Identity Fund

Human Capital Marketplace

The platform for human capital backed assets issue, crowdtraction and exchange

Position paper

Version: 0.4.8

Table of contents

Identity Fund: a marketplace for human capital backed assets issue, crowdtraction and exchange

Kirill Goryunov
kirill@identity.fund

1 Abstract

Technology is at the core of the modern society, yet it is not brought to masses by the inventors. Henry Ford did not create the first car, Steve Jobs did not invent a first smartphone, nor Bill Gates designed the first operating system.

It was not an invention but a combination of their personal traits that allowed them to change the world: find an innovation, shape it according to their vision, and find people to bring it to life.

Those and other entrepreneurs have built a fortune for themselves and historically very few people were able to benefit from their intelligence, vision and tenacity.

2 Problem

2.1 Investing into the entrepreneurship

2.1.1 Venture capital issues

According to TechCrunch research, 95% of VCs are not generating enough return for their investors after adjusting for risk, fees, and very limited liquidity.

A VC fund requires a minimum 3x return to achieve a "venture rate of return" and be considered as adequate given the associated risk. Figure 1 shows distribution of VC investment returns where 95% are between 3x and direct loss.

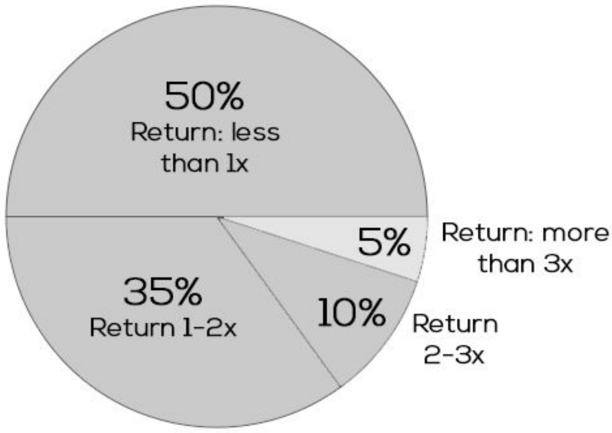

Figure 1: VC fund return on investment

Summarizing the research, we can make statement that venture capital model has maximum 5% of startups succeed and 0.5% are unicorns; the remaining 95% of projects do not pay back adequately.

Despite this, early stage investments still offer a unique opportunity to fund new Googles and Facebooks that will produce tremendous growth for investors. However, the current venture model has many barriers for the effective personal investing:

1. **Exclusivity**. In majority of the countries, including USA and Western Europe, if one wants to invest with venture funds he or she is required by law to be a "qualified investor" -- a person with very high income and total personal wealth. On top of that, venture funds often set "minimal contribution amounts", often in millions, to take one's money. So, if one wants to support vision, drive, and skills of certain entrepreneur with "mere" 10,000 USD he or she would not be physically able to do so.
2. **Liquidity.** Most of the venture capital investments have a lifespan of 3 to 5 years. That is a time between when money is taken from the investor and when money is, hopefully, returned back. Effectively, there is no mechanism to withdraw one's money from certain investment mid-cycle no matter of the situation.
3. **Politics.** Even if an investor manages to personally fund the certain company in early stages, he or she will soon realize that it is far beyond a founder that one have to deal with. Investing in companies means that you have to deal with other participants, who often have greater bargaining power: venture funds, board of directors, regulators, etc. As the result, instead of building a mutually beneficial relationship with an entrepreneur a retail investor is

buried in plethora of legal documents and is preyed upon by the bigger players.

2.1.2 Stock market issues

Investing in publicly traded companies puts even more distance between an entrepreneur and the investor. Moreover, buying shares on the exchange rarely offers a multifold returns in relatively short period of time, as listed companies are usually fairly mature and hence see limited growth. There are obviously exceptions, but even the most attractive of the publicly traded companies have an intrinsic issues:

1. **Volatility.** The stock price is believed to follow so-called "random walk" -- an equal chance of going up or down on any given day. Even the most successful stocks of the past few years, FANG (Facebook, Amazon, Netflix, Google), saw an almost 30% decline in late 2018. It is obvious that personal financial well-being of leaders behind public companies are almost completely remote from fluctuations in the financial markets.
2. **Intermediaries.** Investment in stock sees even more participants than private ones. Price of the shares is affected by Wall Street analysts, trade wars, board politics etc. Besides aforementioned volatility, it also creates a disconnect between founder's and company's success. If say, Elon Musk is forced out of his position in Tesla it would be a tremendous loss for the company, while Elon's personal brand would hardly suffer.
3. **Boundaries.** Buying stock is clearly much more than just buying into the founder's brand -- it is a multitude of employees, customers, suppliers and so on. Moreover, a single person can found several companies and make very profitable and notable investments outside of his or her role in a certain company. By binding oneself to shares of a company one is limiting his or her ability to benefit from whole spectre of success and growth generated by the entrepreneurs.

2.1.3 ICO model issues

Recent years have seen a new mechanism of investment -- initial coin offering. While number of ICO's has skyrocketed in 2017 & 2018 this model is still in a lot of growing pains and faces very high failure rate

Brand new ecosystem, lack of regulations, abundance of hype makes this model is highly susceptible to the following issues:

1. **Inadequate teams.** A very large portion of blockchain-based teams have very little to no experience in the field that they are trying to "disrupt". Most of them would have no more than a questionable website and even more questionable whitepaper. The message would contain a lot of buzz words, yet very little business acumen, sound financial models and reasonable business planning. And only extremely limited set of companies would offer something revolutionary, beyond blockchain-as-a-service -- BAAS.
2. **No ecosystem.** Most of the ICO's lack a healthy environment for their product: relationships, obligations and intrinsic value. Any kind of business needs a wide network of supports to diversify and solidify their revenue; it needs a clearly outlined contract with coin holders to boost confidence; and it needs an organic demand backed by real-life achievements to build a sustainable growth.
3. **Fraud.** Lack of proper ecosystem leads to high percentage of fraud projects. According to Bloomberg more than 80% of ICOs conducted in 2017 were identified as scams. While not all of them are launched as scams but lack of experience and business knowledge very few of those projects go beyond the fundraising stage.

2.2 Early-stage startups

2.2.1 Fundraising on early stage is challenging

Raising funds might be one of the biggest challenges for an entrepreneur and a startup founder who is particularly focused on innovative industry. Funding on early stages can significantly help founders begin operations, hire a core team, launch product MVP.

Securing financing from early-stage venture funds comes with a loss of ownership, restrictions and heavy outside involvement that often jeopardize the growth.

3 Solution

We offer a new type of financial instrument -- Human Capital Backed Asset(HCBA) -- that is build around identity-centric investment model.

It offers entrepreneurs an opportunity to use for their endeavours something that has been only available for corporations before -- an equity financing.

It offers investors a chance to fuel the overall lifetime growth of current and future business leaders and benefit from all of the achievements those leaders are able to reach.

3.1 Identity-centric investment model

According to research done by Paul A. Gompers (Harvard Business School) and Anna Kovner (Federal Reserve Bank of New York), the entrepreneurs who succeeded in a prior ventures have a 30% chance of succeeding in their next venture. By contrast, first-time entrepreneurs has this chance at 18% and those who failed before reach 20% mark.

One of the key conclusions of this research is echoed by general assumption of any traditional financial model -- the past performance is a strong indicator of future success.

Based on the findings above, we can propose an alternative investment model with focus on iterative nature of personal success. In other words, we can propose a new model, where the owner of key metric (entrepreneur) becomes an object of investment.

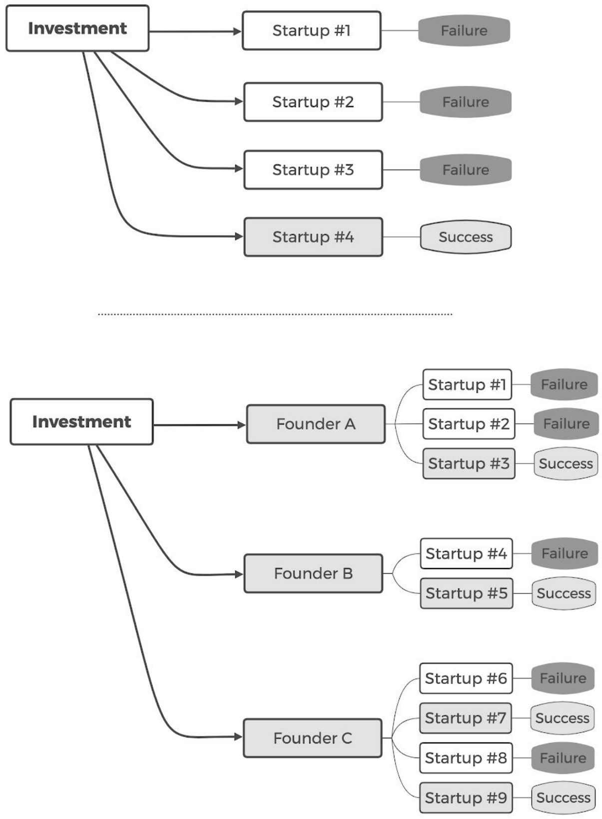

Figure 2: VC model (top) and Identity investment model (bottom).

Figure 2 shows that investing in a serial entrepreneur, unlike in enterprises, highly increases the chance of the eventual “breakthrough”. The achievements of a certain person is accumulated throughout lifetime through business endeavours, personal projects and outside investments.

3.2 Identity capitalization and HCBA

The economist Theodore Schultz invented the definition of "human capital" in the 1960s to reflect the value of human capacities. He believed that human capital was like any other type of capital, and it could be invested through education, training and enhanced benefits that lead to exponential improvement in the quality and level of production.

In other words, human capital is an economic value of a personal skill set. The concept of human capital recognizes that not all the labor is equal and that the quality of personal skills can be improved by investing in them; the education, the experience and the natural abilities all have their economic value.

We also believe that people is the most valuable asset of any enterprise and we have created a platform where one can invest in development, growth of an individual who they deem to be worthy.

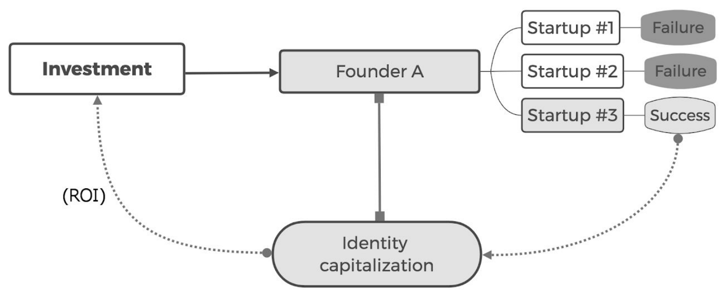

Figure 3: Identity capitalization.

Figure 3 shows the model of Identity capitalization and direct relationship between entrepreneurs success and generated capital through the **HCBA**. The major difference from the enterprise model is that the capital is not bound to a particular project but for an entrepreneur (business owner).

The growth criteria for identity capitalization and HCBA coincide with the criteria in traditional capital models, where the growth of the project's capitalization correlates with the total market value of the project's assets, it’s intrinsic value and investors belief in success.

3.3 Intrinsic value of HCBA

3.3.1 Secured by personal reputation

In the modern society a personal reputation often equates brand’s reputation. As the internet has allowed businesses to become more visible, business leaders became representatives for the values of organization. Reckless tweet or unmindful comment made by a person can steer chaos and materialize in heavy losses.

HCBA is build to monetize the value of personal brand, skills and track record. The lifetime of continuous success created by founding enterprises and other endeavours is translated and captured in the continous growth of personal token

3.3.2 Dividend payout

While personal track record provides a direct support for the market appreciation, we understand that hard money tied to a certain asset provide much better stability, clearer expectations and supported growth.

That is why every HCBA has a number of built-in options for dividend payout model. That way investors and HCBA issuer can negotiate a mutually beneficial scheme of channeling direct material representation of one’s success to his or her supporters.

3.4 Fraud prevention

3.4.1 Crowdtraction

Crowtraction model has been created to protect investors interest and to ensure a safe investment process which managed as a sequence of stages of unlocking raised funds for Identity owner.

It is a model of quarterly evaluation of the asset issuer’s progress during each of 10 consecutive quarters. The valuation is performed on the basis of the volume of contributions reclaim operations for the current quarter. A positive quarterly evaluation means a gradual (quarter-based) unlock of the raised funds.

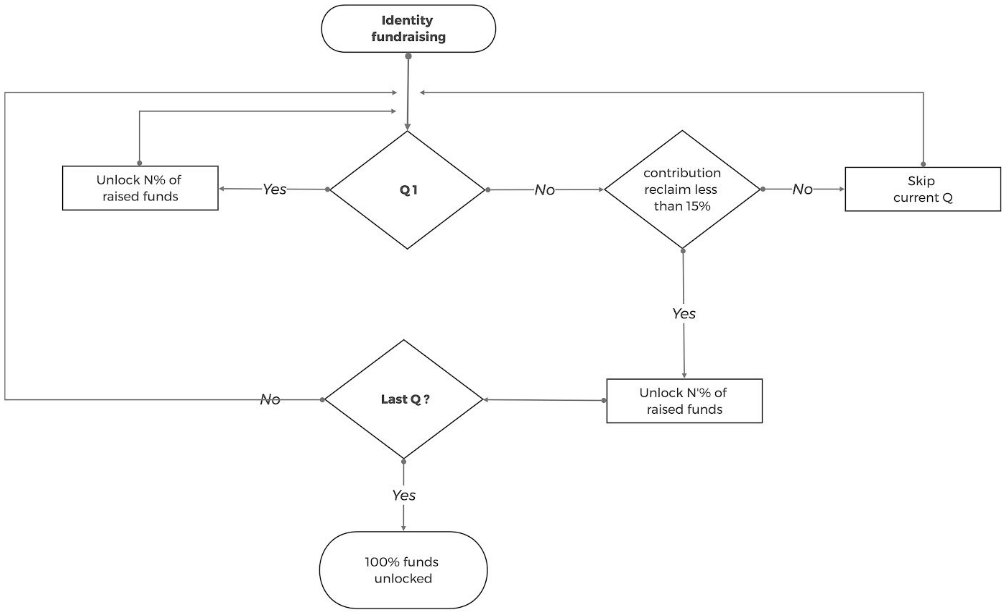

Figure 4: Crowdtraction model.

Figure 4 shows the model's unlock mechanism, where N% is fundraising unlock rate for the current quarter (see Table 1). For example, if for the current quarter the amount of contribution reclaims exceeds 15%, there will be no funds released this quarter and possible release is transferred to the next quarter.

Quarter	Q1	Q2	Q3	Q4	Q5	Q6	Q7	Q8	Q9	Q10
Fundraising unlock (N%)	30%	35%	40%	45%	50%	60%	70%	80%	90%	100%

Table 1: Fundraising unlock model.

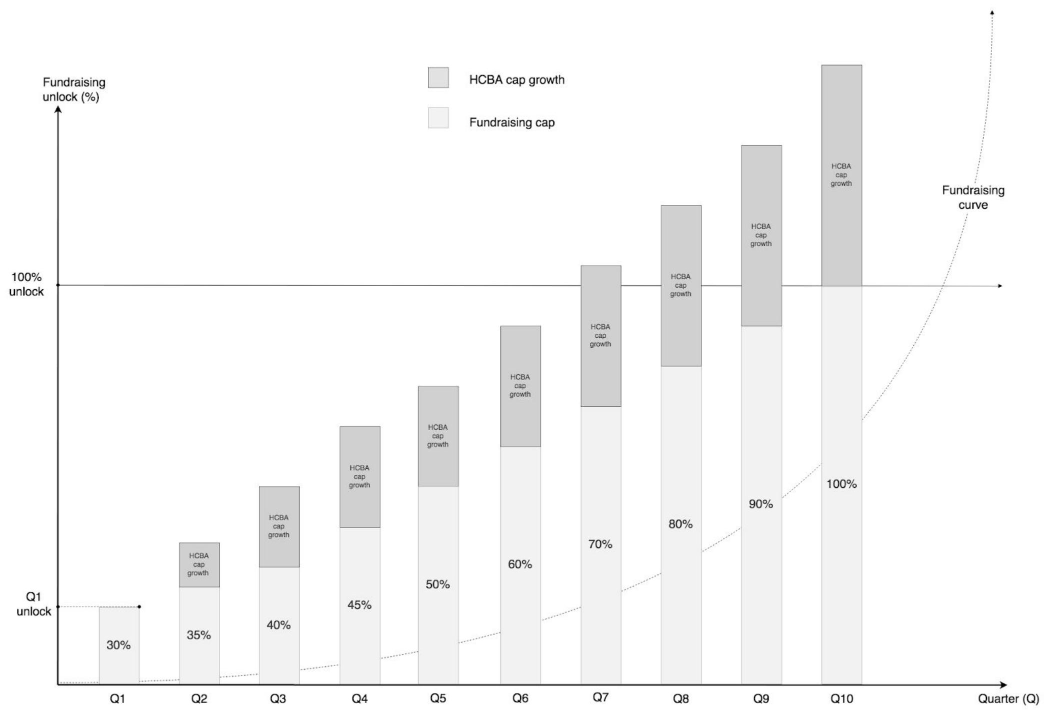

Figure 5: Fundraising diagram.

3.4.2 Contribution reclaim

Contribution reclaim is a safety mechanism for HCBA holders. If investor is not confident in the future of his or her contribution and prefers to withdraw the funds before equal share of HCBA has been released to the external exchange, it could be done with contribution reclaim operation.

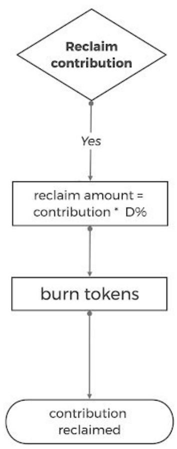

Figure 6: Contribution reclaim.

Contribution reclaim allows to withdraw D% of the initial amount of funds contributed. Assets that has been reclaimed are subject to destruction or asset burn to limit possible dilution.

Table 2 shows the calculation of parameters N% and D%, depending on current quarter.

Quarter	Q1	Q2	Q3	Q4	Q5	Q6	Q7	Q8	Q9	Q10
Reclaim rate (D%)	80%	75%	70%	65%	60%	55%	50%	45%	40%	35%

Table 2: Contribution reclaim model.

3.4.3 Decentralized emission

Decentralized emission prohibits human interference in the issuing of assets. The process is completely under the control of a cryptographic algorithm that follows the rules of a peer-to-peer (P2P) blockchain.

Furthermore, the system cryptographically rejects any attempt to change or crack the data on the number of issued asset units that does not conform to the rules of the entire blockchain.

3.5 ROI

Return on the HCBA investment is driven by two major forces of the traditional stock market: market appreciation and dividend payouts.

As the entrepreneur behind the HCBA reaches new results, validated by crowdtraction, value of his personal brand grows along with HCBA market price. Hence, by using intelligent analysis to pick the HCBA an investor can build a portfolio that will appreciate in value over time.

Additionally, an entrepreneur behind the HCBA can decide to buy back part of his outstanding emission, pushing price even higher. The possible dilution is controlled by crowdtraction model where release of additional assets is only possible after a value-increasing event has happened.

Dividend payouts also play a major role in the asset value, as with stock dividends -- future cash flows can be discounted to the present value and adjusted for growth to determine an intrinsic value of the HCBA.

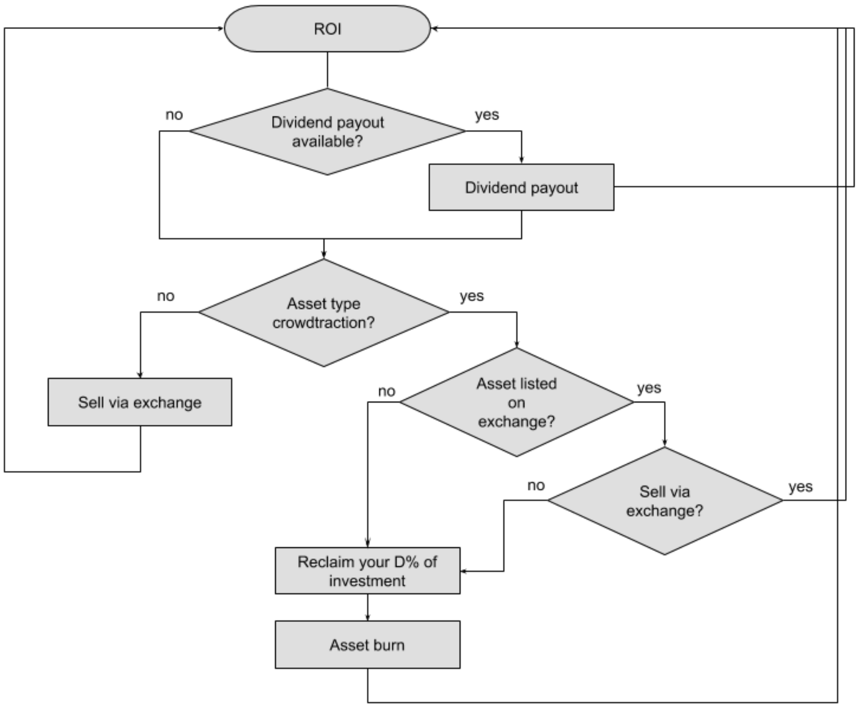

Figure 7: ROI

3.6 Liquidity

In essence, the Identity Fund offers public liquidity for the private investments. After HCBA is traded on the internal exchange, there is an active market for this asset. Therefore any exchange participant is able to liquidate his holdings at any given time by selling HCBA to the broader market.

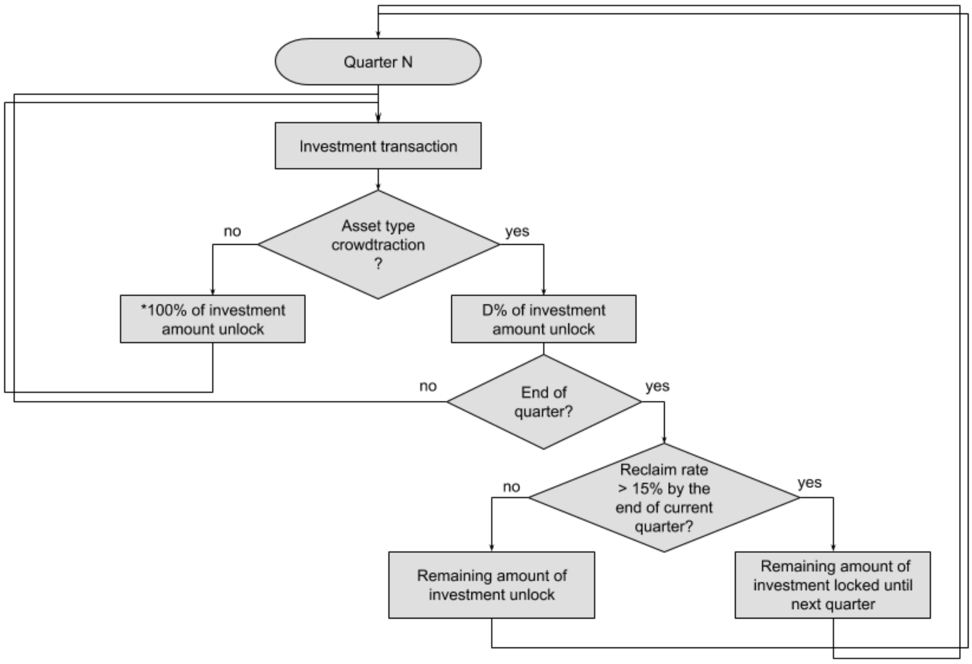

Figure 8: Liquidity

4 Platform overview

Identity Fund is a one platform for human capital backed assets (HCBA) issue, crowdtraction and exchange.

Platform consist of:

1. **Profiles** - open profiles to validate issuers traction, experience and background
2. **Marketcap** - market cap ranking and asset indicators
3. **Explorer** - detailed information about contributors, transactions, addresses, blocks
4. **Portfolio management** - portfolio analytics and strategies
5. **HCBA exchange** - internal HCBA exchange

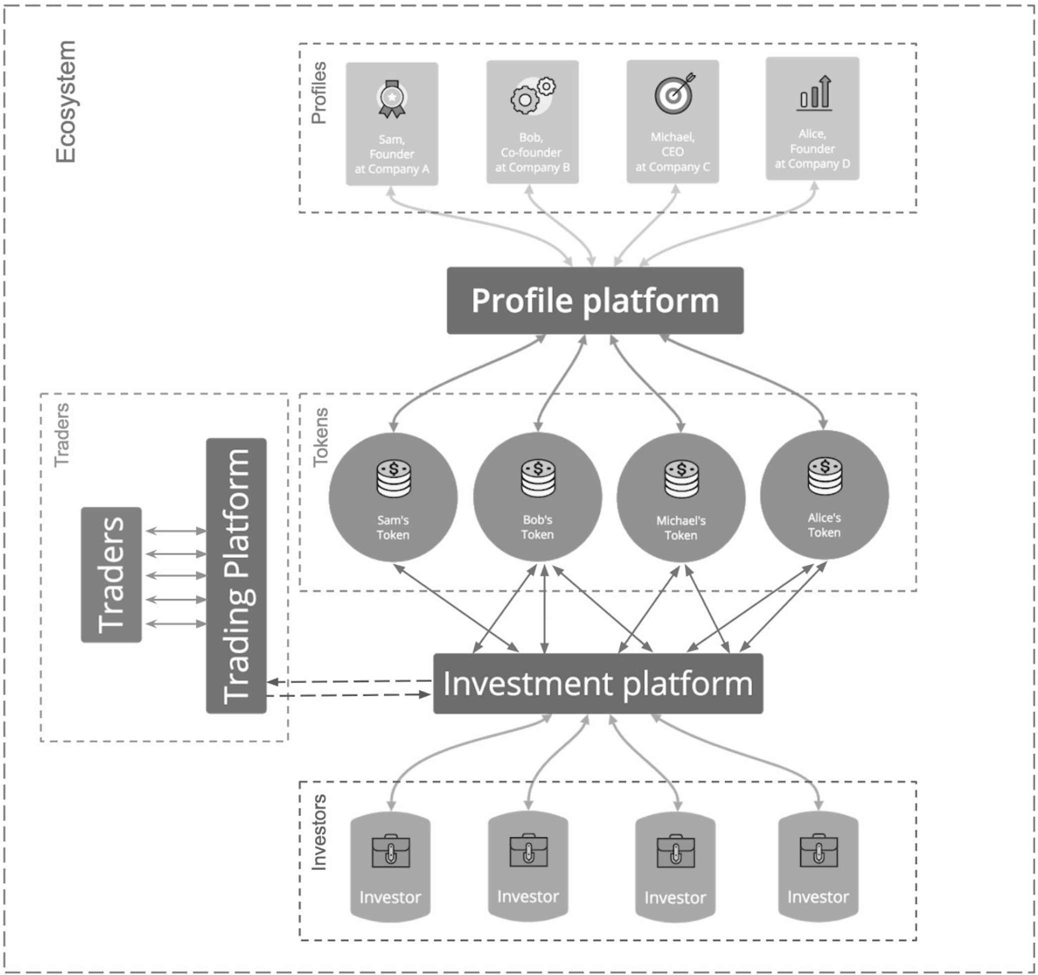

Figure 9: Platform overview.

5 Business model

Platform business model includes a few channels of monetization for different target audiences of users.

Figure 10: Business model.

Transaction commission

The main source for the ecosystem monetization is the transaction fee for the internal exchange for Identity tokens. We plan to start with a fixed fee of 0.20% and gradually reduce it with the turnover growth to facilitate smoother pricing and more stable and efficient market.

Identity token issue fee

Identity owner also has to pay for listing identity token. This fee will be channelled towards verification, fraud protection and overall system stability. The profile registration will always be free.

Investment portfolio management

With the growth of network, the process of profiles / identity tokens segmentation will become more advanced. Investment platform should include additional tools for investment portfolio management, analytics and monitoring. This tool should be offered on a monthly subscription model.

6 References

1. Friedrich Hayek. Denationalisation of Money: The Argument Refined. (1976)
2. Satoshi Nakamoto. Bitcoin: A Peer-to-peer Electronic Cash System. https://bitcoin.org/bitcoin.pdf.
3. Paul A. Gompers, Anna Kovner, Josh Lerner, David S. Scharfstein. Harvard Business School. Skill vs. Luck in Entrepreneurship and Venture Capital: Evidence from Serial Entrepreneurs. https://papers.ssrn.com/sol3/papers.cfm?abstract_id=933932
4. Yongwook Paik. Olin Business School. Serial Entrepreneurs and Venture Performance: Evidence from U.S. Venture-Capital-Financed Semiconductor Firms. https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1632717
5. Paul A. Gompers, Will Gornall, Steven N. Kaplan, Ilya A. Strebulaev. Harvard Business School. How Do Venture Capitalists Make Decisions? https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2835825
6. Piotr Denderski. University of Leicester. A Model of Confounded Entrepreneurial Choice. http://www.tinbergen.nl/wp-content/uploads/2015/06/denderski_jmp_oct29.pdf
7. Paul A. Gompers, Josh Lerner. What Drives Venture Capital Fundraising? https://papers.ssrn.com/sol3/papers.cfm?abstract_id=226390
8. Eric Garton. Harvard Business Review. The Case for Investing More in People. https://hbr.org/2017/09/the-case-for-investing-more-in-people
9. A. Miguel Amaral Rui Baptista. Serial Entrepreneurship: Differentiating Direct from Latent Re-entrants.
10. Kristian Nielsen, Saras D. Sarasvathy. Dept. of Business Studies, Darden School of Business. Who reenters entrepreneurship? And who ought to? An empirical study of success after failure. http://www.lem.sssup.it/WPLem/documents/papers_EMAEE/nielsen.pdf
11. CBI Insights. insights Venture Capital Funnel Shows Odds of Becoming a Unicorn Are Less than 1%. https://www.cbinsights.com/research/venture-capital-funnel-2/
12. Eric Levitz. U.S. Stocks Just Erased All Their 2018 Gains. Here’s Why. http://nymag.com/intelligencer/2018/11/why-is-stock-market-falling-dow-nasdaq-sp-bonds-tech-stocks.html