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TechConnect

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Letter from the Editors

Dear Readers,

Our client, Benji Cohen, was running an Energy Markets Division at Macquarie when he had a lightbulb moment. Everywhere he looked valuation models were being put together in the most laborious way imaginable, with Excel tables containing hundreds of columns and thousands of rows. Benji saw a real point of pain in the marketplace and acted on it. Thus, in 2012, Benji created T-REX as a subscription-based, SaaS, FinTech platform that could compress the time for the valuation process to make the process 50 times faster and more accurate as well. And, the focus would be in a growing niche — the renewable energy sector. Benji was able to see the size of the opportunity, the point of pain in the marketplace, and the solution. With much hard work and great execution, T-REX is now a leader in this part of the FinTech space. In this edition of *TechConnect*, we highlight T-REX in our Innovator Profile.

Additionally, we talk about the progress of crowdfunding under Title III of the JOBS Act, which has now been fully effective for seven months, and the recent revisions to Rule 504 under Regulation D. We know that raising capital is incredibly important to emerging companies and we want to be a resource to our community on the various tools available for raising capital. Finally, we have included a terrific interview with one of the leading emerging companies' lawyers in Israel. No doubt Israel has been, and will continue to be, one of the centers of the technology revolution.

As always, we welcome your questions and inquiries and we invite all of you to visit our website for emerging companies @ **www.mintzedge.com**

Sincerely yours,

Dan + Sam

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- Daniel I. DeWolf
- Samuel Asher Effron

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Regulation Crowdfunding: A Six-Month Update

BY SAMUEL ASHER EFFRON

It has been seven months since issuers across the country began raising money through Regulation Crowdfunding ("Reg CF"), which went into effect on May 16, 2016. In the first six months after Reg CF went into effect, 160 initial filings for crowdfunding offerings on Form C were made with the SEC. The following summary of the highlights and trends is based on data collected from those Form C filings through November 16, 2016.

The General Landscape

First, the good news — despite the naysayers (including this author), a surprising, but still relatively small, number of issuers took advantage of Reg CF to launch 160 crowdfunded offerings, including six issuers who have launched two campaigns each. Of those campaigns, a total of approximately $13.5 million has been pledged or funded, with nearly $8 million raised in 32 successfully funded campaigns. Unfortunately, all of this is also the bad news — the success rate for Reg CF offerings so far is only 20%; that's not great. And the total amount raised in Reg CF offerings in this six-month period compares very unfavorably to the amount raised in Regulation D offerings during the same period, which is close to $30 billion. Further, of the nearly $8 million raised to date, over half represents just five issuers, with three of those hitting the maximum Reg CF offering amount of $3 million. That said, this is just a start, and the data from the first six months reveal some interesting trends that could give us a glimpse into how Reg CF will be used in the future.

Industry Focus

One of the big surprises about the types of companies utilizing Reg CF has been the high participation by, and success of, companies in the food and beverage industry, especially small breweries, distilleries and restaurants. Food and beverage companies comprised a total of 17.5% of all campaigns in the first six months of Reg CF, 28.13% of funded campaigns, by far the largest successful general industry category (with the closest trailing category being "Apps," representing 9% of all funded campaigns). It's possible that the affinity groups associated with food and beverage producers create a built-in audience for crowdfunding. Compare food and beverage's success with the experience of "tech" companies, including apps, online platforms and other technology-related businesses, which have fared particularly poorly with Reg CF — "tech" companies represent 25% of all launched campaigns, but only 12.5% of successfully funded campaigns. The most successful campaign so far, based on both amount raised ($1 million) and number of investors (a whopping 1,396 individuals), was fledgling movie studio Legion M.

Issuers

For a fundraising mechanism designed to assist small private companies to raise small amounts of capital, it is not surprising to discover that most of the companies utilizing Reg CF are relatively young. The median age of a Reg CF issuer is about two years, with almost 62% of all issuers formed since January 2015, and about 28% formed just since Reg CF went into effect! That said, there are some older companies utilizing this new method — about 20% are older than four years, and one issuer has been in business since 2003. The companies' geographic diversity is impressive — campaigns have been launched in 32 states and the District of Columbia. California represents the state with the most campaigns (30%), with Florida (10.6%), Texas (8.1%) and New York (7.5%) trailing a bit further behind. Interestingly, even though only 8.1% of all campaigns were launched in Texas, that state performed disproportionately well, with almost 22% of all successful campaigns.

Investors

Participation levels in the campaigns so far have been varied. While the average number of investors across the 122 campaigns that have disclosed their participation numbers is 79 (excluding two large outliers, including Legion M) and the median number of investors is 20 (same caveat), of that number, 20% have had zero investors, and 32% have had 10 or fewer. That said, the number of investors in a campaign does not correlate to its success — one successfully funded issuer raised its funds from just a single investor. Average investment amounts per investor across all campaigns and all successfully funded campaigns are about $950 and $1,200, respectively.

Platforms

To date, FINRA has approved 21 funding portals to host crowdfunding offerings, with 20 having hosted campaigns during Reg CF's first six months. Of those that have hosted campaigns, WeFunder is far and above the most prolific and successful so far, measured both by number of campaigns (nearly 38% of all campaigns are hosted on WeFunder's platform) and number of successfully funded campaigns (nearly 60%). This could possibly be first mover advantage, as WeFunder was one of the first portals up and running from Day 1 of Reg CF. It could also possibly be a result of competitive pricing — WeFunder generally charges a 3% commission on successful campaigns, whereas the vast majority of other platforms charge between 5% and up to 12%. About 16% of platforms, in addition to a commission based on a successful fundraising, also take some form of equity compensation. Other prominent platforms include StartEngine Capital (13.75% of all campaigns, but only 6.25% of funded campaigns), NextSeed US (4.4% of all campaigns, but a staggering 22% of funded campaigns and a 100% success rate), and uFunding Portal (11.25% of all campaigns, but 0% of funded campaigns), the last of which now has the dubious distinction of being the first Reg CF funding platform to be removed and banned from the FINRA list of approved platforms for failing to screen for potential fraud by companies using its services.

Offering Details

So, what are investors actually investing in? The three principal categories are equity (common and preferred), which accounts for over 50% of all campaigns, debt (straight debt, convertible debt and revenue sharing), which accounts for just under 25%, and SAFEs (simple agreement for future equity — a convertible note-like instrument gaining acceptance in recent years), which were offered in 25% of offerings. What is interesting, though, is that SAFEs were sold in over 40% of successful campaigns, whereas equity was offered in only 25% (comprised of 6.25% preferred stock, and 18.75% common). Further, it is somewhat unusual for SAFEs to be the preferred "security" of choice, both because many of the companies offering them may never actually reach a "qualified financing" in which the principal amount of the SAFE converts into equity, and also because many of the SAFEs have a built-in redemption feature which permits the issuers to repurchase any equity securities into which the instruments are convertible. Neither of these are investor-friendly features. Of the debt securities offered in successful campaigns, only one campaign offered a convertible note — the rest were split evenly between revenue sharing arrangements and straight debt.

Looking Forward

So, what do the six-month numbers tell us about Reg CF so far, and what we can expect in the future? There certainly seems to be an audience for food and beverage offerings, which is promising for small breweries, restaurants and distilleries hoping to make a go of it. And companies with low capital needs may be well served by a Reg CF campaign so long as the expenses are not disproportionate to the amount raised. On the other hand, for tech-based companies that have traditionally relied on venture capital and angel investors, the data suggest that it is still easier, less expensive (proportionate to amounts raised) and less burdensome from a public disclosure and reporting perspective to continue to raise money through Regulation D private placements. On the platform side, WeFunder appears to have a strong, early lead over competitors, but SeedInvest (an established private placement platform) and IndieGoGo (a brand name in the awards-based crowdfunding space) have both entered the arena and could be formidable challengers to WeFunder's supremacy. For now, Reg CF offers another, potentially limited, tool in the fundraising toolbox. With a new incoming administration and SEC Chairperson, changes to the rules might also adjust the regulation in a way that will make it more useful to companies, and more accessible to investors.

Innovator Profile

T-REX

Founded in 2012 and headquartered in New York City, T-REX's secure, enterprise SaaS-based analytics, risk, and portfolio management platform standardizes and provides transparency to the complex structured products evaluation process, increasing liquidity and creating significant investment opportunities for the hundreds of billions of dollars of capital across various esoteric, non-commoditized asset classes.

T-REX has demonstrated its proof-of-concept in markets for solar and Property Assessed Clean Energy (PACE) financing: increasing standardization and efficiency, while lowering costs and compliance needs. Before T-REX, the value of the assets was opaque, non-standard, and manually evaluated one asset at a time. With T-REX, developers, asset managers, and institutional investors can now efficiently invest in, securitize, and manage portfolios of renewable energy assets with complete transparency. Further, T-REX takes structured asset deal sharing to a whole new paradigm, enabling secure, swift, and dynamic information sharing capabilities whereby users can granularly stress the impact of asset-specific risks on the capital structure.

T-REX's vision is to provide the financial infrastructure for the renewable energy asset class and expand the platform benefits to esoteric assets, a $12 trillion market globally. Once T-REX is the lingua franca between developers, investment banks, credit-rating agencies, institutional investors, and key market participants, T-REX will act as a marketplace for transactions, thereby facilitating price discovery and increasing liquidity. By 2021, the market for structured product analytics tools is expected to exceed $1.4 billion. T-REX is addressing this opportunity by aggressively targeting global financial institutions, asset managers, and developers. Today, at major financial institutions, there are fragmented, non-standardized software solutions that are currently being used across the majority of asset classes, giving T-REX a meaningful opportunity to streamline and diversify its initial product offering. As software spending on financial markets infrastructure for structured products increases, additional asset classes will be targeted for development.

"In 2016, we have attained more than 150 end users and established influential industry partnerships, including Morningstar Credit Ratings and Renovate America," says T-REX Founder and CEO, Benjamin Cohen. "In addition, we have achieved key product milestones and developed a repeatable go-to market strategy that has already helped facilitate hundreds of millions of dollars of new capital for our clients. The T-REX platform increases standardization, promotes efficiency, prioritizes transparency and enhances compliance, all while lowering costs for our customers, which include a global set of investors, bankers, and finance professionals."

In November 2016, T-REX announced its $10 million Series B fundraising round led by enterprise VC firm, Safeguard Scientifics, which will be used to expand its product capabilities, enter new markets, and scale its client development and engineering teams. The funding capitalizes T-REX to leverage its expertise and market presence in PACE and solar markets to scale its valuation, structuring, and portfolio management platform across esoteric and non-commoditized asset classes.

"To date, T-REX has demonstrated proof-of-concept in its beachhead markets — solar and Property Assessed Clean Energy ("PACE") — which we believe is instrumental as the company looks to replicate its technology on a much broader scale," said Tina Aufiero, Managing Director at Safeguard, who will join T-REX's Board of Directors. "T-REX was founded with the mission to alleviate critical pain points in building valuation models and enabling more efficient and informed decisions in financing starting in esoteric, non-commoditized asset classes. With Safeguard's refined focus on deploying capital in technology-enabled businesses, particularly within financial services, Safeguard recognizes the opportunity to close the gap for financial markets infrastructure and SaaS-based analytics in a rapidly-evolving structured products landscape."

Attorney Interview: Yuval Horn, Co-chair of the IBA Technology Law Committee and Founder of Horn & Co.

As part of our outreach to provide legal services to companies engaged in the emerging growth industries internationally, Mintz Levin has developed relationships with leading law firms across the globe. In this issue of *TechConnect*, Mintz Levin's Daniel Harary and our former colleague Merav Gershtenman interview Yuval Horn, founder of Horn & Co. and Co-chair of the Technology Law Committee of the International Bar Association (IBA) conference which took place in October in Tel Aviv.

Can you describe, generally, the focus of your practice?

Horn & Co. is a leading Israeli boutique law firm in the field of hi-tech and life sciences, and is unique in its exclusive expertise solely in this field. Our firm includes 16 lawyers and three clerks, who focus on two main areas of activity of tech companies: technology transactions (licensing, joint development, distribution) and corporate finance transactions (private and public funding, M&A).

How do you think financing in the life sciences sector differs from other industries? What is the value of having attorneys experienced in this sector?

Life science companies require significant funding for the completion of their research and development programs. Funding of such companies is typically sought from professional investors and from governmental bodies. Therefore, while the agreements are similar in structure, the funding processes require the ability to analyze intellectual property agreements in order to verify that the relevant rights are secured by the company. They involve the need to understand limitations imposed by governmental and academic institutions on the use and commercialization of IP. In addition, as companies reach situations in which they cannot seek sufficient funding for their programs, they seek alternative means of funding, including by way of commercializing their assets. Our firm represents dozens of life sciences companies, and several prominent investors in the field. The fact that our firm represents some of the most active and significant life sciences investors in Israel provides us with extensive exposure to a majority of the financing transactions being discussed or consummated in this sector, resulting in an in-depth acquaintance with industry standards as far as financing terms and investors rights are concerned. This attribute often proves to be of great value to clients, especially early stage companies and founders.

What were some of the unexpected challenges of launching your own firm — in effect being an entrepreneur, yourself?

We launched our firm with eight lawyers and a strong belief in our business acumen, that clients require personal attention, not firm size. Seven years later, our firm has more than doubled in size. The main ongoing challenge is to keep our focus on the ideal of the firm — to work with the clients that we appreciate, with the same atmosphere and high level of work. Also, as the firm has grown, the managerial challenges change — the staff grows, the office space and budget have increased, and they all require increased maintenance. The balance between these obligations and my desire to focus on working with clients is the continuing challenge.

What should emerging growth companies look for in selecting counsel? What makes a good match?

Companies should verify they pick a team that may assist them. Expertise in the specific areas in which they seek assistance is of utmost importance. A dedicated team is also more cost effective. A good firm will make a point to accept business that fits into its areas of interest and expertise and should refer a client to other firms when the client requires expertise that the retained law firm does not have.

What are the main differences in structuring transactions with Israeli companies as opposed to US corporations? Are the landscapes becoming more similar or drifting apart?

The formats of transactions are becoming similar. We often work with US-based formats even when negotiating an Israeli transaction. I think that the one main difference is the importance of legal counsel in the business discussions. Since Israel is a small country, we are often asked about deal terms and fairness, much like business advisors, in addition to the requirement that we draft and negotiate the documents. Many Israeli lawyers serve as trusted advisors with respect to the deal terms, not only with respect to the negotiation of the documents.

What are some of the toughest challenges you foresee for Israeli and international clients doing business in the US in 2017?

During 2016 we have seen the decreased appetite for public financing of younger companies. If the market will remain unreceptive, companies will need to seek alternative ways to obtain funding for their operations. We have seen an increase in private funding of companies in Israel this year. The unknown effect of the US elections also remains a big question mark, although Israeli technology succeeded in US market penetration throughout the years regardless of the political situation. Furthermore, we noted a recent increase in the valuations and appetite of biotech companies. I truly hope that both phenomena will remain the same in 2017 and on.

What is your role and involvement with the International Bar Association (IBA)?

I currently serve as Co-chair of the IBA Technology Law Committee. Our committee includes hundreds of lawyers from all over the world who represent and advise technology-based companies in their businesses. Prior to my nomination as Co-chair, I served in various officer positions in our committee. Four years ago, I was one of the founding members of the IBA World Life Sciences Conference, and have been part of the organizing committee since. We meet on an annual basis, and discuss issues that interest life science companies, from financing, through technology transactions, to IP and compliance issues. Finally, I was one of the co-organizers of the IBA 2nd Annual M&A in the Tech Sector Conference, held in Tel Aviv in October. In 2017, I am scheduled to moderate a panel on the future of apps at the IBA Silicon Beach Conference.

Featured Article

REVISED RULE 504: ANOTHER TOOL IN THE TOOLKIT TO RAISE CAPITAL

BY DANIEL DEWOLF AND BRIAN NOVELL

If there is one common theme that entrepreneurs tend to have, it is fire — meaning, many entrepreneurs are passionate about an exciting idea that they seek to turn into a business. However, entrepreneurs often quickly realize that, in order to make their fire glow high and bright for the world to see, they need fuel — meaning, capital. While bootstrapping is a smart practice that can keep the embers burning for a period of time, even fantastic ideas will likely sooner or later need a major capital injection — thereby adding fuel to the fire — to take the venture to the next level. This is where the newly revised Rule 504 of Regulation D may be a good option for early stage companies. For qualifying companies, Rule 504 provides an exemption from the registration requirements of the Securities Act of 1933, thereby facilitating the ability of startups to raise capital. Often well-suited for friends and family or seed rounds of funding, Rule 504 provides flexibility to smaller companies seeking assistance with capital formation.

The Rule and the Changes.

On October 26, 2016, the SEC adopted final rules that amend Rule 504, thereby increasing the maximum offering amount permitted to be raised from $1 million to $5 million, which will be effective as of 60 days following publication in the Federal Register. The SEC noted in the adopting release that Rule 504 had been underutilized due to the previous low offering amount limitation. The main benefit of this new increase is that more small businesses will be able to rely on Rule 504, as it will now be in the consideration set for certain companies seeking funding of up to $5 million. Entrepreneurs may then find themselves asking, “Is our company eligible for exemption under Rule 504, and does Rule 504 make sense for us?”

The Fine Print.

In order to be eligible for Rule 504, a company must not yet be required to file reports under the Securities Exchange Act of 1934, and must not be a “blank check company,” meaning that most early-stage companies with a plan for an operating business are eligible. What is unique about Rule 504 is that it (i) provides significant freedom in how one goes about raising the capital, and (ii) permits resales of shares with less friction. Offerings under Rule 504 permit, under certain circumstances, general advertising and solicitation; and, further, the requirement that the securities be restricted from subsequent resale will not apply to offers and sales of securities when following certain requirements.

Is Rule 504 the Right Choice?

While potentially a new tool to raise capital, Rule 504 should be evaluated in comparison to other options for exemption. Over the last decade, the use of Rule 504 offerings had been in decline, both in absolute terms and relative to Rule 506 of Regulation D. Rule 506 provides two potential exemptions from registration. First, Rule 506(b) has no limit on the amount of money that may be raised or the number of accredited investors that may be purchasers, though general solicitation or advertising may not be used and a company may not sell securities to more than 35 non-accredited investors, among other requirements. Second, under Rule 506(c), the SEC eliminated the prohibition against general advertising, provided that all purchasers are accredited investors and the issuer takes reasonable steps to verify so, among other requirements.

What Does It Mean for Entrepreneurs?

The increase in the maximum amount that may be offered and sold under Rule 504 allows for more companies to potentially leverage Rule 504 for their capital raising needs. In light of this recent development, Rule 504 may be a good choice for many early stage companies. It is another tool in the toolkit to consider when raising capital.

Upcoming Events

New York

January 10: Brunchwork with Foursquare
January 13: Nintendo Switch Presentation
January 18: Private Equity International CFOs and COOs Forum
January 18-19: AdExchanger's Industry Preview
February 23: Health & Bio Technology Summit

Boston

January 25: Climate Preparedness in Massachusetts
January 26: MITX Influence(her)
January 31: Boston Accelerators: Navigating Your Options
February 2-3: 2017 LearnLaunch Across Boundaries Conference
February 8: MITX eCommerce Summit 2017
February 23: Tech in Motion: Cybersecurity & Industry Vulnerabilities: A Fireside Chat

San Francisco

January 23-24: Corporate Venturing 2 Day Program — Silicon Valley
January 31 - February 2: DesignCon
February 1-2: Mobile Growth Summit
February 6: 10th Annual Crunchies Awards
February 6-8: SuperReturn US West 2017
February 7-10: Venture Capital Unlocked: Deal Camp (500 Startups and UC Berkeley) February 21-23: Container World 2017
February 28 - March 1: Venture Summit West

San Diego

February 2-3: Third Annual Emerald Conference — Exploring the Science of Cannabis
February 21-22: Illuminate Education User Conference: California IEUC 2017

Washington, DC

January 26: Tech in Motion: New Year, New Connections!

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