

Obtain Financing By Leveraging Your Company's Top-Line Revenues

No Equity Dilution at Today's Low Valuations.

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Overview

Despite interest rates being lowered to historical levels, companies remain severely challenged in obtaining corporate financing. In the wake of the Credit Crunch, lenders have imposed stricter lending requirements, while equity investors will only invest at much lower valuations than just a few months ago. As a result, many well-managed middle market companies which do not qualify for (additional) business loans, and/or do not want to dilute shareholder equity at today's lower valuations, are frustrated by their inability access capital for growth and recapitalizations.

One attractive and innovative financing solution that CFOs at middle market companies might consider is obtaining lump sum capital in exchange for giving the investor a monthly fixed percentage of the company's top-line (GAAP) gross revenues for a finite period of time, or perpetually. This form of financing, traditionally known as Royalty Financing, is commonly used by software companies that license their intellectual property in exchange for the discounted present value of future licensing fees, as well as by life science and film companies that take present royalties in exchange for future distribution rights.

Until recently, collateralizing debt obligations with top-line revenues was not

used as a main stream corporate finance tool, and there was no secondary market for such securities to provide a liquidity channel for investors. However, after three years of development, Entrex, Inc., based in Chicago, along with Bank of New York/Mellon, are institutionalizing the Entrex Capital Market System for revenue-based securities, and launching an exchange for the trading of this type of security.

These securities are known as Top-Line Income Generation Rights Certificates (aka TIGRcubs™). A TIGRcub™ security can operate as a substitute for either debt or equity securities. Pursuant to a U.S. patent, issued in 2006, other patent applications filed since then, and the development of other intellectual property, Entrex grants patent rights and rights to its intellectual property to private companies that want to issue TIGRcub™ securities in private placements to accredited investors, or alternatively, to public companies that issue registered TIGRcub™ securities. As primary issuances of TIGRcubs™ proliferate, Entrex plans to operate its securities exchange specifically for the secondary trading of TIGRcubs™.

Benefits of TIGRcubs™ For Companies

For private and public companies with positive cash flows, annual revenues between \$5M - \$250M, relatively strong gross margins, and promising future revenue growth, TIGRcubs™ appear to be a well-suited corporate finance solution. The main advantage for companies issuing TIGRcub™ securities is that there is no equity ownership dilution to the current shareholders.

This top-line focus to derive investor returns elegantly avoids today's awkward company valuation discussions, the difficult analyses associated with estimates of future



Issuer Benefits of TIGRcubs

- Non-Dilutive to Equity
- Variable Cost
- Less Governance
- No Exit Pressure

Investor Benefits of TIGRcubs

- Monthly Cash Returns
- Alternative Yields
- Inflation Hedge
- Transparent

EBITDA results, and the liquidity discount often applied to illiquid private equity valuations. Instead, investors, who receive a fixed percentage of the company's variable gross revenue, truly become aligned in promoting company growth. Variable payments enable companies some relief if cash flow drops, at a time when they need it most.

Issuing TIGRcubs™ also enables companies to raise capital and avoid a down equity round that can often trigger preferred shareholder rights such as ratchets, additional board seats, and potentially additional warrant coverage. Substituting a TIGRcub™ issuance for an equity round

allows a company to raise capital and defer the sale of equity to a time when valuations become more favorable.

Importantly, unlike venture capitalist (VC) and private equity (PE) firms, which almost always require a seat on the Board of Directors to monitor their investment, TIGRcub investors are passive investors and do not impose this requirement, which results in less governance from the company's perspective. Moreover, TIGRcub investors do not invest with the same time horizons as do VC and PE investors, so companies issuing TIGRcub™ do not experience the same pressures imposed by investors for a liquidity event by either going public or selling. In other

words, while TIGRcubs™ do not preclude or restrict a liquidity event, they are designed to deliver investor returns without the requirement for a liquidity event. Thus, the current shareholders benefit by maintaining ownership control until they determine to sell or merge the business, not pursuant to the IRR hurdles and timelines of outside investors.

Companies issuing TIGRcubs™ also benefit by being able to deduct for Federal and State Income Tax purposes their payments in excess of the principal debt obligation as an interest expense equivalent. However, pursuant to the Financial Accounting Standards Board (FASB 133), companies must qualify for this interest deduction by assuring that the TIGRcub™ issuance includes a firm obligation that the principal portion be repaid by or on a date certain; if so, then the security qualifies as a debt obligation and can be accounted for accordingly.

From an accounting and tax standpoint, companies issuing TIGRcub™ securities and their auditors must be careful to accurately explain such contingent liabilities on their balance sheet and consider all relevant facts and circumstances as they determine the accounting and tax treatment. Depending on the debt or equity characteristics of the TIGRcub security, companies may be required to impute the amount of the contingent obligation under the fair value reporting standards of FASB 159 as well as file Contingent Payment Debt Obligation (CPDI) tax schedules.

Benefits of TIGRcubs™ For Investors

As depicted in the diagram above, benefits also exist for investors, who are primarily the increasing number of private funds familiar with the Entrex and TIGRcub™

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securities. First, investors purchasing TIGRcubs™ receive monthly income from the issuer, which produces a reliable ROI, at least to the extent company revenues are stable and growing. When structured as an equity substitute for high-growth companies and unsecured, the TIGRcub™ security is priced by investors to achieve return levels commensurate with risks, likely in the 25% - 40% range, similar to venture capital or private equity IRR expectations. When structured as a debt substitute, senior and secured, the TIGRcub security is priced comparatively to mezzanine debt with 15% - 20% IRR targets, but without equity dilution from warrants.

Second, TIGRcub™ investors will like that their returns are not dependent upon company profitability or company liquidity events. This feature of the TIGRcub™ security, in contrast to equity security structures or mezzanine debt with equity components, enables investors to obtain returns from revenue growth, while management focuses on increasing sales and enterprise value, instead of being distracted by an investor's emphasis on liquidity events that favor them at the expense of management and/or other shareholders.

Third, investors can achieve broad based diversification by investing in TIGRcubs™ which can be structured to simulate debt or equity securities, depending on the risk/reward profile that the investor seeks. TIGRcubs™ operate as an effective inflation hedge, since the investor's return varies with the company's revenue performance, while taking into account the fluctuating value of the dollar, as well as the appearance of increasing revenues in an inflationary economy.

Fourth, the Entrex Exchange, with centralized information and transaction support, is being designed to provide high

degrees of transparency so that public companies – as well as private companies – keep investors fully informed of their financial progress, as well as the performance of the TIGRcub™ security. Investors will be able to monitor their investments through integrated securities registration and listing, asset servicing, corporate trust functions, issuer financial reporting and corporate action disclosures.

In short, the many desirable features of the TIGRcub™ security should prompt accredited investors from a variety of segments to begin cautiously allocating more capital into this asset class.

HOW IT WORKS

Procedurally, issuers declare periodic revenues (monthly, or quarterly in the case of public entities) and make the appropriate monthly payments to Bank of New York/Mellon, who operates pursuant to a TIGRcub™ indenture agreement, as the exclusive corporate trustee, registrar, and transfer agent for TIGRcub™ securities. In turn, Bank of New York/Mellon makes the monthly/quarterly distributions to TIGRcub™ certificate holders (investors) on a pro-rata basis.

TIGRcub™ certificates are usually issued for 10 year terms, which can be redeemed or accelerated prior to the maturity date, typically by a recapitalization that replaces the TIGRcub™ with traditional, lower cost bank debt. In the event of a company sale or change of control, the TIGRcub™ mandatorily redeems. The prepayment amount is calculated by applying the same IRR agreed to upon inception, however, prepayment penalties in the early years usually apply.

Entrex also supports TIGRcub™ securities of different structures with maturity dates other than 10 years including, but not limited to: (1) the **Perpetual TIGRcub™**, which is permanent financing, akin to an equity-like investment (without the complexities of equity financings some of which were mentioned earlier) and with lower monthly payments (meaning a lower percentage of revenues promised to investors). This form of TIGRcub™ is well suited for venture-backed companies, as well as more mature companies, and (2) the **Min/Max TIGRcub™** that has an IRR floor and ceiling, which would appeal to bullish issuers that want to limit an investor's potential up-side participation in top-line revenues (and, therefore, also the issuer's cost of capital) in trade for agreeing with the investor to a minimum monthly payment.

The use of proceeds from a TIGRcub™ issuance is wide ranging, and can include financing for growth, recapitalization, and "going private" transactions for orphaned small-cap public companies. Again, TIGRcub™ issuances appear best suited for companies with \$5M - \$250M in existing annual revenues who are projecting significant growth as in the case of a company rolling out a proven product into new market segments or geographies.

A TIGRcub™ issuance is also an effective succession planning tool, which enables the senior family members, or a block of shareholders, to take some money out of the company, while avoiding the dilutive effect of taking on new shareholders, particularly institutional investors that require Board seats. Another practical application for a TIGRcub™ issuance is in the form of a tender offer, which thinly-traded small cap public companies can use

to raise cash in order to buy out the majority of outstanding shares, and take the company private. This requires careful legal advice, specific SEC filings, and shareholder consents.

Talk To Your Investment Banker About TIGRcubs™

TIGRcub™ issuances are structured and offered by SEC registered investment banks who are also independent licensees of Entrex. Entrex is a neutral party, and refers inquiries regarding TIGRcub™ issuances to its' network of investment banks.

Investment banks, including **Corporate Finance Associates**, help companies evaluate the comparative cost of capital, arrange investments in either debt-like or equity-like TIGRcub™ by select investors and specialized funds, and negotiate term sheets.

TIGRcub™ issuances are structured to qualify under the Regulation D exemptions from SEC registration of securities or as registered securities pursuant to the Securities Act of 1933. Whether private or public, a company issuing TIGRcubs™ must agree to provide audited financial statements and other disclosures on a going forward basis to investors. Therefore, the entire TIGRcub™ issuance process is coordinated with the company's attorneys, as well as the company's internal and external accounting professionals, who provide the necessary advice and opinions in connection with the offering.

Entrex is assembling an online data base of pertinent research materials on TIGRcub™ security structures. The permission-based TIGRcub™ Collaboration and Support Center (configured using Microsoft SharePoint), will be made available to

licensed investment banks, issuers, and their accounting and legal professionals. Designed as a knowledge base, the online archive will contain a wide range of helpful documentation including security descriptions, model documentation and templates, financial models, TIGRcub™ application case studies, accounting and tax technical reference materials, best practices, price discovery support, presentation templates, and discussion boards. These materials will in part be contributed by the independent investment banking licensees of Entrex and other security industry professionals.

For 56 years, Corporate Finance Associates (CFA) has been one of North America's largest investment banking firms serving middle market companies. CFA has more than 30 offices in the United States, India and Canada, as well as investment banking alliance partners in Europe and Brazil. CFA focuses on transactions in the \$5 million to \$250 million range. Securities transactions are offered through Corporate Finance Securities, Inc. (CFS), a SEC registered broker-dealer, and FINRA member firm. CFS is licensed by the Entrex, Inc. to sell Top-Line Income Generating Rights Certificates (TIGRcubs™).

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