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Opportunities for International Entrepreneurs and Investors

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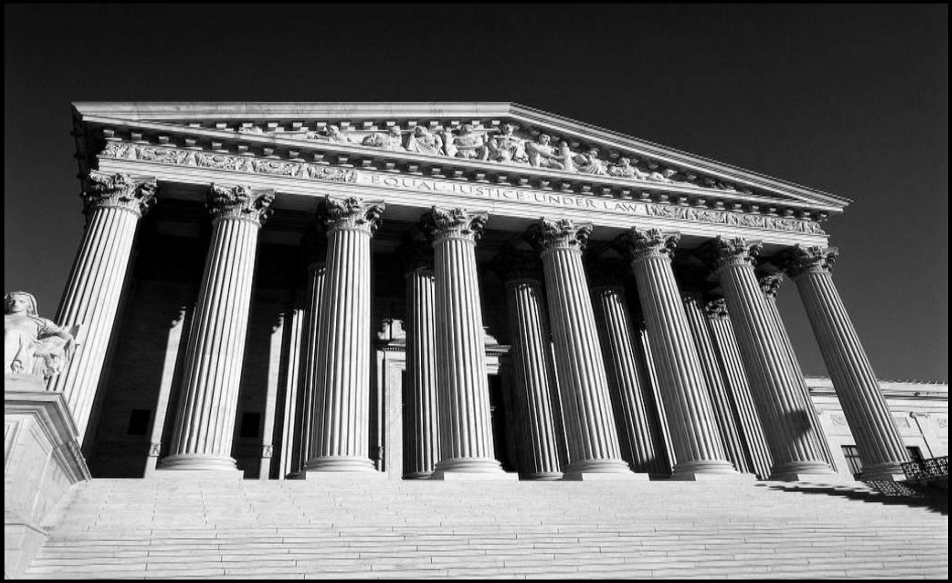
Starting Place: Registration Required

- All offerings must be registered with the SEC
- Unless, that offering is exempt from Registration
- Doesn't matter if small private sale or an offering which is immediately listed on the NYSE

Offer vs. Sale

- Offer triggers compliance requirements
- Compliance must happen <u>before</u> selling process starts



Private Offerings = Exempt

- Privately negotiated sales
- Must not involve any general solicitation or general advertising

- ***Section 4(2)* - the private-offering exemption*** - "<u>transactions by an issuer not involving any public offering</u>"

** Securities Act of 1933 (the "Securities Act")*

Requirements under Section 4(2)

The purchasers of the securities must:

- have sufficient knowledge and experience in finance and business matters to evaluate the risks and merits of the investment ("*sophisticated investor*"), or be able to bear the economic risk of investment;
- have access to the type of information normally provided in a prospectus; and
- agree not to resell or distribute the securities to the public.

Desire for Definition

- **Regulation A**
- Exempts public offerings not exceeding $5 million in any 12-month period
- must file an offering statement (called a "Form 1-A) with the SEC for review

Regulation D

- **Safe harbor** promulgated by the SEC under Section 4(2)
- Most common and today's focus

Reg D

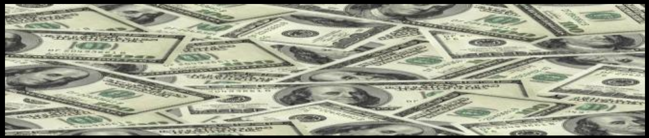
- Rule 504 provides an exemption for the offer and sale of up to $1 million of securities in a 12-month period
- Rule 505 provides an exemption for offers and sales of securities totaling up to $5 million in any 12-month period.
- Rule 506 provides another exemption for sales of securities under Section 4(2) with no dollar limit.

Rule 506

- Unlimited number of “accredited investors” and 35 “sophisticated” nonaccredited investors
- Popular if Integration is a concern
- Popular to comply with Blue Sky (National Securities Markets Improvement Act of 1996 (NSMIA) removed offerings under Rule 506 from state regulation)

“Accredited Investor”

- a bank, insurance company, registered investment company, etc.
- an employee benefit plan
- a charitable organization, corporation or partnership with assets ≥ $5 million
- a director, executive officer or general partner of the company selling the securities
- a business in which all the equity owners are accredited investors
- **a natural person with a net worth of at least $1 million**
- **a natural person with income exceeding $200,000 in each of the two most recent years or joint income with a spouse exceeding $300,000**
- a trust with assets of at least $5 million

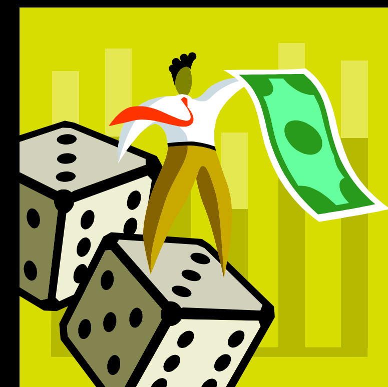


Why Only Accredited Investors?

- Private placement memorandum (“PPM”) that meets Reg D requirements = $$$$$
- If more than $1 million is raised in a 12-month period, Rule 504 is not available
- Under Rule 505 and 506, a PPM would be required to offer securities to nonaccredited investors
- Even if not required, delivering a PPM or at least a detailed business plan is probably advisable for liability and marketing reasons, particularly in fulfilling the antifraud requirement.

Initial Public Offering

- Registered with the SEC
- Underwritten
- i.e. Google, Rackspace...



Invest in Growing Operations and Revenue

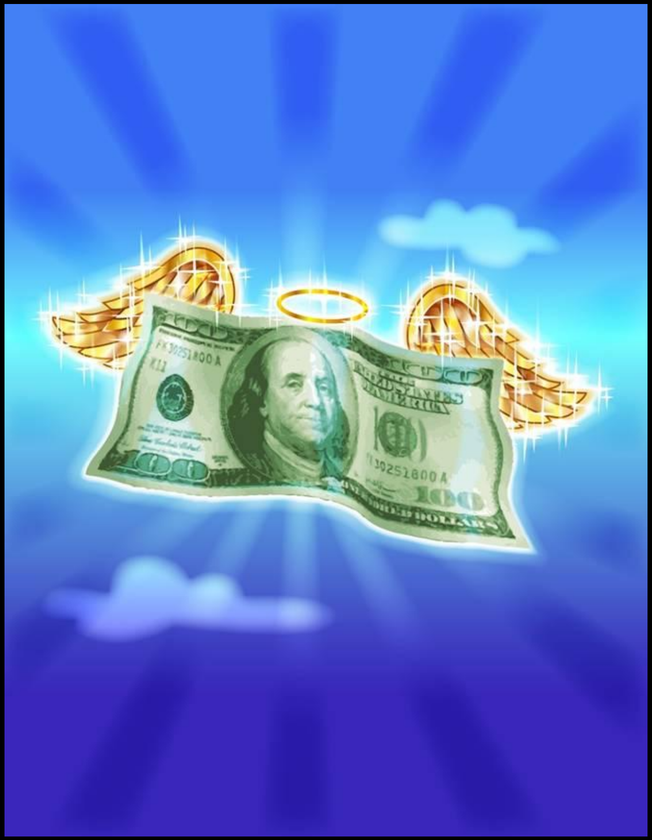
Traditional and Non-Traditional Lenders

- Most major traditional banks do not lend to startups/do so only rarely
- Comerica, Square 1 Bank, Silicon Valley Bank lend to entrepreneurial companies (positive c/f)
- Accts Receivable, Inventory, Fixed Assets
- Very sensitive to market conditions – this last down turn caused them to become risk adverse

- Terms may include: company's stock, fees, collateral, agreement to pay for AR audits, monthly reporting, audited financial statements, compliance reporting, financial covenants plus all banking relationships – checking, credit cards, investments, etc. must be with lender

Angel Investors

- **Friends and Family**
- **Angel Funding** – wealthy private individuals, with background in business, usually smaller than VC’s ($25K - $250K). They prefer to deal directly with the entrepreneur, like local deals, often want to develop a relationship with owners, they are limited in the number of investments they will do concurrently. Usually easier to deal with than VC’s. Invaluable to start-ups.

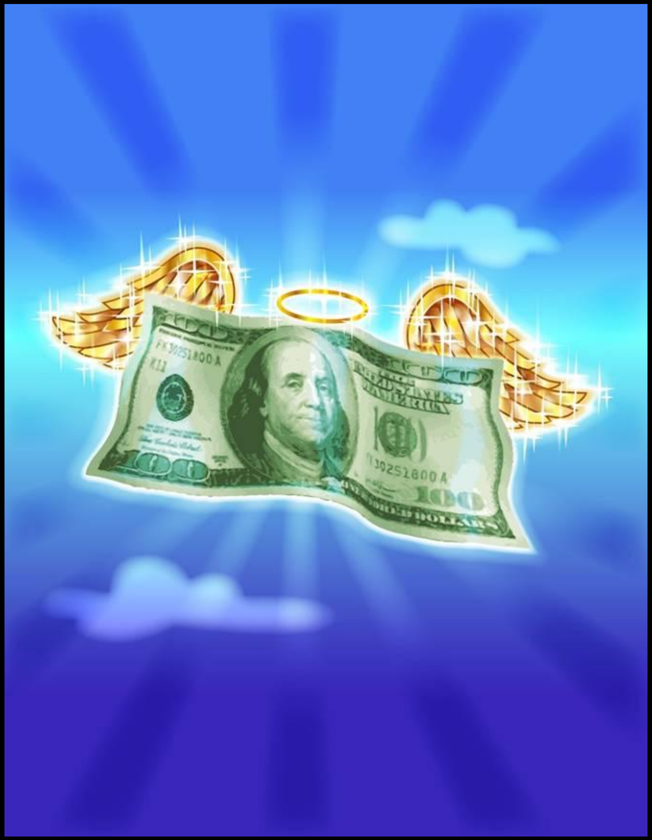


Must Still Comply with Applicable Securities Laws:

- **Exemption (“accredited investors”)**
- **Notice Filings**

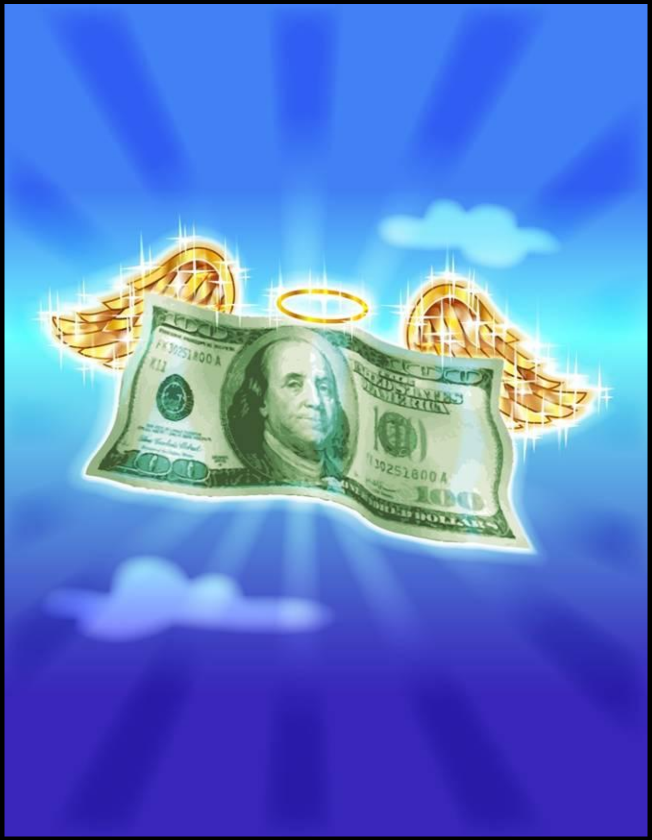
San Antonio Activity

- Targeted Technology Ventures
- First Capital Fund
- InCube Ventures and InCube Labs
- UTSA Entrepreneurship Lab
- STTM – Tech Transfer
- Angel Groups



San Antonio Activity – International Investors

- **Regulation S applies to investors outside of the US** **(… the terms *offer, offer to sell, sell, sale, and offer to buy* shall be deemed to include offers and sales that <u>occur within the United States</u> and shall be deemed not to include offers and sales that occur outside the United States.)**
- **Expect savvy startups to request data to comply with anti-money laundering diligence**
- **Direct Real Estate - FIRPTA compliance**



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Venture Capital ($1 million - $50 million)

Advantages

- Excellent source of capital / funding committed to your business
- VC's often are prepared to invest in continued rounds as the business grows and achieve it's milestones
- Bring valuable skills, contacts, experience and <u>discipline</u> to your business
- VC's have common goals with the entrepreneur – growth, profitability and increased value of the business
- VC's time horizon is often 3 – 7 years before exiting.
- Looking to have a 3 – 7 times return on their capital
- Exiting usually in the form of a Public Offering or Sale to a larger business after reaching certain milestones.

Venture Capital

($1 million - $50 million)

Disadvantages

- Raising Equity Capital – demanding, costly, time consuming. Your business suffers as you devote your time to answering questions
- Due Diligence process can be brutal – background checks, justification of your business plan, legal review, patent review, financial forecasts, etc (note: this can be a very useful process to force management to think through every issue. This is valuable even if funding doesn't occur)
- Often the entrepreneur will lose control after 2nd round of financing. VC's may want to bring in a marquee CEO, CFO, etc. to run the business.
- Management reporting to the VC's is often onerous, requiring 4 to 6 board meetings per year plus answering questions, providing updates and monthly reporting.

Grants

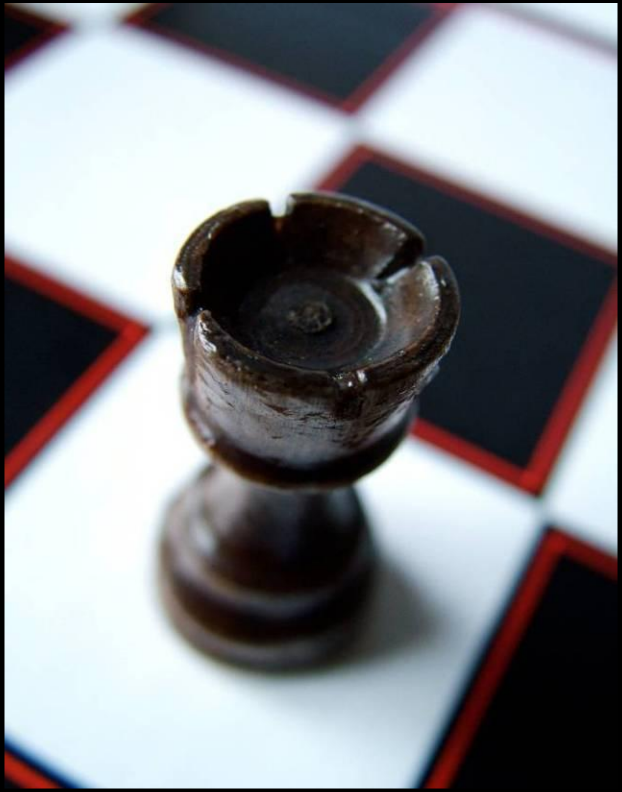
- GRANTS.gov
- STTR (Small Business Technology Transfer)
  - 5 federal departments participate
  - 0.3% of the relevant agencies' extramural research budgets
- CPRIT (Cancer Prevention and Research Institute of Texas)

Governmental Funds

- Texas Emerging Technology Fund (ETF)
  - Apply through Startech (South Texas)
  - Emerging scientific or technology fields that have a reasonable probability of enhancing this state ’s national and global economic competitiveness.

Strategic Partnering

- Strategic Private Investors/Partners
  - Large corporations
    - Potential Acquirors
    - Potential Customers



Getting Comfortable with Investor Terminology

- **NVCA Model Legal Documents**
  - – www.nvca.org - Model Legal Docs Button
- **Know Offering Terminology**

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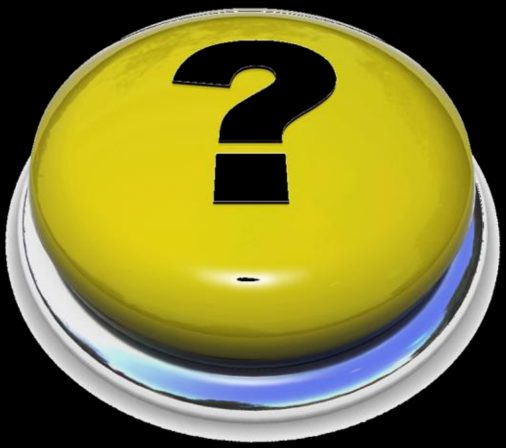

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