The Future of "Going Public"

The purpose of this call...	The purpose of this ***investor education training*** is to help you make higher quality investment decisions in the emerging ***"Crowdfunding Capital Markets."***
Who is this training for?	This call is designed for anyone who wants to learn more about how companies go public (and what this means for crowdfunding investors). It doesn't matter if you're a Wall Street Insider or you're brand new to investing, this training is for you. Regardless of your prior investing experience, we'll assume you are brand new to the ***Crowdfunding Capital Markets***. The **Crowdfunding Capital Markets** operate by a different set of rules than the ***Public Capital Markets***. As always, all investing activity carries some sort of risk. ***"Early Stage Companies"*** and ***"Emerging Growth Companies"*** should be considered high risk and speculative in nature. Please do not invest with funds you cannot afford to lose.
What kind of results should I expect?	By federal law, we cannot legally promise (or otherwise guarantee) that you will make any money using this workbook. Nor can we guarantee you will avoid poorly-performing investments. That being said, if you don't currently have a well-defined due diligence process like the one described in this call, you'll almost certainly benefit by implementing what you learn today.

Additional Resources	• Equifund Basic Due Diligence Tool

Disclaimers

Before we begin...	Nothing in this training should be considered as professional advice or individualized advice. Please consult your financial professionals before making any investment. All investments carry some sort of risk. Regulation Crowdfunding should be considered a risky asset class with a high rate of failure. Please don't risk any capital you need immediate access to, or otherwise cannot afford to lose.

Key Concepts, Terms, and Definitions

The Importance of Reliable Information — How the JOBS Act Affects Institutional Investors

Commissioner Luis A. Aguilar
U.S. Securities and Exchange Commission

Supporters of the JOBS Act hoped that the legislation would encourage so-called "emerging growth companies" to raise capital through initial public offerings (IPOs), enabling them to expand and — hopefully — create jobs. To achieve that goal, the legislation tries to reduce the cost of going public for these companies. This is an extremely broad swath of the market.

	The JOBS Act defines emerging growth company to include businesses with up to $1 billion in annual gross revenue, for up to five years after their IPO. This definition would encompass more than three-quarters of all active filers today — and it has been estimated that 98% of all IPOs since 1970 would have fit into that category. ***Unfortunately, the JOBS Act tries to cut the cost of capital raising by limiting the financial and other information that these companies are required to provide to their investors.*** This reduced disclosure can make it harder for investors to evaluate companies by obscuring the company's track record and material business and financial trends. The result could be an adverse impact on capital formation. ***Regrettably, there continues to be efforts to lobby for limiting disclosure requirements, on the claim that reducing the amount of required disclosures will lower the cost of capital raising.*** In my view, that would be penny-wise and pound-foolish, as money raised for inefficient uses does not in the long-term create jobs or help the economy grow. ***The goal should be capital formation, not just capital raising.*** Proponents of less disclosure lose sight of the fact that capital raising is not the same as capital formation. By itself, selling a bond or a share of stock doesn't add a thing to the real economy, no matter how quickly or cheaply you do it. True capital formation requires that the capital raised be invested in productive assets — like a factory, store, or new technology — or otherwise used to make a business more productive. The more productive those assets are, the greater the capital formation from the investment — and, importantly, the more jobs

	created.
Traditional IPO	**What is an IPO?** If a company wants to sell stock shares to the general public, it conducts an IPO. By doing so, a company goes from the status of private (no general shareholders) to public (a firm with general shareholders). Private companies can have shareholders, but they are few in number and they and the firm are not subject to regulations by the Securities and Exchange Commission. This changes dramatically with an IPO, as we'll see later. **Why does a company go public?** It's simply a money-making move. The idea is to raise funds and have more liquidity or cash on hand by selling shares publicly. The money can be used in various ways, such as re-investing in the company's infrastructure or expanding the business. An added benefit from **issuing shares** is that they can be used to attract top management candidates through the offer of perks like stock option plans. Another plus from going public is that stocks can be used in merger and acquisition deals as part of the payment. There's also the prestige — bragging rights for some firms — of being listed on a major stock exchange like the NYSE or Nasdaq. **What's the first step in an IPO?**

The firm going public hires an investment bank, or banks, to handle the IPO. It's possible for a company to sell shares on its own but, in reality, that never happens.

Investment banks can work alone or together on one IPO, with one taking the lead. They usually form a group of banks or investors to spread around the funding — and the risk — for the IPO.

Banks submit bids to companies going public on how much money the firm will make in the IPO and what the bank will walk away with. The process of an investment bank handling an IPO is called underwriting.

When an investment bank, like Goldman Sachs or Morgan Stanley is eventually hired, the company and the investment bank talk about how much money they think they will raise from the IPO, the type of securities to be issued, and all the details in the underwriting agreement.

What happens next?

After the company and investment bank agree to an underwriting deal, the bank puts together a registration statement to be filed with the SEC.

This statement has detailed information about the offering and company info such as financial statements, management background, any legal problems, where the money is to be used, and who owns any stock before the company goes public.

The SEC will investigate the company to make sure all the information submitted to it is correct and that all relevant financial data has been disclosed.

	If everything is OK, the SEC will work with the company to set a date for the IPO. After SEC approval for the IPO, the underwriter must put together a prospectus; that is, all financial information on the company that's doing the IPO. **How do underwriters make their money?** A bank or group of banks put up the money to fund the IPO and 'buys' the shares of the company before they are actually listed on a stock exchange. The banks make their profit on the difference in price between what they paid before the IPO and when the shares are officially offered to the public. Competition among investment banks for handling an IPO can be fierce, depending on the company that's going public and the money the bank thinks it will make on the deal. **What part of an IPO is a road show?** To try and drum up interest in the IPO, the underwriter takes the prospectus and presents it to prospective investors. This is what's called a road show. These can be trips around the world — thus the name road show — or can be video or internet presentations. If a prospective investor likes the IPO, underwriters can legally offer them shares at the price they eventually set before the stock is listed on an exchange. This is called IPO allocation. Road shows are usually for the bigger institutional investors like pension funds, rather than an individual investor. **How is the price of the IPO stock determined?**

As the IPO date comes closer, the underwriter and company decide on the price. This can depend on the company, the success of the road show and current market conditions.

What determines which exchange gets a new stock listing?

Like underwriters, stock exchanges such as the Nasdaq and NYSE want the business of an IPO. That's because it could lead to more trading and future business from other IPOs. There's also the prestige of having a famous company listed.

Exchanges make pitches to the companies. Then the firm with the underwriting will make the final selection.

How do investors get in on an IPO?

For small investors, it's nearly impossible to get any kind of IPO allocation. They usually have to wait until the stock is listed on an exchange, unless they have a very large account with the bank or banks doing the underwriting. Only then would they be offered some shares.

Many market experts say that the small investors should wait and refrain from immediately buying shares of an IPO. That's because insiders, such as hedge fund managers, are buying up shares that push up the price.

Smaller investors are advised to wait a couple of days for the stock price to settle back down.

What happens legally when a firm goes public?

The company falls under the guidelines of the SEC.That means it will have to follow disclosure rules like holdings and transactions of insiders or the officers and directors of the company.

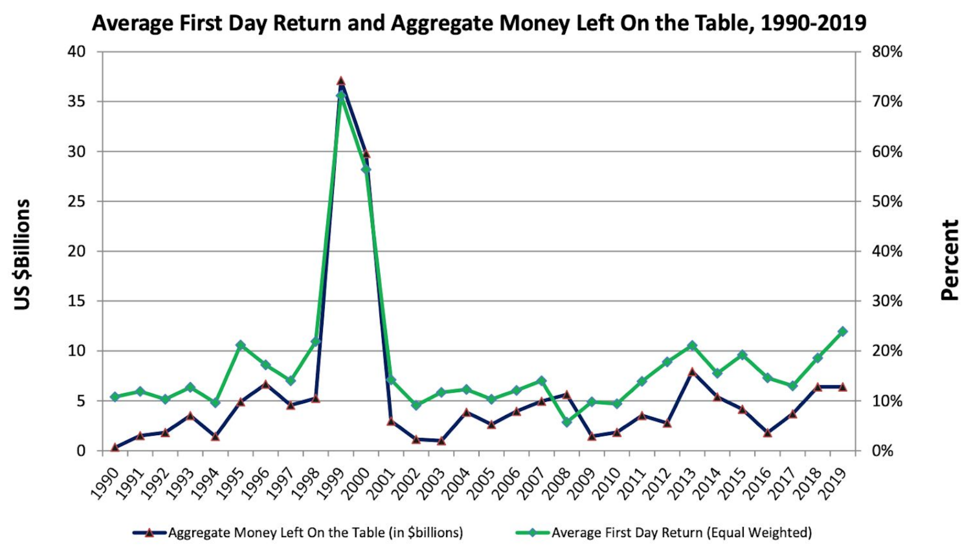
It will have to disclose its financial status on a regular basis and come under surveillance by the SEC on its trading practices. And it will have to hold shareholder meetings.
(source)

Criticism of IPOs

The IPO "Pop" (and the "Single Day Transfer of Wealth")

The Cost ($ Billions) of Underpricing (1st Day Net Gain)

Year	# IPOs	Day 1 Underpricing	$$$ Underpriced
1980-2019	8,610	20.7%	**$197.89B**
2016	75	16.6%	$2.07B
2017	107	15.0%	$4.24B
2018	134	21.4%	$7.35B
2019	112	27.0%	$7.97B
2020 (1H)	58	31.0%	$7.8B
	Source: Jay Ritter, Univeristy of Florida, https://site.warrington.ufl.edu/ritter/files/2019/04/IPOs2018Statistics-1.pdf		



Reverse Take Over	**[Reverse Takeover (RTO)](#) ("The Poor Man's IPO)** A reverse takeover (RTO) is a process whereby private companies can become publicly traded companies without going through an initial public offering (IPO). To begin, a private company buys enough shares to control a publicly-traded company. The private company's shareholder then exchanges its shares in the private company for shares in the public company. At this point, the private company has effectively become a publicly-traded company. An RTO is also sometimes referred to as a reverse merger or a reverse IPO. **How a Reverse Takeover (RTO) Works** By engaging in an RTO, a private company can avoid the expensive fees associated with setting up an IPO. However, the company does not acquire any additional funds through an RTO,

	and it must have enough funds to complete the transaction on its own. While not a requirement of an RTO, the name of the publicly-traded company involved is often changed as part of the process. For example, the computer company Dell (DELL) completed a reverse takeover of VMware tracking stock (DVMT) in December 2018 and returned to being a publicly traded company. It also changed its name to Dell Technologies. Additionally, the corporate restructuring of one—or both—of the merging companies is adjusted to accommodate the new business design. Prior to the RTO, it is not uncommon for the publicly-traded company to have had little to no recent activity, existing as more of a shell corporation. This allows the private company to shift its operations into the shell of the public entity with relative ease, all while avoiding the costs, regulatory requirements, and time constraints associated with an IPO. While a traditional IPO may require months or years to complete, an RTO may be completed in just weeks. Sometimes RTOs are referred to as the "poor man's IPO." This is because studies have shown that companies that go public through an RTO generally have lower survival rates and performance in the long-run, compared to companies that go through a traditional IPO to become a publicly traded company.
	Why Pursue a Reverse Merger? A private operating company may pursue a reverse merger in order to facilitate its access to the capital markets, including the liquidity that comes with having its stock quoted on a market or listed on an

exchange. Private operating companies generally have access only to private forms of equity, while public companies potentially have access to funding from a broader pool of public investors.

A reverse merger often is perceived to be a quicker and cheaper method of "going public" than an initial public offering (IPO). The legal and accounting fees associated with a reverse merger tend to be lower than for an IPO. And while the public shell company is required to report the reverse merger in a Form 8-K filing with the SEC, there are no registration requirements under the Securities Act of 1933 as there would be for an IPO. In addition, being public may give a company increased value in the eyes of potential acquirers.

Trading Reverse Merger Company Stock

Shares of reverse merger companies may be traded in exchange markets or over-the-counter (OTC) Exchange Markets.

If the reverse merger company securities are listed and traded on an exchange, the listed company must meet the exchange's initial listing standards to be eligible for listing. The listed company must also satisfy the exchange's maintenance or continued listing standards to remain listed and must comply with the exchange's rules, the federal securities laws, and other applicable provisions of the law.

When certain market or company events occur, an exchange may halt trading in the securities of a listed company. Also, if a listed company fails to meet the exchange's continued listing standards, the exchange may initiate proceedings to delist that company's securities from its marketplace. There is no assurance that a security listed on an exchange will remain so and trade on that exchange indefinitely.

In addition to enforcing listing and maintenance standards for companies trading on their market, the exchanges must have rules to oversee and monitor the trading of those securities. The exchanges also have rules in place to discipline those brokers and dealers who are exchange members.

Over-the-Counter

The OTC market operates on a decentralized, inter- dealer basis and does not require a direct relationship with the companies whose shares are traded. General- ly, in order for a company's stock to trade in the OTC market, a market maker (a firm that stands ready to buy and sell a particular stock on a regular and con- tinuous basis at a publicly quoted price) must first file a Form 211 with the Financial Industry Regulatory Body.

Delisted stocks may still trade in the OTC market, however, if certain statutory and regulatory conditions are met.

For example, a company whose securities are traded OTC generally does not have a direct relationship with the market maker that files the Form 211 with FINRA, with other market makers that trade the securities, or with FINRA itself, which oversees the OTC market and market participants.

Authority (FINRA) and demonstrate that the company meets the requirements of Rule 15c2-11 under the Securities Exchange Act of 1934 (Exchange Act) as well as FINRA's rules.

However, if a company being acquired in a reverse merger was continuously quoted OTC before the takeover, the post-merger company may be able to rely on that status to permit its shares to continue to be quoted without going through the Form 211 review process. Unless a company that is quoted OTC is reporting under the Exchange Act, which is not always required in the OTC market, investors may find it difficult to discern whether a particular company is a reverse merger entity. Investors may also have trouble obtaining information about the management, operations, financials, and other important aspects of a company.

Some Risks of Investing in Reverse Merger Companies

As with any investment, investors should proceed with caution when considering whether to invest in reverse merger companies. Many companies either fail or struggle to remain viable following a reverse merger. Also, as with other kinds of investments, there have been instances of fraud and other abuses involving reverse merger companies. In light of these considerations, individual investors should take into account their own financial situation, consult their financial adviser, and perform thorough research before making any investment decisions concerning these types of companies.

Another consideration is that some of the foreign companies that access the U.S. markets through the reverse merger process have been using small U.S. auditing firms, some of which may not have the resources to meet its auditing obligations when all or substantially all of the private company's operations are in another country. As a result, such auditing firms might not identify circumstances where these companies may not be complying with the relevant accounting standards. This can result in increased risks for investors.
(source)

Breaking Down a Reverse Takeover

The process of reverse takeover usually involves two simple steps:

	#1 Mass buying of shares At the start, the acquirer conducting a reverse takeover commissions the mass-buying of the publicly listed company's shares. The goal is to gain control of the target company by acquiring 50%+ of the outstanding voting shares. **#2 Shareholders-shares-buy activities** It is the next phase that leads to the merger and public listing. The process involves the private company's shareholders engaging actively in the exchange of its shares with those of the public company. The public company – which is now effectively a shell company – cedes a large majority of its stock shares to the private company's shareholders, along with control of the board of directors. They pay for the shell company with their shares in the private company. (source)
Special Purpose Acquisition Company (SPAC)	**What is a Special Purpose Acquisition Company (SPAC)?** A special purpose acquisition company (SPAC) is a corporation formed for the sole purpose of raising investment capital through an initial public offering (IPO). Such a business structure allows investors to contribute money towards a fund, which is then used to acquire one or more unspecified businesses to be identified after the IPO. **Special Purpose Acquisition Company (SPAC)**

When the SPAC raises the required funds through an IPO, the money is held in a trust until a predetermined period elapses or the desired acquisition is made. In the event that the planned acquisition is not made or legal formalities are still pending, the SPAC is required to return the funds to the investors, after deducting bank and broker fees.

How Does a Special Purpose Acquisition Company Work?

A special purpose acquisition company is formed by experienced business executives who are confident that their reputation and experience will help them identify a profitable company to acquire. Since the SPAC is only a shell company, the founders become the selling point when sourcing funds from investors.

The founders provide the starting capital for the company and they stand to benefit from a sizeable stake in the acquired company. The founders often hold an interest in a specific industry when starting a special purpose acquisition company.

Issuing the IPO

When issuing the IPO, the management team of the SPAC contracts an investment bank to handle the IPO. The investment bank and the management team of the company agree on a fee to be charged for the service, usually about 10% of the IPO proceeds. The securities sold during an IPO are offered at a unit price, which represents one or more shares of common stock.

The prospectus of the SPAC mainly focuses on the sponsors, and less on company history and revenues since the SPAC lacks performance history or revenue reports. All proceeds from the IPO are held in a trust account until a private company is identified as an acquisition target.

Acquiring a Target Company

After the SPAC has raised the required capital through an IPO, the management team has 18 to 24 months to identify a target and complete the acquisition. The period may vary depending on the company and industry. The fair market value of the target company must be 80% or more of the SPAC's trust assets.

Once acquired, the founders will profit from their stake in the new company, usually 20% of the common stock, while the investors receive an equity interest according to their capital contribution.

In the event that the predetermined period lapses before an acquisition is completed, the SPAC is dissolved, and the IPO proceeds held in the trust account are returned to the investors. When running the SPAC, the management team is not allowed to collect salaries until the deal is completed.

SPAC Capital Structure

Public Units

A SPAC floats an IPO to raise the required capital to complete an acquisition of a private company. The capital is sourced from retail and institutional investors, and 100% of the money raised in the IPO is held in a trust account. In return for the capital, investors get to own units, with each unit comprising a share of common stock and a warrant to purchase more stock at a later date.

The purchase price per unit of the securities is usually $10.00. After the IPO, the units become separable into shares of common stock and warrants, which can be traded in the public market. The purpose of the warrant is to provide investors with additional compensation for investing in the SPAC.

Founder Shares

The founders of the SPAC will purchase founder shares at the onset of the SPAC registration, and pay nominal consideration for the number of shares that results in a 20% ownership stake in the outstanding shares after the completion of the IPO. The shares are intended to compensate the management team, who are not allowed to receive any salary or commission from the company until an acquisition transaction is completed.

Warrants

The units sold to the public comprise a fraction of a warrant, which allows the investors to purchase a whole share of common stock. Depending on the bank issuing the IPO and the size of the SPAC, one warrant may be excisable for a fraction of a share (either half, one-third or two-thirds) or a full share of stock.

For example, if a price per unit in the IPO is $10, the warrant may be exercisable at $11.50 per share. The warrants become exercisable either 30 days after the De-SPAC transaction or twelve months after the SPAC IPO.

The public warrants are cash-settled, meaning that the investor must pay the full cost of the warrant in cash to receive a full share of stock. Founder warrants, on the other hand, may be net settled, meaning that they are not required to deliver cash to receive a full share of stock. Instead, they are issued shares of stock with a fair market value equal to the difference between the stock trading price and the warrant strike price.

	(source)
Direct Listed IPO	**What Is a Direct Listing?** In a direct listing, a company's outstanding shares are listed on a stock exchange without either a primary or secondary underwritten offering. Existing shareholders, such as employees and early-stage investors, become free to sell their shares on the stock exchange, but are not obligated to do so. Since there is no underwritten offering, a direct listing does not require the participation of underwriters. This means that certain features that are typical of a traditional IPO—such as lock-up agreements and price stabilization activities—are not present in a direct listing. **Why a Direct Listing?** When Spotify came to Latham (ed note: Latham is a law firm) in May of 2017 with its goal of becoming a publicly traded company, it also wanted to achieve a number of other important objectives that did not necessarily align well with a traditional US IPO process. Specifically, Spotify wanted to: • Offer greater liquidity for its existing shareholders, without raising capital itself and without the restrictions imposed by standard lock-up agreements • Provide unfettered access to all buyers and sellers of its shares, allowing Spotify's existing shareholders the ability to sell their shares immediately after listing at market prices • Conduct its listing process with maximum transparency and enable market-driven price discovery

- Having enjoyed great success in the private capital markets, Spotify had no immediate need for funding. So, with a large and diverse shareholder base, a well-known brand, global scale, a relatively easily understood business model, and a transparent company culture, Spotify felt that reimagining the process of going public through a direct listing was the path that best enabled it to achieve these goals.

Offer Liquidity for Shareholders

Shareholders in a private company face a basic limitation—they can't freely resell their shares on a securities exchange. An IPO solves that problem, but at the cost (among other things) of contractual lock-up agreements.

These lock-up agreements, which are commonly required by the underwriters of the IPO, typically restrict additional sales of shares outside of the IPO by certain existing shareholders and the issuer for 180 days post-listing.

They are designed to assist in the distribution of the shares being offered by managing potential post-offering supply and resulting volatility in the market.

By forgoing the underwritten offering process, Spotify was able to accomplish its goal of providing liquidity without imposing IPO-style lock-up agreements upon listing, and, as a result, the Spotify shareholders were free to sell their shares on the New York Stock Exchange (NYSE) immediately.

Provide Equal Access to All Buyers and Sellers

Spotify wanted to provide all buyers and sellers of its shares with unfettered access to the markets. The traditional IPO process

	includes a limited set of participants: a company and possibly certain existing shareholders who are offering to resell their shares in the IPO; an underwriting syndicate of investment banks that builds an order book of indications of interest from investors; and the investors who receive the initial allocation of shares being offered in the IPO at the price to the public appearing on the front page of the prospectus. Institutional buyers tend to feature prominently in the initial allocation. In the Spotify direct listing, no fixed number of shares was being sold to the public and no allocations were available at a set public offering price; rather, any prospective purchasers of shares could place orders with their broker of choice, at whatever price they believed was appropriate and that order would be part of the price-setting process on the NYSE. This open access feature and the ability of virtually all existing holders to sell their shares, and of any investor to buy their shares, created a powerful market-driven dynamic for the opening of trading. Since virtually all of Spotify's existing shareholders had the opportunity to participate in the first day of trading, shareholders who chose to sell were able to do so at market trading prices rather than only at the initial price to the public that would have been available to them in a traditional IPO. The ability to sell at market prices on the first day of a listing can be a significant benefit to sellers. In 2017, the average first-day return for IPOs was 11.8%, up slightly from 11.4% in 2016, but below the long-term average of 13%. As of March 28, 2018, the average first-day return for 2018 IPOs was 13.2%. [4] On April 3, 2018, when Spotify opened for trading on the NYSE, the NYSE's initial reference price that was published

to the market pre-trading was US$132.00 per share and the opening price of the shares was US$165.90 per share, or approximately 25.7% higher than the NYSE reference price. Trading in Spotify's shares closed at a price of US$149.01 per share, which was approximately 10.2% below the opening price and 12.9% above the reference price.

(source)

According to Jay Heller, Nasdaq's Head of Capital Markets, an ideal candidate for a direct listing is a well-known company that doesn't have a need for capital, has a seasoned management team with an established track record, and is willing to give financial metrics and forecasts ahead of time.

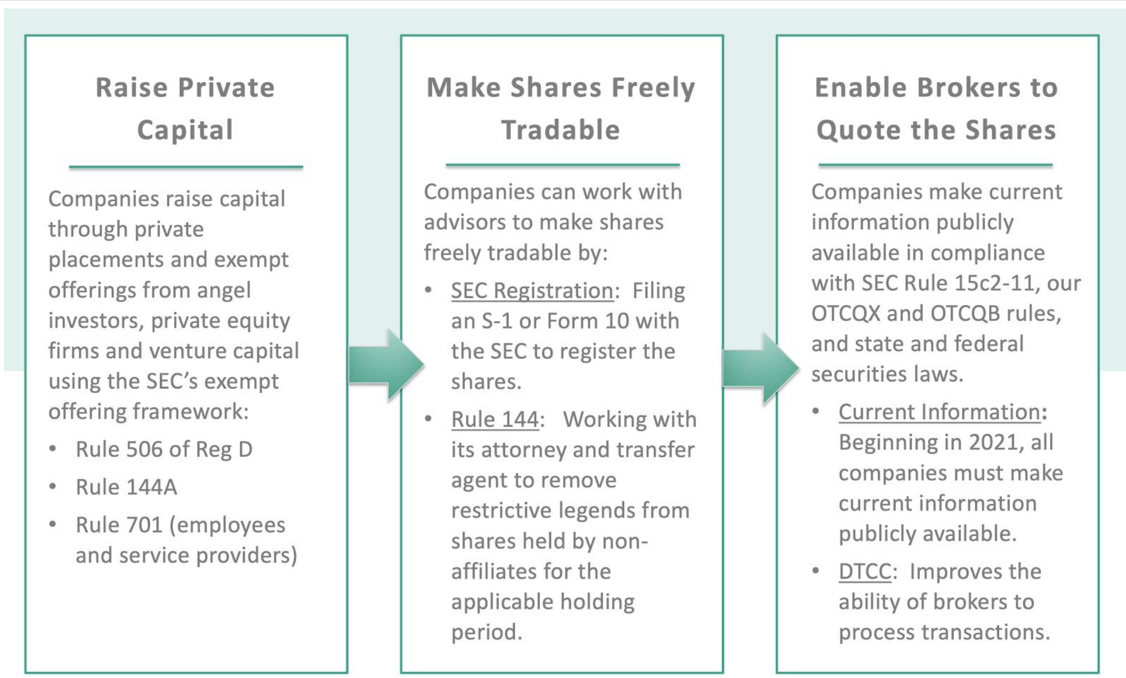
Direct listings have benefits like no lockup periods (a time restriction preventing early shareholders from selling stock), but they also have challenges like liquidity and potential volatility, Heller said.
(source)

Until Spotify went public via direct listing, there hasn't been anyone big enough - or bold enough - to challenge the IPO model.

And they were able to do it because of one simple reason…

They didn't need to raise new capital by issuing new shares (which is what happens with an IPO).

"Having enjoyed great success in the private capital markets, Spotify had no immediate need for funding. So, with a large and diverse shareholder base, a well-known brand, global scale, a relatively easily understood business model, and a transparent company culture, Spotify felt that reimagining the process of going public through a direct listing was the path that best enabled it to achieve these goals." – Marc D. Jaffe, Greg Rodgers, and Horacio Gutierrez, Latham & Watkins LLP [source]



(source)

I want to make one other point, which is the reason that I think this happens and the reason that it's been so systematic and happened over and over and over again, is you have a massive frequency mismatch.

And so a Silicon Valley entrepreneur founder and/or CEO is most likely to do one IPO in their lifetime. Well, actually, they have to be really successful and then they get to do one. The number of people that touch two is very rare if I dare.

And so if you look at the other people involved in the process, let's just use the big three, the investment in the bank, the buysider mutual fund investor who's buying the IPO, and that founder. These other two parties are doing 20 to 40 a year, versus one in a lifetime.

I think that's the primary reason that you have this problem that just keeps repeating itself.

In Game Theory, they have this thing called Flow and they look at what happens if you have a game where certain players have way more experience than the other player. And what ends up happening is you have massive anxiety on the under-skilled player.

And so I think if you're going to be anxious, you're very likely to fall back on tradition because it's the safest bet. It's like the old IBM ... you know, "You don't get fired for buying an IBM," that's a very old saying, but like it's the same thing were to do what Barry did, to do what Daniel did, to do what Stewart at Slack did, requires an enormous amount of confidence when you recognize this frequency differential…

When we get into the details, I hope that everyone will see that the way the process is run today, an underpricing is tautological. It is exactly what you would expect because the process is so broken…

And so the average underpricing that's been happening as a result of this process is about 18%. But what he sent me back was fairly shocking. The bank that underpriced the least across 35 IPOs when

	their lead left was Credit Suisse, but that was 3.3% underpricing, hardly any underpricing at all, and very far away from the average. And the bank at the top, with 111 IPOs is Goldman Sachs at 33.5% underpriced. Now, this is 10 years of data. It's not like we're saying, "Here's one example of it or here's another," it's 10 years, over 100 IPOs. Morgan Stanley second, 29%. And you have this highly variable spread depending on who the lead left banker was. And that was really really surprising to me because I think the general perspective across the investment community is the two very best banks you could choose are Goldman and Morgan. But when it comes to executing on behalf of the company, they give you the worst execution. And that's for me, but it's about trying to understand what's wrong with the system. And this looks like this highlights that there's a broken market inefficiency. If GM were out buying steel, you'd expect them to get the best price. If Amazon were out buying cardboard, you'd expect them to get the best price. So, why is it that when the best companies in Silicon Valley, the very best, pick the very best banks, they get the worst execution? It's not what you would expect… Yeah, yeah. There are two things that I would mention, although there are many, many more esoteric details. One of them is the greenshoe. Most people don't know what a greenshoe is. Most people that know what a greenshoe is don't understand the greenshoe. It couldn't be more esoteric. It's named after a company, the Green Shoe company where this first happened. But I'll give it a very quick effort to try and explain. But in every IPO they sell 15% more shares than ... it's called the over-allotment option, and you can read about it in the S-1. They sell 15% more shares than you talk about the entire time you're planning the IPO. And if it pops and goes up, which is what happens the majority of the time because we've talked about these underpricings, you just did a bigger, 15% bigger raise than you were really planning on. And that's what happens most of the time.

	To the extent that the stock breaks issue, the bank is then allowed to use the 15% to buy shares underwater and then they cross those out. And in that case, you didn't sell 15% more of the company than you were planning to. And the bank argues that having this extra buying power is for stabilization. Now, one huge, massive irony is that the bank actually gets to keep that profit. And so in the Uber case where we were involved, and the company did break issue, the bankers made over $100 million on the greenshoe alone, double the fee...One of the great things about the direct listing is it just simplifies so much stuff, but this just goes away...

	IPO	SPAC	Direct Listing
Strengths	• Can raise primary capital • Established mechanism—underwriters have significant experience with the process: - Provide regulatory guidance - Market to investors and advise on pricing/allocation - Often guarantee the sale of a certain amount of stock and provide post-issuance price support	• Faster and simpler than IPO for target company (less financial and business disclosures and regulatory scrutiny) • More straightforward process for target company, which deals with one party and agrees to a fixed price • More flexibility and liquidity for SPAC investors • Provides access to all investors	• Market-driven price discovery • Democratic allocation based on demand • More liquidity • Existing shareholders can avoid dilution • Lower fees than IPOs and SPACs • No lockup period
Weaknesses	• Higher fees than direct listings • First day price pop suggests company could have raised more capital • Allocation not strictly based on market demand • Less trading volume/liquidity	• Higher fees than direct listings • No market-driven price discovery—still opportunity for first day price pop • Uncertainty for investors in the SPAC IPO regarding the eventual target company and the price • Target company unsure of how much capital it will raise	• Cannot raise primary capital • Limited experience/history • No post-issuance price support

Source: Counterpoint Global; "What to Know About Direct Listings—From a Banker," Morgan Stanley Global Capital Markets, November 21, 2019; and Nicholas Jasinski, "SPACs Are All the Rage, but These Private-Equity-Like Vehicles Are Complicated. Here's What You Need to Know," Barron's, *July 31, 2020.*

[Bill Gurley, General Partner at Benchmark Capital]

	If someone says we're going public… https://www.sec.gov/spotlight/sbcfac/otc-markets-group-cass-sanford-pulse-public-markets.pdf

#1) Are you DTC eligible? If so, more brokerages will take the shares. This costs between $12k - $15k for the company to do.

WHAT IS DTC ELIGIBILITY?

DTC Eligibility means that a public company's securities are able to be deposited through DTC. DTC is the largest securities depository in the world and holds over thirty-five trillion dollars worth of securities on deposit. DTC accepts deposits of securities from its participants only, who are usually clearing firms.

Most brokers clear stock in-house or hire a clearing firm to do so on their behalf. All movements of securities are made to the participant's account electronically with book-entry adjustments.

If an issuer is not DTC eligible, then its shares cannot be transferred between brokerage accounts electronically, which basically means its shares cannot be traded easily.

Major Exchanges such as NYSE and NASDAQ require DTC eligibility. Other Platforms such as the OTC Bulletin Board and the Pink Sheet markets do not.

Only a DTC participant can request that DTC make a security eligible. Most large U.S. broker-dealers and banks are DTC participants. Once an issuer has been approved for trading by FINRA, they must apply to DTC for their initial eligibility to trade. If DTC approves the application they will hold all of the issuer's free-trading street name shares on deposit.

As with a Form 15C2-11 submission to FINRA, an issuer cannot make a direct application to DTC for eligibility. The issuer must have a relationship with a broker-dealer or other financial institution that is a participant and will sponsor the eligibility process. This firm is also known as the “market-maker”. They will carry the initial position in inventory on behalf of their firm. A current

#2) Then you have to file a 15c2-11 with a market maker. You will need 2 years of audited financials or a Form 10. Any company can file a Form 10 that makes them a Sarbanes-Oxley reporting company.

Who is a market maker?

https://www.otcmarkets.com/market-activity/broker-dealer-data

When you see a ticker with a bid-ask, this is who is "making the market"

#3) Now you need a transfer agent

#4) **FOR THE INVESTOR**: You now have to get your shares deposited into a brokerage account

Your ability to deposit these shares will depend heavily on the assumed risk the broker is taking, both on you as the customer and the issuer in question.

The broker will look at how you acquired these shares.
IF there is a raise exemption used, there is a track record and a chain of custody.

The first thing they will ask you is "is this DTCC eligible?"

You'll show them your share purchase agreement, the form C, and the transfer agent statement

	====== Unless the company has been properly advised from the get go, they will likely mess this up. Right now, all stocks are held in book entry (which is the decision to not hire a transfer agent, and manage the cap table themselves), not electronic certificates.
Core Topic: Direct Listing on the OTC	
Game Board	Types of Markets In the exchange of assets, there are several different types of markets to facilitate trade. Each market operates under different trading mechanisms, which affect liquidity and control. These three are the main types of markets: 1. Dealers (Over-the-counter) 2. Brokers 3. Exchanges
- **Dealer Markets**	**Dealer Markets** A dealer market operates with a dealer that acts as a counterparty for both buyers and sellers. The dealer sets bid and asks prices for the security in question, and will trade with any investor willing to accept those prices. Securities sold by dealers are sometimes known as traded over-the-counter (OTC).

	In doing so, the dealer provides liquidity in the market at the cost of a small premium. In other words, dealers will often set bid prices lower than the market and ask prices higher. The spread between these prices is the profit the dealer makes. In return, the dealer assumes counterparty risk. Dealer markets are less common in stocks, but more common in bonds and currency. Dealer markets are also appropriate for futures and options, or other standardized contracts and derivatives. Finally, the foreign exchange market is usually operated through dealers, with banks and currency exchanges acting as the dealer intermediary. Of the three types of markets, the dealer market is usually the most liquid.
Negotiated Market	What Is a Negotiated Market? A negotiated market is a type of secondary market exchange in which the prices of each security are bargained out between buyers and sellers. In a negotiated market, there are no market-makers or order matching. Instead, buyers and sellers actively negotiate on the price at which a transaction is finalized either directly or through the use of brokers. These markets are considered very inefficient as the time, effort, and lack of transparency in pricing are large issues that can't be resolved for this type of trading. **Understanding a Negotiated Market** A negotiated market refers to the decentralized buying and selling of securities without one central market maker. Negotiated markets exist and function via the basic principle of supply and demand.

	Buyers produce demand for a given security or asset by entering bid orders to buy the security at a specified amount and price; sellers create the supply for the security by entering ask orders, again for set amounts and prices. The over-the-counter securities market is one major example of a negotiated market.
	“Over the Counter” is an ATS (alternative trading system) These shares can’t be deposited anywhere. The listing requirements are so low, you won’t brag about your company on the OTC. They also allow for simultaneous listing, which gives marketers the ability to figure out the best demand (i.e. Canada vs US) CSE => OTC => Frankfurt (The bottom of the barrel)
- **OTCQX**	OTCQX THE BEST MARKET ● OTCQX US Listing Requirements ○ Have $2 million in total assets as of the most recent annual or quarter end; ○ As of the most recent fiscal year end have at least one of the following: (i) $2 million in revenues; (ii) $1 million in net tangible assets; (iii) $500,000 in net income; or (iv) $5 million in market value of publicly traded securities;

	○ Meet one of the following penny stock exemptions under Rule 3a51-1 of the Exchange Act: (i) have a bid price of $5 or more; or (ii) have net tangible assets of $2 million if the Company has been in continuous operation for at least three years, or $5,000,000 if the Company has been in continuous operation for less than three years which qualification can be satisfied as of the end of a fiscal period or as a result of an interim capital raise; or (iii) have average revenue of at least $6,000,000 for the last three years; ○ Not be a blank check or shell company as defined by the Securities Act of 1933 ("Securities Act"); ○ Not be in bankruptcy or reorganization proceedings; ○ Be in good standing in its state of incorporation and in each state in which it conducts business; ○ Have a minimum of 50 beneficial shareholders owning at least one round lot (100 shares) each; ○ Be quoted by a market maker on the OTC Link; ○ Have a minimum bid price of $0.10 per share for its common stock as of the close of business on each of the 30 consecutive calendar days immediately preceding the Company's application for OTCQX. If (i) there has been no prior public market for the Company's securities in the U.S. and (ii) FINRA has approved a Form 211, then the Company may apply to OTC Markets for an exemption from the minimum bid price requirements, which exemption is at the sole discretion of OTC Markets. In the event that the Company is a Seasoned Public Issuer

(i.e., has been in operation and quoted on either OTC Link, the OTCBB or an exchange for at least one year) that completed a reverse stock split within 6 months prior to applying for admission to OTCQX U.S., the Company must have a minimum bid price of $0.10 per share for its common stock as of the close of business on each of the 5 consecutive trading days immediately preceding the Company's application for OTCQX, after the reverse split;

- Have GAAP compliant (i) audited balance sheets as of the end of each of the two most recent fiscal years, or as of a date within 135 days if the Company has been in existence for less than two fiscal years, and audited statements of income, cash flows and changes in stockholders' equity for each of the fiscal years immediately preceding the date of each such audited balance sheet (or such shorter period as the Company has been in existence), and must include all going concern disclosures including plans for mitigation; and GAAP compliant (ii) unaudited interim financial reports, including a balance sheet as of the end of the Company's most recent fiscal quarter, and income statements, statements of changes in stockholders' equity and statements of cash flows for the interim period up to the date of such balance sheet and the comparable period of the preceding fiscal year; and

- Be included in a Recognized Securities Manual or be subject to the reporting requirements of the Exchange Act.

OTCQX U.S.

Eligibility Standards

- Not be a Shell Company or Blank-Check Company
- Not be subject to any Bankruptcy or reorganization proceedings
- Not a Penny Stock
- Have Priced Quotes by a market maker on OTC Link
- Submit a Letter of Introduction from an OTCQX Sponsor
- Have a transfer agent that participates in the Transfer Agent Verified Share Program

Disclosure Standards

Meet one of the following Reporting Standards:

- SEC Reporting Standard
- Regulation A Reporting Standard
- Alternative Reporting Standard

Audited annual financials by a Public Company Accounting Oversight Board (PCAOB) auditor and unaudited interim financial reports, prepared in accordance with U.S. GAAP
Timely disclosure of material news

Corporate Governance Standards

- Have a board of directors that includes at least 2 Independent Directors;
- Have an Audit Committee, a majority of the members of which are Independent Directors; and
- Conduct annual shareholders' meetings and make annual financial reports available to its shareholders at least 15 calendar days prior to such meetings

OTCQX US Premier

- Satisfy all of the eligibility requirements for OTCQX U.S. set forth above;
- Have (i) At least (a) 500,000 publicly held shares; and (b) $1 million in market value of publicly held shares; and (ii) at least (a) $500,000 in net income (in the latest fiscal year or in two of the last three fiscal years); or (b) $2.5 million in stockholders' equity; or (c) $35 million in market value of listed securities;
- Have a minimum of 100 beneficial shareholders owning at least one round lot (100 shares) each;
- Have a minimum bid price of $1.00 per share for its common stock as of the close of business on each of the 30 consecutive calendar days immediately preceding the Company's application for OTCQX. If
  - (i) there has been no prior public market for the Company's securities in the U.S. and
  - (ii) FINRA has approved a Form 211 and
  - (iii) the bid price is equal to or greater than $1.00, then the Company may apply to OTC Markets for an exemption from the 30-day minimum bid price requirements, which exemption is at the sole discretion of OTC Markets.
- In the event that the Company is a Seasoned Public Issuer (i.e., has been in operations and quoted on either OTC Link, the OTCBB or an exchange for at least one year) that completed a reverse stock split within 6 months prior to applying for admission to OTCQX U.S.,

	the Company must have a minimum bid price of $1.00 per share for its common stock as of the close of business on each of the 5 consecutive trading days immediately preceding the Company's application for OTCQX, after the reverse split; ○ Conduct annual shareholders' meetings and submit annual financial reports to its shareholders at least 15 calendar days prior to such meetings.
- **OTCQB**	OTCQB **Eligibility Requirements** ● U.S. companies must have audited annual financials by a PCAOB auditor. (Tier 2 Regulation A Companies are exempt from requirement to use a PCAOB auditor for their initial audit) ● Meet minimum bid price test of $0.01 ● Not be in bankruptcy ● Have at least 50 Beneficial Shareholders, each owning at least 100 shares ● Have a freely traded Public Float of at least 10% of the total issued and outstanding of that security. Companies with a freely traded Public Float of at least

	5% (and $2 million in market value of public float), or a separate class of securities traded on a national exchange may apply for an exemption (see OTCQB Standards) • Have a transfer agent that participates in the Transfer Agent Verified Share Program (US Companies only) • International companies must be listed on a Qualified Foreign Exchange (or SEC Reporting) and submit a Letter of Introduction from an approved OTCQB Sponsor **Reporting Requirements** Meet one of the following Reporting Standards: • SEC Reporting Standard • Regulation A Reporting Standard (Tier 2) • U.S. Bank Reporting Standard • International Reporting Standard • Alternative Reporting Standard **Timely disclosure of material news** Corporate Governance Requirements (Alternative Reporting only) • Have a board of directors that includes at least two Independent Directors • Have an Audit Committee, a majority of the members of which are Independent Directors **Verification Requirements** • Maintain a Verified Company Profile • Post initial and annual verification and management certification

- **OTC Pink**	Only needs STATED financials
- **Delisted / "Grey Sheet"**	**These are the worst companies** Doesn't have updated financials
Transfer Agent	The Transfer Agent Verified Shares Program provides reliable share data to investors of OTCQX, OTCQB and Pink securities by allowing participating transfer agents to submit verified shares outstanding information for their clients directly to OTC Markets Group via a secure, electronic file transfer. Participating Transfer Agents: • Action Stock Transfer • • American Registrar & Transfer Co. • • AST - American Stock Transfer & Trust Company • • Broadridge Financial Solutions, Inc. • • ClearTrust, LLC • • Colonial Stock Transfer Co. Inc. • • Computershare US • • Continental Stock Transfer & Trust Company • • Corporate Stock Transfer • • Direct Transfer LLC • • Dynamic Stock Transfer, Inc. • • Empire Stock Transfer • • EQ Shareowner Services • • Equity Stock Transfer • • First American Stock Transfer • • Globex Transfer, LLC • • Heritage U.S. Transfer Corp. • • Integral Transfer Agency •

	• Island Stock Transfer • • Madison Stock Transfer Inc. • Manhattan Transfer Registrar Co. Mountain Share Transfer National Securities Administrators Nevada Agency and Transfer Company New Horizon Transfer Inc. Odyssey Trust Company Olde Monmouth Stock Transfer Olympia Trust Company Pacific Stock Transfer Philadelphia Stock Transfer, Inc. Standard Registrar & Transfer Co., Inc. Securities Transfer Corporation Signature Stock Transfer, Inc. TransCanada Transfer Inc. Transfer Online, Inc. TranShare Corporation TSX Trust Vail Stock Transfer VStock Transfer West Coast Stock Transfer, Inc. Worldwide Stock Transfer, LLC (source)
Depositing Shares	**Issues Facing Small Cap Issuers** As the market operator where thousands of small and micro-cap securities trade, we occasionally hear from issuers and their investors who are frustrated when brokers won't deposit their stock. While this is generally perceived to be an OTC issue, the reality is that this affects privately issued shares on all public markets, including national exchanges. The problems with the deposit of shares often center around broker-dealers' gatekeeper responsibility to understand "how" the company's shares were obtained and know "who" the investor looking to complete the transaction is, so as to protect public markets from illegal distributions of securities.

KYC (Know Your Customer) and Anti-Money Laundering (AML) compliance checks

Rules and regulations governing the broker-dealer industry require that firms know how a shareholder obtained their shares, as well as whether those shares are restricted. The Patriot Act and other regulations also require brokerage firms to perform adequate KYC (Know Your Customer) and Anti-Money Laundering (AML) compliance checks. Failure to comply could result in significant financial fines or worse. A case in point is Bank of America Corp.'s Merrill Lynch unit which recently agreed to pay $1.4 million to settle SEC allegations that it did not do enough to investigate red flags surrounding the deposit, and subsequent sale by an affiliate, of unregistered shares of NYSE listed financial-software company Longtop Financial Technologies Ltd.

Questions to Ask when Accepting Deposit of Shares

When deciding to accept a deposit of shares, brokers often assess the following:

Are the shares in Certificate form? Are they legended?
Is the holder an affiliate of the issuer?
How were the shares acquired? Was it done through a private transaction (or chain of transactions) with an issuer or affiliate? At a material discount to market prices?
Are those shares currently restricted? If not, is there adequate legal documentation showing the shares are freely tradable?
What is the company's share structure and share issuance history?
Has the company done a number of issuances/private placements?
How many shares does the company have outstanding?
Does the holder have an existing account with the brokerage firm?
If so, for how long, and what is the total value of the account?

	(source) “Forum participants report that many broker-dealers will not accept, deposit, clear, sell and/or trade low-priced stocks. They note that the Financial Industry Regulatory Authority (“FINRA”) and the Depository Trust Company (“DTC”) are requiring broker-dealers to take inordinate responsibility and liability for possible counterfeit certificates, tracking the origin of prior share transfers and monitoring the placement of restricted legends. This issue seriously impacts the participation of investors in financing micro-cap issuers.” (source)
	• **Exchange Act Rule 15c2-11:** Approval of a regulated “Expert Market” for sophisticated and professional investors to trade securities that do not make current information available. • **Rule 144:** Modernize “red flag” guidance for brokers and other intermediaries and make Form 144 information more readily available to investors. • **Regulation A:** Allow for at-the-market offerings. • **Transfer Agent Rules:** Require additional disclosure so industry participants can gain valuable insight into share ownership, distributions and transfer history. • **Paid Stock Promotion:** Enhance and modernize Section 17(b) disclosure requirements for stock promoters. • **13F Institutional Reporting:** Extend reporting requirement to apply to holdings in OTC securities. • **Clearing & Depositing:** Issue industry guidance and examine NSCC/DTCC Rules impacting “Illiquid” securities. (source)
Q&A	