Prepare for a Capital Raise: CROWDFUNDING

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Capital Raise

- Sales
- Gifts
- Debt
- Equity
Crowdfunding

- Raising small amounts of capital from a large number of sources
- Offshoot of “crowdsourcing”
Types of Crowdfunding

- Sales – Kickstarter
- Gifts – Indiegogo
- Debt – Kiva
- Equity – Earlyshares
Equity Options

- IPO
- Private Placement, the Maserati Model
  - Angel Investors
  - Exemptions
- New “crowdfunding,” the Hyundai Model
  - Facebook
  - Aunt Josie’s
JOBS Act

- Jumpstart Our Business Startups
- Increase capital opportunities
- Article III – CROWDFUND Act
  - Capital Raising Online While Deterring Fraud and Unethical Non-Disclosure Act
  - Relief, 4 years later
Private Placement

4(2)

Regulation D

- 504
- 505
- 506
Rule 504

- $1,000,000
- Investor worth limitations – none
- Investor number limitations – none
- Other qualifications
  - No general solicitation
  - Not freely tradable
- Not a “covered security”
Rule 505

- $5,000,000
- Investor worth limitations – none
- Investor number limitations – 35 non- “accredited investors”
- Other qualifications
  - No general solicitation
  - Not freely tradable
- Not a “covered security”
Accredited Investor

- $200,000 last two years and expectation of current year or $300,000 for couple
- $1,000,000 in assets excluding primary residence
- Businesses consisting of accredited investors
- Certain trusts, charities, control persons and benefit plans
Rule 506

- No dollar limitations
- Investor worth limitations – none
- Investor number limitations – 35 non- “accredited investors” who must be “sophisticated”
- Other qualifications
  - No general solicitation (JOBS Act revisions)
  - Not freely tradable
## Exemption Comparison

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Crowdfunding Exemption

- No investor worth limitation
- No investor number limitation
- Public solicitation and sale permitted
Funding Portals

- Online broker/dealer
- Flat fee
- Requirements
  - Investor review of terms and risk
  - Fraud risk reduction
  - Information to the SEC and investors
  - Escrow
  - Investment limits
  - Privacy protections
Individual Capital Limits

- Less than $100,000 annually
  - Greater of $2,000 or 5% of annual gross income
- Over $100,000
  - Up to 10% of annual gross income
  - Up to $100,000
Aggregate Capital Limit

- $1,000,000
- 12 month look-back
Issuer Qualifications

- Entity
- 4A(b) disclosures
- No “bad Actor” under Rule 262
- No publicly traded stock
- Not an investment company under 1940 Act
Required Disclosures

- Name
- Legal status
- Physical address
- Website address
- Directors, officers and 20% stockholders
- Description of its business
- Business plan
Description of its financial condition
  ◦ Aggregate offering amounts of $100,000 or less: tax returns and financial statements certified by the issuer
  ◦ More than $100,00 but less than $500,000: reviewed financial statements
  ◦ More than $500,000: audited financial statements
Required Disclosures (con’t)

- Description of the intended use of the proceeds
- Target offering amount
- Deadline to reach the target offering amount
- Regular updates regarding progress
- The price of the securities method for determining the price
Required Disclosures (con’t)

- Description of all securities
- Description of principals’ rights
- Name and ownership level of each 20% stockholder
- Potential future valuation methods
- Risks of minority ownership
Company Cons

- 10b-5
- 12(a)(2)
- Ongoing disclosure requirements
- Shareholder inspection rights
- Short form merger rights
- Oppression rights
Corporate formalities
  ◦ Shareholder meetings
  ◦ Director meetings
  ◦ Proxies
  ◦ Inspector of elections
  ◦ Rules of order
  ◦ Share certificates and transfer ledgers
Company Cons (con’t)

- Legal
- Accounting
- “Expensive” capital
- Dilution of economic/non-economic rights
- Future angel investors
Company Cons (con’t)

- Special cases
  - Family businesses
  - Contractual prohibition
  - Governmental prohibitions
  - Entity prohibitions
Investors Cons

- Illiquidity
- Dilution
- Minority status
- Discounts
- Risk / unawareness
Preparation for Crowdfunding

- Due diligence
- Business plan
- Market research
- Financial statements
- Amass network
Preparation (con’t)

- Executive team and executive team bio
- Corporate governance
- Corporate structure
- Commingling of funds
- Video
Pros

- Large customer base
- Large customer network
- Wide validation
- Annuity
Portals exist

270 180 90 60 30 ??? days until launch
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