Overview of Private Money financing

Raising private money from accredited or sophisticated (SEC terms/descriptions) is tightly regulated by the Securities Exchange Commission. This document is an overview of the process and requirements.

In order to be in compliance with the SEC requirements 3 things are needed in order to approach accredited investors/sophisticated investors (AKA wealthy individuals, groups of wealthy individuals, hedge funds, venture capital, etc.). These 3 things are a preliminary prospectus, private placement memorandum and a series 7 license. Raising money without these 3 things means that it is being done illegally. An example of this situation is Hemp Inc (google Hemp Inc. SEC violations) and there are thousands of other examples to look at also. All professional investors will require these documents to evaluate their interest in investing in a deal.

The preliminary prospectus is a business plan geared towards raising capital from professional investors and it is the supporting document used to create the PPM. The prospectus details all of the good and also details all of the risks. The risks are mitigated (if they can be mitigated) through breaking them down and finding the solutions to minimize the risk. The solutions and sources of the info used to mitigate the risk are cited and sourced. Five year financial projections, models and underlying assumptions that are prepared according to AICPA (American Institute Certified Public Accountants) guidelines are used to evaluate and support the financial claims asserted in the preliminary prospectus and the private placement memorandum that is presented to potential investors. When using AICPA standards to support and verify the financial modeling the info being presented to investors is accepted as factual. The AICPA standards are accepted globally.

The private placement memorandum is the legal document that is presented to investors to describe the investment as required by the SEC. It is a highly technical and living document that is updated and maintained throughout the course of the relationship with investors. The PPM chronicles and records all investments made and how they are agreed upon (notes, shares, ownership %, etc.). It is a complete record of investor money involvement.

A series 7 license is required to broker/sell investment opportunities and to approach investors and investor groups.

Process and key differences in raising capital

After the preliminary prospectus and the PPM are created then the capital raise begins. There are two ways to do a capital raise and one way is better than the other. Our group does it in the manner that is more beneficial to the client. If working with an equity funding group that group will typically only approach the equity markets and raise the capital from one or two sources and these sources will be straight equity. When doing it this way the investor groups will typically want to own 90% of the company (if there is not a significant personal investment by the client) and it is not unfair of them to want to do that since they did invest all of the money. They will typically expect a 25% annual return on the money invested and they will seek a buyout after 5 years.

The client can participate in the selling of the company after 5 years and exit with the investors or the client can buy the investors out with a new round of funding or from the profits accumulated from the business. This is the typical scenario of how things are done. Most equity funding groups will go directly to the equity markets and only raise money there because it is a "straight line" to the money and a faster and easier way for them to complete the cap[ital raise. They go to one source, get the money, deliver it to the client and then get paid the success fee. The client, who is unfamiliar and unaware that there is a different approach will not know any better and will be happy that they are funded. But, there is a better way to do it and it does not take additional time, only additional effort. We put in the effort so that our clients gets a better outcome.

Our capital raise approach and method

We will break the capital raise down into 3 phases and phase one will occur simultaneously with the creation of the PPM in order to maximize time savings.

- Free money in the form of grants, federal-state and local incentives, targeting opportunity zones and using Port Authority financing to obtain low interest rate government loans.
- Identifying and securing everything that the client can personally sign for using personal credit. Things such as real estate, equipment leasing/financing, lines of credit and other institutional financing programs.
- Equity financing/private investor money.

Breaking the capital raise down into three sections is a benefit for the client because the free money and the financing programs the client personally signs for will dilute the equity that the investors will ask for. Simply put, if an investor provides all of the funding for the business it is not unfair for them to want to have 90% ownership of the company and majority control. But, if the client/business owner contributes to the funding by securing a portion of the funding (1/3, ½ or more of the funding) then it is unfair for the investor to want to own the majority of the company. At that point, the group (Patriot BFC/Quantum) that is representing the client/business owners is in a stronger position to negotiate the equity that the investors are looking for to the benefit of the client. If they are only putting in a portion of the money then they should only receive a portion of the equity in the company. This equals a lower cost of money for the client, more ownership and less to pay out when the investor buyout occurs 5 years down the road.

Costs for the preliminary prospectus/PPM/Capital raise

These are professional services and they are upfront costs that must be paid in advance, much like when paying other professional services such as attorneys, accountants, advisors and medical professionals.

- $35,000 preliminary prospectus – 2 to 3 month time frame to complete
- $25,000 PPM – 2 to 3 month time frame to complete.
- $40,000 deposit to be credited to the success fee upon completion of the capital raise.
- This is a typical example above. Each deal is unique and the complexity of the deal and the amount to be raised may add to the initial upfront costs. The above deal is based on a $20 million dollar capital raise.

The capital raise will take 2 months or up to 6 months (after the legal paperwork is completed) depending upon the complexity of the project. The cost for raising capital is 7% to 8% of the money raised. Example: Raising $20 million dollars for the client will cost $1.4 million dollars if the success fee is 7%. This will equate to a $21.4 million dollar capital raise so that the client will net $20 million. We are only paid a success fee if we raise all of the money and the $40,000 initial deposit will be deducted from the success fee.

Why is a deposit required for the capital raise?

Raising capital is expensive and it requires that money be spent in the effort to raise the capital. If our group is in the 4th month of the capital raise and the client advises that he has the money secured and says thanks for the effort but I don't need it anymore then the expenses cannot be recouped. Minimum wage workers are not working on these types of deals and the staff that is employed to do this task is expensive because they are capable and experienced in raising large amounts of capital for existing and start-up businesses. Our fees, deposit required are typical to this industry and in most cases less expensive than others. We do not require a monthly retainer as some companies do and the deposit does not cover the expenses incurred during the capital raise. We are more than often "out of pocket" during the capital raise but this is ok, because we know that the end result will be a successful capital raise. We do not take deals on that we do not believe will end in success and we only accept deals that we know that we can accomplish successfully.

Process to engage for services

- Meet & greet/interview/evaluate. We have a phone call and explain the process to the client. We sign NDA's and then provide info on our partners, including their names, website, intro to Quantum PDF describing their business and introducing their the owners and their staff.
- If the client has the capital to go forward, we collect info and write a white paper/scope outline. These documents are forwarded to our partners and they evaluate the info for 7 to 10 days to determine if it is a project that they they feel will be successful. They will then create a proposal and a contract describing all of the services to be provided and the associated costs as described in the cost section above.
- We forward the contract and proposal to the client for their review and approval. We then set a zoom meeting for the client to meet our partners. No contract has been signed yet and there is no obligation.
- We have a zoom meeting and our partners will introduce themselves, describe their capabilities and experience as well as the process. The floor belongs to the client and the client can ask any question at all. Everyone becomes comfortable with one another and the process for capitalizing the company is the focus.
- The client can then make the decision to go forward, sign the contract and overnight mail the check. After receiving the check for payment, we will immediately go to work on the project.

- An additional step that can be taken is for the client to travel to Cleveland, Ohio and meet all of us in person before signing the contract and going forward. This is not required, but the invitation is open. Many people like to meet the people that they are doing big business with before engaging with a contract and we understand and appreciate that.

Deal parameters

- 5 million minimum up to over 100 million dollars for the deal size.
- Any industry is acceptable.
- No geographic limits.
- Professional services and the capital raise deposit are required up front or in stages.
- Personal investment by the client/business owner is beneficial. This can be in the form of money to be invested up front or money/resources that have already been invested by the client/business owner to get the company to the point that it is at right now.

Recap & overview

Capital can be raised for a startup business or an existing business in any industry. When raising capital, it must be done with strict adherence to SEC guidelines, rules, laws and procedures in order to avoid civil and criminal violations, we will only do it the right way.

When starting a business or capitalizing an existing business there are three ways to do it.

- Using personal funds.
- Using institutional lending programs.
- Using private/investor money and being SEC compliant.

Some types of businesses (startup/existing) can be capitalized with institutional lenders (SBA, equipment leasing, asset loans) but they will still require that money be invested/put down by the borrower. In the case of startup businesses this amount of money is typically 35% plus and there will be restrictive covenants governing the way that the money is spent and used. Additional collateral may also be required by the lender above and beyond the down payment money. Private money/investor financing is most often a more flexible and agile financial tool to use in order to get to the goal. Our method for the capital raise is unique and there are few, if any other companies out there that do it the same way, most companies that raise capital will go straight to the equity markets and complete the capital raise without involving any of the available "free money" (Grant money) or low cost money. They will also ignore the extra step of identifying and structuring the deal with available finance programs (Institutional lenders, banks, leasing companies) that the borrower can personally sign for such as real estate or equipment financing and this is to the detriment of the client. They complete it this way because it easier and faster for them to get the money from one source and they can complete the deal faster resulting in them being paid quicker for less work. We always take the better route and structure it so that the client receives the maximum benefit from the better deal structure.

Key terms

- Preliminary prospectus
- Private placement memorandum
- Securities and Exchange Commission
- Grant money, opportunity zone money, Port Authority money, All incentives available.
- Capital raise
- Success fee
- Series 7 licensing
- Fully capitalized vs just enough to get by for the startup/existing business
- Professional services
- 90% equity in company for capital vs less with a better capital raise structure
- 5 year buyout or sell with the investor/partners