience. Today it has 1.7 million users and 250,000 small businesses hosted on that platform.

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Sramana Mitra: By this point of your career you had founded three successful companies. What are some of your tips on customer acquisition and how to build businesses?

David Koretz: There is an interesting challenge of risk. For a long time BlueTie was way out ahead of Google and Microsoft. When they began doing Web-based applications we still had a big lead over them. We had nine-figure **M&A offers** on the table that, in retrospect, we should have taken. We got caught up in an easy trap of believing that ramp rates will never stop.

We turned down the offer right around the time that Zimbra did their deal. As those assets came up there were fewer companies that could be the drop-off point, and when they left other companies got even more desperate. We should have realized that we had a unique time and opportunity, and we didn't.

Sramana Mitra: Who among the large guys in business in 2007 should have bought your company?

David Koretz: Cisco would have been a logical buyer because what powers Web conferencing today is the calendar. They needed to own the calendar.

Sramana Mitra: The primary business of WebEx was sales lead generation.

David Koretz: Clearly webinars were a big part of it. The salespeople who use it for presentation, that was their primary purpose.

Sramana Mitra: I don't see that being the part of a workflow where the email system finds its home.

David Koretz: It's where a calendar finds its home. If you are a sales rep and you make a calendar appointment, it should automatically establish the WebEx meeting for you.

Sramana Mitra: I don't buy it.

David Koretz: You have history on your side because it clearly didn't work.

Sramana Mitra: Companies like Microsoft are in this business.

David Koretz: There were definitely big companies in the business, and long term there was undoubtedly going to be **vendor consolidation**. People are going to want a tighter, more integrated stack. They want a system where everything is integrated, including Web conferencing. I don't think anybody has executed on it particularly well.

Sramana Mitra: Google is going after this space as well now. I have a company in 1M/1M that is going after a related space. There is a big exodus from Lotus Notes to Microsoft or Google. The Microsoft part is not a surprise, the Google part is.

David Koretz: I am not sure Google has it right yet. They have taken the headlines and have created the fear.

Sramana Mitra: They are doing very well in the space. Serious enterprises are moving to Google for this application space. That surprises me.

David Koretz: We watch the deals they are doing on the backend because we compete with them there. Here is why I don't think they have it right yet. A huge percentage of their deals are still free. They have a very low up-sell percentage. They are doing deals at massive, massive discounts off retail. Right now they are trying to capture market share.

Sramana Mitra: The company that needs to be in this space, and would like to be there, is Salesforce.com.

David Koretz: On paper today **Salesforce.com is a Google partner**.

Sramana Mitra: True, but they need to be in this space.

David Koretz: I know the guys there pretty well. I don't believe they are convinced that they need an alternative to Google. They believe Google gives them the right competitive advantage. I also think five years from now they will recognize that as a big error.

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Sramana Mitra: What is the story behind Mykonos?

David Koretz: We started seeing a problem inside BlueTie. It was a huge issue; hackers were trying to break into our databases for a number of reasons. Some were trying to steal credit cards and others wanted to use us as a spam engine. The net effect is that we were constantly being attacked. We went out and looked at the tools in the market to identify how we were being attacked, and every single tool fell into the same category of being theoretically un-valuable.

The tools were called **Web app firewalls**, folks like **Citrix** and **Barracuda**. They are all based on an open source product called **ModSecurity** and they all work the same way. They work just like antivirus works. They rely on attack signatures, and then they wait for those types of attacks and block them. There are two problems with that thinking. First, it does not work because there are an infinite number of attack vectors but there are a **finite amount of attack signatures**. The second problem is that it is only good for attacks you know about.

On the Web, the attacks are much faster. I can do an SQL injection and have a million credit card records the same day. Knowing about that four days later is worthless. The security model that has been around for the past decade is a castle-and-moat model; keep people from getting in. Computer network defense companies keep trying to make the moat better, but I think that approach is fundamentally flawed. If you believe that you have a browser with potential vulnerabilities, there is a range of attack vectors that approaches infinity.

We started solving the problem with a very different approach. We don't want to keep them on the perimeter; rather, we want to change the fundamental economics of the hack. We started looking at deception as a core strategy. Instead of trying to keep the hacker out, we add hundreds of fake vulnerabilities. As the hacker starts to look for holes they are going to trip over a number of vulnerabilities. We might even make more work for them.

We will return **fake .htaccess files** that point to fake password files. If they take the six or seven hours it takes to break the encryption on the password files, we will even let them login to a fake config.int file. The problem for them is that it is all fictitious. It has all been generated on the fly by a Mykonos server and is specifically intended to waste their time while at the same time demonstrating to us just how sophisticated they are.

Our approach breaks automated scanning tools. You are now in a world where you have to manually hack. You are now in our game where you are trying to filter through a huge number of vulnerabilities. We have dramatically increased the cost of hacking.

Sramana Mitra: Who came up with this?

David Koretz: A team of us inside of **BlueTie**. We spun that concept off as a different company.

Sramana Mitra: When did you spin it off?

David Koretz: We did that in December 2009. I knew nothing about security, but I took it to the **RSA conference** and told them that this is what we had. Two days after Gartner named us one of the 2010 Cool Vendors of the Year. We put it into beta and people told us that not only did it work, but it was showing them things that they had never seen before. **Bertelsmann** put us in front of their site and found out that 11% of all traffic that had been flowing through their site was malicious. We identified 300 attacks against their site the first day.

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Sramana Mitra: What did you charge Bertelsmann for that deal and what does your product cost today?

David Koretz: We charged them very little because we really wanted the reference. Our product is an enterprise product. We start at 25 thousand dollars and it can range up to 150,000 dollars. Large organizations may have multiple deployments because they have multiple data centers. Compared to the cost of getting hacked we may be massively under pricing today. The problem we encounter at places like RSA is that we are so different people will tell us that if we are successful, we will be a billion dollar company. They always, always use the 'if' caveat.

Sramana Mitra: Has this all been funded out of BlueTie?

David Koretz: We spun it off and it is funded through the same investors. We will probably raise a round in the future. It is truly a standalone company. We gave the investors at **BlueTie** a pro-rata equity stake in Mykonos when we spun it off of **BlueTie**. All additional investments have come from that same group of investors which includes myself, **Tom Golisano**, the Polisseni family, and **Walter Turek**. They are all originally a Rochester based group.

Sramana Mitra: What has been your experience working on technology companies in Rochester?

David Koretz: It is without question a double edged sword. There are two enormous advantages. Our annual voluntary attrition rate on the engineering team is right around zero. We don't compete against any other **security companies in Rochester, NY**. We also have a massive economic advantage because we are not paying Silicon Valley overhead. The downside is that most cultures outside of Silicon Valley are lifestyle driven. They are driven by people who want a nice life-work balance, have families, and live the traditional 9 to 5 life.

Work is a part of their overall thing but not a big driver of it. I always found it difficult to find people who share the same level of aspiration and work ethic. When I created the first business I remember employees saying that we should just leave it alone and let it be a cash cow. Even at 16 that did not make sense to me. I am willing to take a risk on a really good thing to be a part of a really incredible thing.

Sramana Mitra: Do you intend to raise money in Silicon Valley?

David Koretz: They key for us is to raise money from firms who have a security expertise. That is why I moved the headquarters to Silicon Valley. Development is still in Rochester which lets us have a great cost center, but we now have an emerging Silicon Valley culture in the company. We have great relationships with **Rochester Institute of Technology** and it is a great center for us to find talent. I have helped push RIT to be one of the first computing schools in the country to teach application security and it is an NSA center of excellence.

Sramana Mitra: What are some of the key lessons learned from your journey so far?

David Koretz: There is a difference in the risk profile in Silicon Valley. I was lucky in Rochester because everything I did worked out. Outside of Silicon Valley there is a low tolerance for risk. Outside of the valley companies don't fail, people do. I work hard to get people to accept that failure is part of the processes if you are truly innovating.

Sramana Mitra: Thank you for taking the time to share your story with us, I look forward to following your continued success.

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