



## **“Investor-Readiness” for Start-ups**

November 2019

# Money is not Fungible:

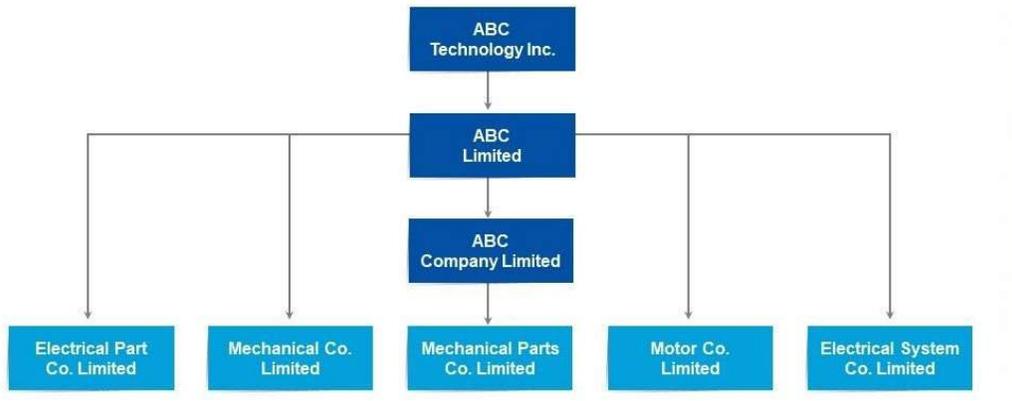
- Do not be desperate
- Do not undersell yourself
- Your friends and family may NOT be your friends
- Watch out for that person who wants to be a silent partner but turns noisy
- Contracts are your friends

# Business-Ready vs Investor-Ready:

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- Business plans, budgets, cap tables – easy for the business to produce.
- What an investor expects you to have ready.... VERY DIFFERENT.
  - 2 page Flyer
  - Marketing deck
  - Term sheet
  - Investment Information
  - Subscription document

# Corporate Structuring / Reorganization:



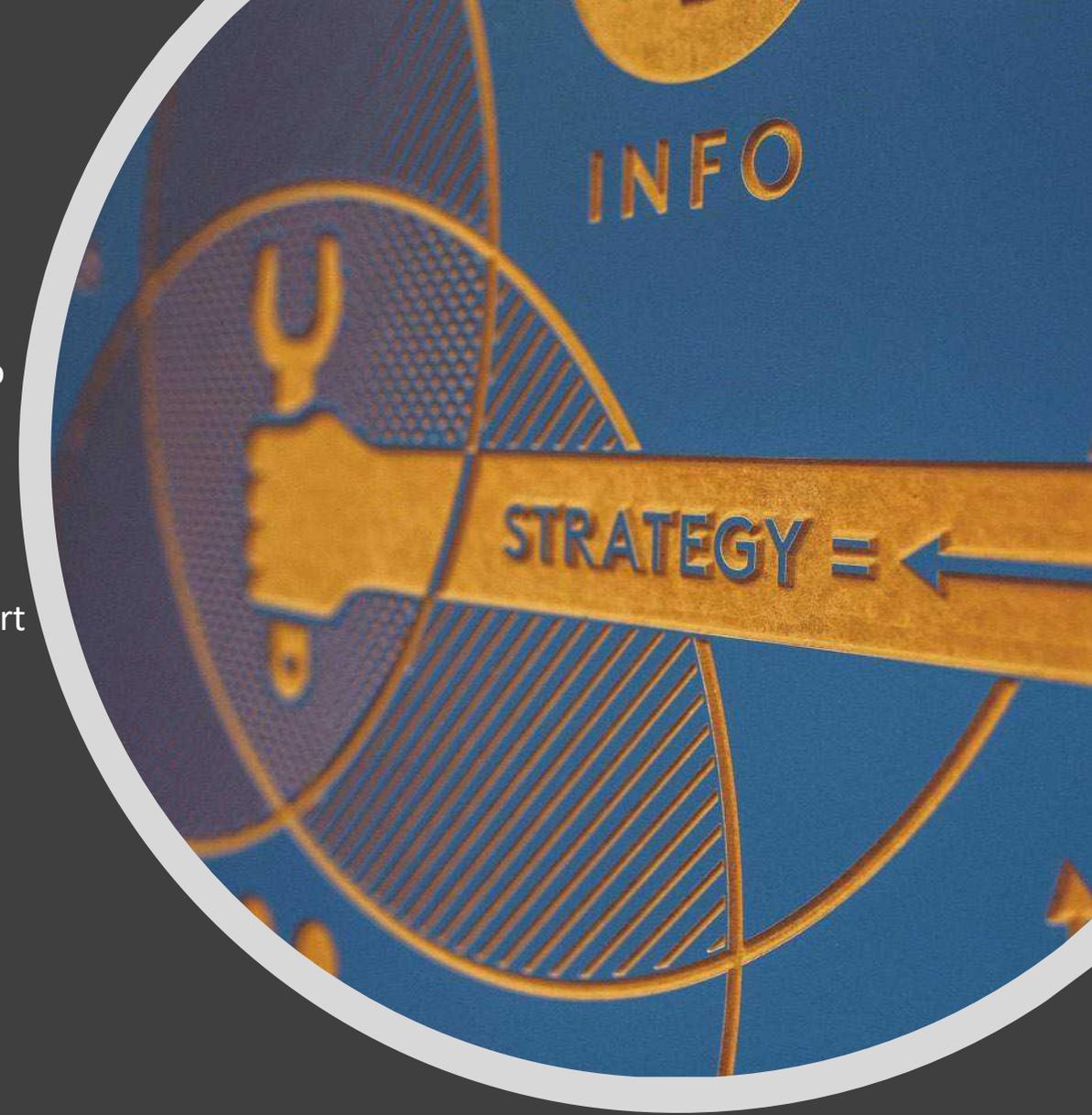
- Tax from the Investor Perspective
  - Taxable
  - Tax Exempt
  - Rest-of-world
- Protection of Assets
- Liability

# Record-keeping / book-keeping: *start NOW*

- Oral agreements vs *writing things down*
- Strategy:
  - How to use 'Memos-to-file'
  - Writing down agreements among founders / team:
    - who does what
    - who gets what
    - what happens in scenarios (departure, sale, buyout)
- Assume you will face an audit (tax; accounting):
  - FIAT / crypto recording procedures
  - payroll and expense procedures
- Diligence your proposed partners

# Marketing

- Marketing: Forget the fact that you can (and will) go to jail or be fined for marketing violations
  - You might think that risk is worth it, so I am not going to try to convince you
- BUT PLEASE REMEMBER: If you violate the rules, you show immediately how unsophisticated you are
  - This is like wearing an ill-fitting suit – if you don't LOOK the part you cannot play the part
- You also need the VOCABULARY – there is a language, use Google!
- Common example of what an investor will test you on:
  - Use of logos
  - Privacy
  - Proper sourcing of data/numbers
  - The dreaded BCP
  - Cherry Picking
  - Regulation S/Rule 144A
  - Investor types



# What is Due Diligence (and why is it happening to you!):

- What does the Investor want?
  - HINT: that you know your business from an OPERATIONAL standpoint
  - Start-ups fail ... and fail to raise because of sloppiness
  - Why would I give you money if you don't have basic items?
- Do not, under any circumstances, oversell yourself:
  - Example: "license" and "AIP"
  - Don't be afraid to be clear about where you are in the process – you are a start up, you are supposed to be starting up. If you had everything you needed, you wouldn't be a start up.





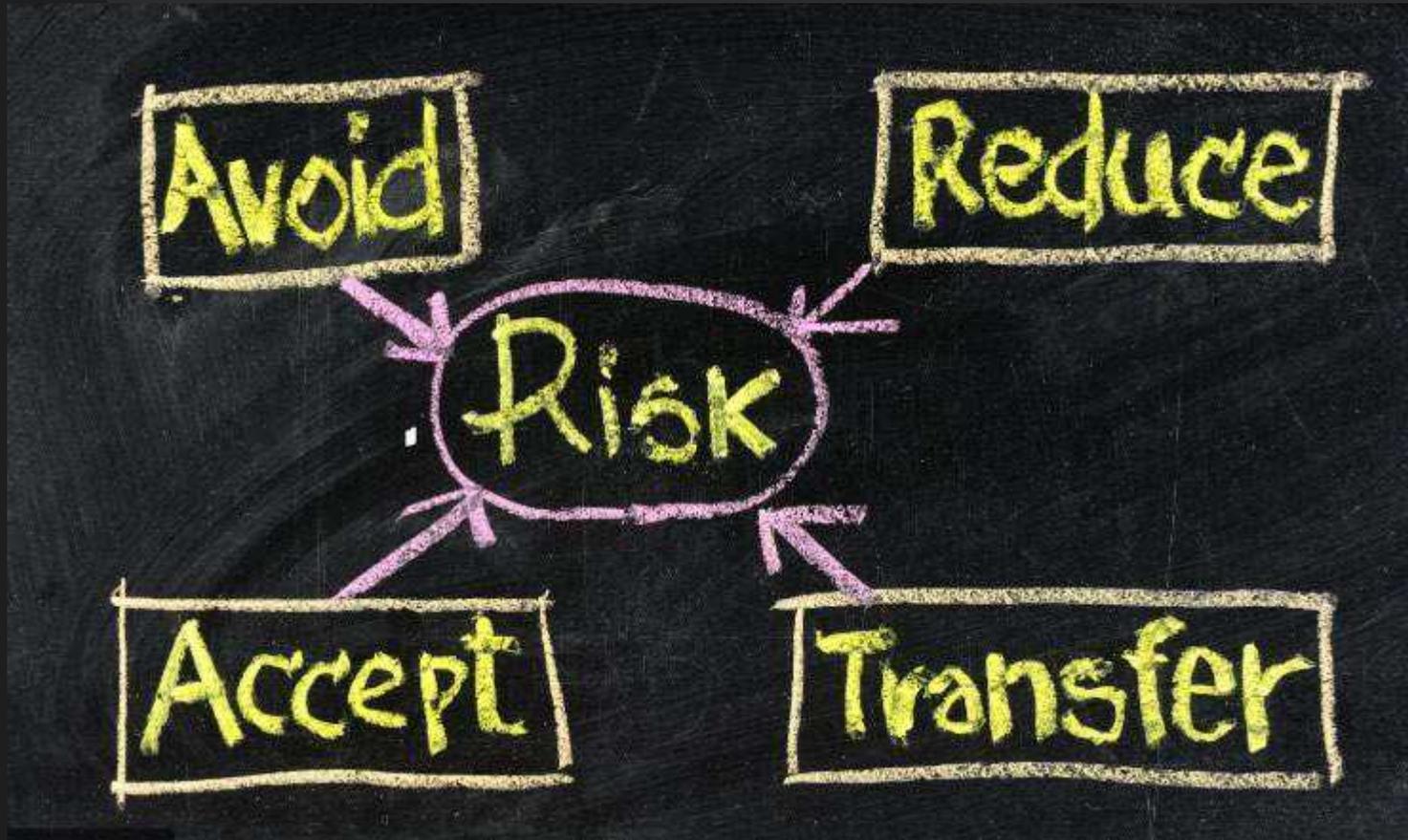
*Laws. These are all the ones you always forget and Investors know to test you on*



- Tax
- Company (partnership) law / fiduciary duties / liability
  - Unexpected requirements – insurance, display of registration
  - record-keeping requirements: texting is not a proper record
  - directors/shareholders/partner/member/manager resolutions
  - signing authority
- Employment law:
  - Immigration/minimum wage/vacation/discrimination/workplace safety laws
  - Employee vs contractor
- Privacy (learn about the “GDPR” and weep – change your websites NOW)
- Cybersecurity
- Bribery



# RISKS



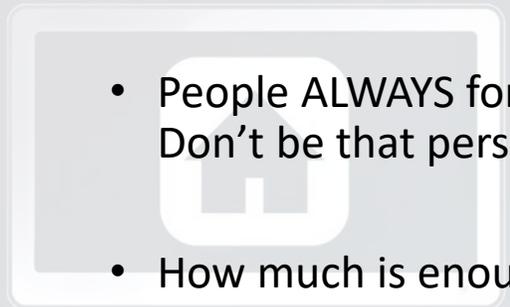
- Tax
- AML/KYC
- Business
- People
- Counterparty
- Data Protection

# The Investor Notebook:

- |   |   |
|---|---|
| <ol style="list-style-type: none"><li>1. Market Environment (for all Strategies)</li><li>2. Fund Organization and Structure</li><li>3. Fund Governance</li><li>4. External Consultants (PB, Custodian, Auditor etc)</li><li>5. Key Men and Track Record</li><li>6. Trading Team Members</li><li>7. Investment Strategies</li><li>8. Pre and Post Trade Compliance</li><li>9. Trade Error Procedure</li><li>10. AUM Allocation among Strategies</li><li>11. Accounting and Reporting</li><li>12. Regulatory Agency, Filings and Reports (Cayman, US etc)</li><li>13. Fund Expense Allocation</li></ol> | <ol style="list-style-type: none"><li>14. Fees per Strategy</li><li>15. Code of Ethics (for both Strategies)</li><li>16. Alignment of Interests for Team Members (per Strategy)</li><li>17. AML/KYC Arrangements</li><li>18. FATCA/CRS Arrangements</li><li>19. Cybersecurity and Privacy</li><li>20. Side Letter Key Terms</li><li>21. Compliance Program/Procedures and Processes/Training</li><li>22. Email and Electronic Communications Compliance</li><li>23. Counterparty Risk Arrangements</li><li>24. BCP</li><li>25. Litigation</li><li>26. Investor Complaints</li></ol> |
|---|---|

# AML/KYC

- Before the first cent/satoshi is accepted
- People ALWAYS forget AML/KYC: Don't be that person
- How much is enough?
- record keeping & filing system





# Money Control: Operational pitfalls

- Bank account controls: misuse of corporate assets
- Bank account strategy:
  - Types of accounts
  - What an Investor will expect of your bank account

# US SEC & YOU

- **No, you cannot avoid the SEC: search for SEC vs Scoville/Traffic Monsoon; Jan 29, 2019**
- **SEC v Scoville reaffirmed the Dodd-Frank Act two pronged test for the SEC to take jurisdiction: (a) if the wrongful conduct occurred in the US OR (b) if the wrongful conduct had a ‘foreseeable substantial effect’ in the US/on Americans (the infamous ‘conduct & effects’ test).**
- **Both prongs WILL get you. Is Youtube ‘in the US’/available to and often used by Americans? Is Paypal and American company? Where are your servers located if you use Google products?**
- **What if you have already violated the law? What should you do? Feb 20, 2019 – Gladius Network LLC:**

**The Securities and Exchange Commission today charged Gladius Network LLC with conducting an unregistered initial coin offering (ICO), which the company self-reported to the SEC.**

According to the SEC’s order, Gladius conducted an ICO in late 2017, after the Commission had warned in its DAO Report of Investigation that ICOs can be securities offerings. Gladius, a Washington, DC-based company, raised approximately \$12.7 million in digital assets to finance its plan to develop a network for renting spare computer bandwidth to defend against cyberattacks and enhance delivery speed. Gladius did not register its ICO under the federal securities laws, and the ICO did not qualify for an exemption from registration requirements.

Gladius self-reported to the SEC’s Enforcement staff in the summer of 2018, expressed an interest in taking prompt remedial steps, and cooperated with the investigation. The SEC did not impose a penalty because the company self-reported the conduct, agreed to compensate investors, and will register the tokens as a class of securities. The case follows the Commission’s two recent ICO registration cases, in which companies agreed to pay penalties for similar registration violations and agreed to similar undertakings.