



## THE PROCESS OF RAISING MONEY

On the following pages we have broken down the standard steps when raising capital into their component parts. *(This is designed to be only a general discussion of the process and implementation can be somewhat more complex.)*

When reviewing the following material please keep in mind that Rule 144+ prefers to approach this process in two distinct stages. The first stage is centered on those areas (Steps 1-4) that can be accomplished for the least amount of cost. Thereafter, if appropriate, Steps 5-7 (by far the most expensive steps) can begin, provided project management is comfortable with moving forward. By approaching the process in this manner costs are kept low during the early development stages when there is the greatest uncertainty. In addition, maximum flexibility is maintained should there be a need to change direction, adjust a project's scope, etc., or should market conditions change and require adjustments in the base financial structure.

### OUTLINE OF BASIC STEPS TO RAISE CAPITAL

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|--------------------------------------|---|
| <b>1. Develop Concept</b>            | Determine the scope of the project and determine if project is worth pursuing – initial due diligence   |
| <b>2. Select Management Team</b>     | Determine who will own and control the project  |
| <b>3. Gather Information</b>         | Accumulate information for the Business Plan section of the Offering Memorandum.  |
| <b>4. Prepare Business Plan</b>      | Prepare rough draft outline of everything related to the project including project business, industry background, management, risk factors, etc. This material will be given to the law firm as the basis for the formal Offering paperwork |
| <b>5. Prepare Offering Paperwork</b> | Prepare specialized paperwork that is given to potential investors. (Accomplished by a major law firm)  |
| <b>6. Market the Offering</b>        | Either “self underwrite” the Offering or market through an Underwriting firm (usually a major brokerage firm)   |
| <b>7. Close</b>                      | Transfer funds and begin project  |

### NARRATIVE OF STEPS

#### STEP 1 DEFINE PROJECT CONCEPT AND SCOPE

To begin the process, one would need to determine the breadth of the project's scope including what will be included or excluded, what areas will take precedent over others, and finally, what components will be added in the future that are not part of the project initially.

This step of the process may take a number of meetings and should not be rushed. Decisions here impact all future steps.

The preliminary process typically includes: (1) brainstorming short, intermediate, and long term goals, (2) discussing the scope of the initial project and where one anticipates it will go in the future, (3) assessing the amount of capital that may be required, (4) determining project management responsibilities, (5) accumulating basic research and support documentation, and (6) roughing general financial projections explaining how income is to be produced and how profits are to be shared with potential limited partners/investors.

The step also enables an organization to accumulate further education related to the financial concepts that may be used and the future steps required.

### **STEP SELECT MANAGEMENT**

Most projects can be judged as to their ultimate success by evaluating the management of the project. It is the area that is most often scrutinized by investors and therefore requires the most care in assembling. While an organization may have a number of solid managers, key employees, and other administrative leaders, what is needed are to identify individuals who will own the project, manage the project, and act as a Board of Directors. Combined, all these groups should encompass the following:

Substantial Industry Experience - including individuals who have owned, managed, or been key individuals in successful companies

A Proven Track Record - in a sector of the industry that is germane to the project

Proven Leadership Skills - in industries that may or may not be related, but can easily be carried over to the project

Strong Reputations - for business acumen, achievement, and integrity

Well Connected to Major Institutions - such as banks, investment brokers, industry organizations, etc.

Well Connected to Professional Organizations - such as law, brokerage, accounting, and advisory firms.

Selection of management personnel is critical to the project's success, and therefore should be taken with the utmost care, regardless of the length of time it takes. The key to selecting management will be the ability to judge the potential participants impact on investors.

### **STEP 3 GATHER INFORMATION**

In order to save time and money, it is important to gather as much information about

the project to be funded as possible. Business plans, management resumes, contracts, news releases and articles, testimonials, research reports, industry trade reports, brochures from competitors, etc., will all be accumulated and made available for review by the project managers identified in Step 2.

#### **STEP 4            PREPARE A “ROUGH DRAFT” DISCLOSURE DOCUMENT**

Raising funds from any source requires that an organization describe the details of its project in writing. This document, sometimes referred to as a “Disclosure” document, comes in various forms depending upon who is being approached. The disclosure document describes the business of the company, the underlying company’s financial structure, its management experience, how the company intends to spend the money, and ultimately how the whole process will benefit those who may be putting up the capital.

Our approach is to create a “rough draft” document, prior to submitting material to the attorneys who will then be charged with creating the final offering Memorandum (see Step 5). By so doing, many of the problems can be worked out ahead of time – before the attorneys get involved. This saves time and money and will make the next step more productive.

In order for a fund-raising effort to be successful, the “Disclosure” document must address four main factors that are of concern to potential investors:

##### The Required Factors

Application of Proceeds	How is the investor’s capital utilized by the company or project?
Profit Potential	How is potential income and profits shared with the investor?
Risk	What are the risk factors associated with the investment?
Exit Strategy	What options do the investors have to “exit” out of the investment?

As investors are regularly approached by organizations looking for funding, eventual success in raising capital will tend to be in direct proportion to how well project management can answer these investor concerns in the disclosure document.

##### Adding Value

In most fund-raising situations, the company or project is the **only** factor investors have to consider when deciding to make an investment. The problem is that investors are typically left to judge the company’s projections based on and representations of the management who may not be known to the investor. Investors also recognize that there may be an inherent conflict of interest between the company and the investor when it comes to the participation percentage that is offered for investor dollars. *(The conflict comes as a result of companies wanting to give up less equity for more dollars, whereas investors usually want to give up fewer dollars for more*

*equity.)*

However, our proposed approach, which combines Restricted Stock Utilization and Preservation of Principal features, makes an offering substantially more attractive to investors. It also enables the project to raise larger sums without having to offer as much equity to the investor as would otherwise be required if there were no assurances of a return of principal. In addition, these conservative concepts may represent deciding factors in motivating investors to capitalize a project. Each characteristic enhances the competitiveness of the company's offering over other offerings that do not have such features, and each one makes the total package more appealing, and less risky.

#### **STEP 5 PREPARE A FORMAL "DISCLOSURE DOCUMENT"**

While an offering can be made without a formal disclosure document, it would be impossible to raise substantial funds without the assistance of qualified legal counsel. Therefore, once the project manager has completed the above steps he or she will have to choose the legal counsel that will prepare the final documents and attach the necessary "legal opinion" to the disclosure documents. While very costly, this step eliminates liability (short of management malfeasance) and provides the underwriter and investors with a comfort zone that everything has been done according to the law.

The following are the typical documents that must be prepared:

#### **Private Placement Memorandum**

A Private Placement Memorandum (PPM) is the document that discloses everything the investor needs to know in order to make an informed investment decision. This includes: the offering structure, SEC required disclosures about the securities being purchased, company information, risks involved with the investment, terms of securities being sold, management information, use of proceeds, information on certain transactions that could affect the investor, and investor suitability data.

PPM's can be designed as a stand-alone document - there need not be other information presented to the investor for them to make an accurate investment decision. Many companies will attach their business plans to the PPM as supporting documentation. This is an acceptable practice so long as the information in the business plan properly corresponds with the information in the PPM and that the investor is made aware that the business plan alone does not constitute an offer to sell securities - only the PPM can make that offer.

#### Key Sections of the PPM

The specific disclosure items included in a PPM will vary depending on the size of the offering and nature of the investors. Key categories of disclosure items might include:

Description of the Company  
Risk Factors

Capitalization of the Issuer  
Management of the Company  
Terms of the Offering  
Use of Proceeds  
Dilution  
Description of Securities  
Financial Statements  
Exhibits

### **Management Agreement**

The Management Agreement describes how the management company will operate and function as the manager of the overall project.

### **Partnership Agreement**

The Partnership Agreement describes the relationship between the Holding Company, Management Company and the Limited Partners.

### **Subscription Agreement**

The Subscription Agreement outlines how the investor will acquire partnership interests and that the investor has read the prospectus, is aware of the risks, is over 21 years of age, understands the restrictions on future sale, and has completed the signature and power of attorney page. The investor may also be required to fill out a suitability questionnaire to determine his or her qualification as an accredited investor.

### **Escrow Agreement**

The rules applicable to offerings require the maintenance of an escrow account. In general, monies or securities paid for the purchase of partnership interests must be returned to the investors if the offering has not reached its capitalization goals within a specified time. Also, the funds or securities received from investors must be deposited into a separate segregated account and held for the investors' benefit until the terms of the offering have been complied with. If the terms of the offering are met, the securities or funds are transmitted to the issuer. If not, they are to be returned to subscribers.

## **STEP 6 MARKETING**

There are a number of ways to market an offering to investors, from direct marketing to the use of a major underwriting firm. Each method requires a level of expertise and has benefits and drawbacks. The problem with the typical marketing method used by most organizations is that marketing occurs after the first five steps. By waiting until the disclosure documents have been completed, organizations run the risk of marketing an issue that may not be acceptable to the investor.

We tend to recommend the implementation of a pre-stage to marketing. Rather than wait

until the disclosure statement has been completed, management should begin to discuss the potential offering with interested parties during early development stages. In certain states this process is made even easier. Regulatory exemptions such as “Test the Waters” allow organizations to approach certain investors with an abbreviated Memorandum that describes the future offering and enables management to secure indications of interest from potential investors. This also allows management to hear suggestions that may make the offering more attractive and to customize the offering based upon the known needs of the potential investors. In addition, if it becomes apparent that an offering would not be accepted as planned, management has the option of altering the approach prior to assuming a final course of action. This saves time and money while allowing for a more stable administrative planning process.

Once the pre-stage to marketing has been completed, and the legal team completes the offering Memorandum, the package will be ready to market to investors.

There are two ways to market an offering.

#### Utilization of a Full Service Underwriting Firm

In the utilization of a full-service underwriting firm (usually a brokerage firm), the underwriter markets the issue to their existing investors. As such there are few complexities other than determining the firm to be chosen, negotiating fees, and determining the willingness on our part to adhere to the requirements the underwriting firm may impose on project management in order to market the package.

#### Self Underwriting

Self Underwriting is a process where the company underwrites the issue through their own efforts, thereby bypassing the use of an underwriting firm. The marketing strategy includes approaching attorney contacts; the release of strategic news articles; contacts with accountants, investment advisors, and venture capital firms; personal contacts through us; word of mouth programs; web site programs; bank contacts; joint venture partner contacts; Dunn and Bradstreet contact sheets, and contacts with certain financial institutions that provide services to Restricted Stock owners.

What must also be considered is that when self marketing a partnership that includes approaching Restricted Stock owners or wealthy individuals, it will not be possible to use the standard due diligence meeting similar to those employed to market Initial Public Offerings (IPO's). First the participants are far too wealthy, busy, powerful, and egotistical to sit in a room with a group of other potential investors. Second, these individuals are extremely cognizant of their positions within their respective industries or companies and are likely to want anonymity. In some cases, especially with Restricted Stock holders it may even be a violation of their position as fiduciaries of a public company to attend such a public or group meeting. Finally, Restricted Stock owners seldom make judgments on their own, but instead rely almost exclusively on the advice of their counsel, whether it be their attorneys, accountants, or independent financial advisors.

What can be done is elicit and indication of interest (under very strict guidelines) using the marketing strategies listed above. Once a response has been received, the project manager

can send out an Offering Memorandum, with all the attachments. Thereafter project management will answer questions over the phone, and/or meet with potential investors and their counsel, and/or accept stock and cash via a prepared Subscription Agreement that is mailed out with the offering documents.

## **STEP 7 IMPLEMENTATION**

Once the proceeds of the offering have been received the project manager sets up the mechanism of accountability (annual and interim reports, audits, etc.), coordinates the review of cash flow management and investment account activities, reviews project performance, and examines new capitalization proposals should additional financing be necessary.

### **COSTS**

The cost of an offering can be prohibitive if not handled properly. As stated earlier we propose a low-cost method that allows maximum flexibility. It will likely be a two-stage program that includes:

#### Stage One

The first stage is a "preliminary development stage" that attempts to accomplish as much possible, short of actual implementation of the legal and marketing stages which normally entail the highest costs. During this first stage travel and administrative expenses are required to accomplish the deliverables previously mentioned.

*Note: Depending upon available resources there are financial mechanisms available that can generate sufficient income to pay for each stage of the process without risking personal capital.*

*Also, Stage One funds would not be required up front but could be distributed over time, based on performance against each step in the process.*

#### Stage Two

Once the Steps 1-4 are completed, and provided everything is a "Go", the next costs are centered upon legal expenses charged by the law firm that prepares the Offering Memorandum, plus the costs of the underwriting effort. Combined, these costs vary depending upon the size and complexity of the offering itself.

*Note: It is our belief that the more documentation one can develop before having to retain a law firm, the less cost will be incurred overall. The goal would be to prepare rough drafts and other materials detailing all elements of the project prior to asking for legal assistance.*

*Also, as above in Stage One, there may be ways of raising the capital to pay for these development costs so that little or no funds are required by a project organization.*