

Making fintech work for fintechs

The state of equity and cap table management
for UK fintech industry founders





Taking a deep dive into the complexities of equity management, this report highlights a critical need for fintechs to adopt new ways to manage equity and the potential impact of COVID-19 on the fintech sector.

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Foreword

Fintech businesses are the beating heart of the UK tech sector and can be seen as a proxy for the wider start-up community given financial tech has been Europe's largest investment category¹ since 2013.

Over the last decade, the industry has been the source of hundreds if not thousands of innovations that have revolutionised financial services as we have known it. Today, managing company books has never been easier, sending and receiving payments is less costly and accessing new products like business loans has become far more streamlined. And this is only a tiny snapshot of what the sector has achieved in a few short years.

But while fintechs have transformed an array of legacy sub-sectors such as insurance, lending, personal finance payments and regtech, there is at least one area which remains starved of innovation. Equity management is integral to the success of a fintech company, yet many fintech founders are relying on outdated, analogue methods to manage their companies' equity. This could spell wasted time, lost funding, and missed opportunities for the industry as a whole.

These findings come at a time when the fintech market is rapidly trying to conserve resources and drive revenue amid the fallout of the global COVID-19 crisis.



Julian David, CEO

tech^{UK}

The UK's fintech industry is a true success story. The nation is a world-leading hub for financial technology and is often recognised at a global level for what it has achieved in such a short time.

However, companies are still seeing areas where innovation can go further in expanding and improving the sector. The area of business administration of equity management is one such example.

Equity management is both complex and time-consuming. Fintech founders and CEOs want to devote their time to the growth of the company, its strategic direction or helping craft its next product but the admin surrounding key business functions such as cap table management can be overwhelming.

This issue is having an impact on fintech companies and may not only be detrimental to the growth of a company but the entire industry.

To guarantee the UK's future at the centre of a sector that attracts the most European investment, it is vital that business processes continue to be made more efficient, particularly as we emerge from this current crisis.

Without the right support, the start-up community will struggle to take advantage of what is a huge growth sector and opportunity will be lost.

Equity management has been overlooked for a long time. The insights contained in this report help us to understand how it is impacting growth at a company and national level.

This study is essential reading for any founder who wants to build a more efficient company, it is time for UK fintech firms to find better ways of managing equity.

¹ Finch Capital and Dealroom.co, The State of European Fintech, October 2019



Executive summary

The fintech industry has been booming. In February, it was revealed that the UK had secured £37.4bn of fintech investment from 2018-2019¹, a 91% increase from the previous year. And the health of the fintech sector can be seen as a proxy for the wider startup scene, given financial tech has been Europe's largest investment category since 2013.

But things are fast changing. The sector, like many others, is now facing an unprecedented crisis. COVID-19 is stifling the global economy, and the fintech industry is no exception. There are now a number of question marks around how much investment will continue to flow into the market and whether some companies will disappear altogether.

The pressure is truly on for founders. Yet even before COVID-19 emerged, the fintech industry, which is known for its innovation, had been plagued by inefficiencies.

Equity management has been particularly challenging and cumbersome. Securing funding is intense but high-value and so exactly where a founder wants to spend their time. The administration? Not so much. Requiring a detailed understanding of the minutiae, the management of equity can be hard to understand, and many often fall back on basic tools like spreadsheets, or even pen and paper to manage.

Tracking and managing equity percentages, communicating updates to investors, and modelling funding rounds requires precision, close management, and consistency. It does not necessarily require the hours of manual calculation that are currently devoted to this essential company administration.

What is the impact of the time attributed to equity management instead of more strategic business functions? To understand this impact and assess the extent to which equity management challenges correlate to overall company success, Qadre conducted an independent survey of 59 UK fintech founders.



¹ KPMG, The Pulse of Fintech H1 2019



Executive summary continued

This whitepaper is the result of the survey and reveals insights across four key areas of capitalisation table (cap table) and equity management:

Building and managing of cap tables today

For 86% of founders, the current demands revolve heavily around the issuing of equity, with some founders (17%) stating it takes them up to a year to issue equity. There is a significant time and cost investment with external support needed to set-up cap tables and equity management processes.

The founder

23% of founders stated that they did not have a good understanding of cap table and equity management with one in three (34%) finding the process 'painful' or 'very painful'. Overall, a surprising seven in ten (73%) still use Microsoft Excel or Google Sheets to manage equity and over two thirds (67%) believe time spent on equity management would be better invested elsewhere.

The company

61% of founders believe time spent on closing investment rounds has impaired their ability to successfully scale the business, run the company, or deliver a product. Time spent and lost on operational costs or equity management has contributed to delayed projects, inhibited business growth, and missed funding opportunities.

The industry

Significant amounts of investment are potentially missed because of complicated cap table management to the tune of £2.6bn in total. Across the industry 4,640 days are lost because of the amount of time invested in cap table management, which equates to almost thirteen years! Further investment has been lost due to the COVID-19 pandemic, 68% of founders say they have missed out on up to £500k in funding. Extrapolating that by the number of fintech businesses in the UK, it is estimated that over £1bn of UK fintech investment could be lost because of COVID-19.

The results reveal that the time dedicated to equity and cap table management spells lost time for founders, delayed product launches, and lost funding for fintech businesses - overall, billions of pounds in missed opportunity for the wider UK fintech market.

To combat these challenges, founders must consider introducing new processes and technologies which can automate the time-consuming management of equity. The hours spent manually calculating and modelling equity are overlooked but could be costing early-stage businesses vital resources that could see them hitting key company milestones.



Introduction

Being a company founder is highly demanding with responsibilities ranging from acquiring clients, recruiting talent, building products, and setting the company's strategic vision. But it also includes the minutiae of managing company formation, cap tables, and investment structure. And now COVID-19 is bringing with it more pressures including the need to focus on profitability, and answer questions around job security and the long-term impact of a downturn on the sector.

Prior to this research, studies showed that companies currently spend between £6,000 and £20,000¹ on business administration in their first year but, until now, the impact of equity management challenges on the success of a company has been relatively unexplored.

Fintech founders, who are themselves building solutions to streamline inefficiencies across financial services, should be relatively advanced in solving the challenges that equity management poses to start-ups. However, this is simply not the case. In fact, many are relying on outdated, archaic methods to manage equity, which could be affecting everything from a founder's capacity to take on more strategic functions, a business' ability to acquire funding, and the market's ability to progress and innovate.

To assess and quantify the true impact of equity management challenges, Qadre has conducted an independent survey of 59 UK fintech founders. This report presents the findings which reveal:

- The current demands of cap table and equity management within fintech businesses.
- The challenges founders experience with equity management and funding-related administration.
- The correlation between equity management issues and overall company success.
- The wider market-impact these challenges are having on the industry and the impact of COVID-19 on funding.



¹ How much money does your start-up need to survive the first year?', The Telegraph



Key findings

Building and managing a capitalisation table today

A start-up’s capitalisation table (cap table) is a record of who owns the company. It’s a live reference point of a company’s shareholders (founders, investors, employees) denoting how much each party owns, the class of the shares owned, the price assigned to those shares and therefore, the overall distribution of equity. A cap table might also include rights to purchase additional equity in the future, vesting schedules, voting percentages and purchase price.

The study revealed that the most common trigger requiring updates to a company’s cap table was issuing equity, with 86% of respondents confirming that they had done this. A further 46% of respondents said they had established employee share schemes and 34% had issued options. But this only accounts for the initial set up. A company’s cap table needs updating every time the company makes a new hire where equity is involved, every time new investors are onboarded or where options are tied to employee promotions or performance. And for those with a vesting scheme, their company’s cap table will change at least every month.

“ 17% of respondents said that it could take up to a year to clear a funding round.

Founders also need to educate employees and non-professional stakeholders around what it means to hold shares and statutory rights. For private limited companies, there can often be a large mismatch between the layperson’s understanding of being a shareholder and the reality (e.g.: owning “x% of a company” vs “y shares out of z current existing shares”).

This problem is compounded when companies are actively seeking funding. The data showed that the average time taken to clear a funding round varies significantly. More than half of respondents (54%) said that the process could take up to three months from the opening of funding rounds to the issuing of shares but as many as 17% cited this could take up to a year. Each offer and counter-offer means a founder must recalculate the modelling of their round and alert existing investors of potential changes to the cap table, dragging out an already lengthy and complex process.

As a company matures, growing its revenues, securing additional investment and procuring talent, its cap table becomes increasingly complex at a time when founders most need to lean into their businesses to take advantage of what’s working and fuel further growth.

There are also a number of firms who choose to outsource their equity management to external specialists - usually lawyers. Almost a quarter of fintech founders (24%) admitted to spending over 10 hours per funding round on professional advice to structure their investment. This external support is costly. As many as 35% said they had spent up to £5,000 on legal and accountancy fees to set-up and manage their equity and a further 28% admitted to spending over £20,000.

Chart 1. How much have you spent on legal and accountancy fees to-date to set up and manage your equity?





Key findings

The founder

Typically, the burdens of cap table and equity management fall to the company founder. The findings in this report refer to the 59 founders from a total of 63 who said they were responsible for cap table management within their company.

The trouble is, it's a responsibility for which founders aren't well-equipped. Almost a quarter (23%) of fintech founders admit they don't have a good understanding of cap table requirements. And beyond the complexity, it is also time-consuming to set up and manage. Almost a third of founders (29%) said it took them more than 10 working days to set up their equity structure; including obtaining legal advice, educating themselves and communicating with stakeholders. It is time that many founders simply do not have.

“ When asked how they manage their cap table, one respondent even said “simple mathematics on a napkin”.

The reality is, founders are relying on tools which were not built for complex equity management. Over seven in ten (73%) still rely on spreadsheets such as Excel or Google Sheets to manage their cap table and model investment rounds. One respondent even said “simple mathematics on a napkin” was their answer to equity management. As it remains a manual process for the majority of founders, it comes as no surprise that nearly a third (31%) admitted managing their cap table is ‘painful’ or ‘very painful’.

Founders who are not using spreadsheets are spending thousands of pounds to outsource their cap table management to a professional services firm. The remainder of survey respondents said they either used an online tool (27%) while almost a quarter (24%) defer to their legal team on equity management. While 21% firms spend less than £5,000 on these services, almost one in three spend over £20,000 for the cost of these services.

“ 1 in 4 shareholder or director disputes results in a significant legal and opportunity cost for the business.

A well managed cap table not only provides founders with a sense of control and the ability to take on new hires quickly or make speedy decisions around investment, it can also help with shareholder or director disputes. According to the findings, 25% of founders have been involved in a shareholder or director dispute of which almost 1 in 4 (24%) states had resulted in a significant legal and opportunity cost for their business. These disputes can be expensive, painful, and lengthy, the brunt of which could be minimised with a more robust way of managing and proving data in statutory registers - via a company's cap table.

For example, if a former company director attempted to falsify records, this could impede the company's ability to perform any corporate action and result in six figure legal fees. Yet, managing these records in an indisputable arm's length manner could have easily prevented the costs from occurring.

Chart 2. How do you currently manage equity?
(e.g. capitalisation tables, vesting option schemes and round modelling)





Key findings

The company

Beyond the pain and operational headache for founders, equity management presents a serious challenge at a company level and is a critical factor holding businesses back. Until now, equity management was viewed as painful but for the first time, this research reveals a direct link between cap table challenges and wider company success.

“ 61% of founders believe the time spent on closing investment rounds has impaired their ability to scale the business, run the company, or deliver a product.

More than two thirds (67%) of the founders asked believed that time spent on equity management was a distraction from growing their core business.

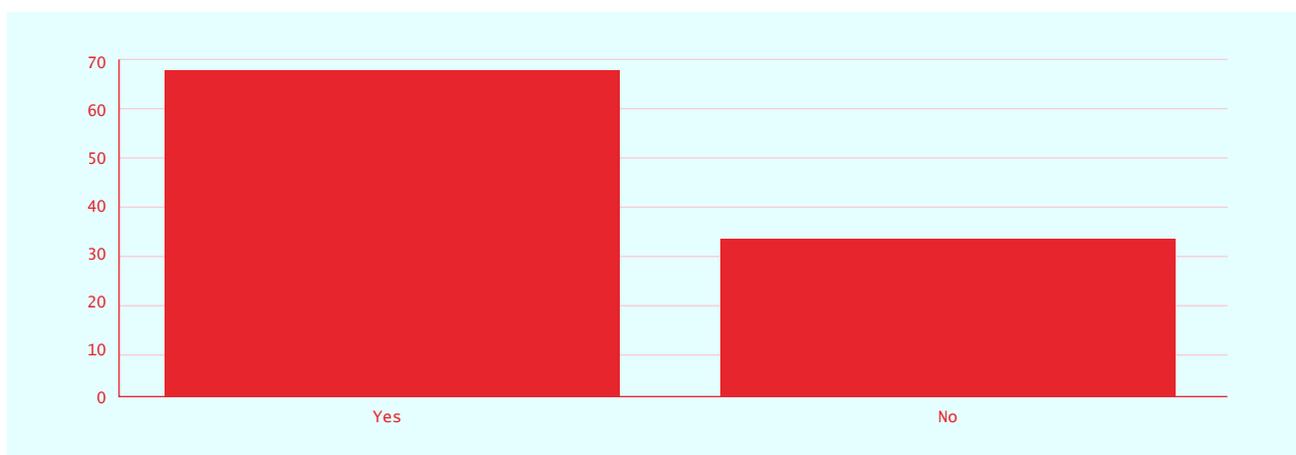
Although the ongoing administration around investment and equity management may seem like a relatively small responsibility, 61% of founders believe the time spent on closing investment rounds has impaired their ability to scale the business, run the company, or deliver a product.

What is more, time spent and lost operational costs through equity management has significantly affected investment, growth, and progress against key milestones. When asked about the specific impacts:

- More than a third (35%) of founders had delayed projects within the organisation due to the time and costs of equity management
- 31% of founders said this problem had inhibited business growth
- Almost one in five had lost out on vital funding (19%)

It's clear. Challenges around equity and cap table management are not only causing pain but impeding company success. The true impact is likely far worse, stopping many companies from obtaining any funding and therefore writing them off before they've begun. Despite these consequences, 63% of all respondents who said they used technology to automate the fundraising process, invested just £1,000 or less on tools which would support cap table management.

Chart 3. Do you feel the time spent on equity management would be better spent focusing on your core business or that managing your cap tables is a distraction from growing your core business?





Key findings

The industry

From all of this data it looks as though the very industry that champions innovation at every turn is stuck in a rut. Managing equity is a slow, outdated process, which is actually impacting the welfare of these businesses. Fintech just isn't working for fintechs.

What effect is this having on the market as a whole? The study reveals that a huge amount of investment is potentially being lost, both for individual companies and across the market as a whole.

“ The time dedicated to equity and cap table management spells lost time for fintech founders, delayed product launches and lost funding for fintech businesses and billions in missed opportunity for the wider UK fintech market.

Based on the total capital raised by those surveyed, we can estimate that the average fintech business has raised around £8.6m in funding. With over 1,600 fintech businesses currently operating in the UK (as of 2019, source: Fintech: State of the Nation report) and 19% of the surveyed respondents stating they had missed out on vital funding, equity management challenges could be costing the UK fintech industry approximately £2.6bn in missed funding.

Furthermore, almost a third (29%) of founders said they spent 2 working weeks on setting up their equity structure. With the average weekly salary (as of 23 April 2020, source: Glassdoor) of a UK founder being £1,336.94k, this equates to £4.2m of resource across the market that could be better at the core of fintech businesses.

That's more than 34,800 hours or 4,640 working days spent on setting up cap tables overall.

COVID-19: An added stress to the industry

The COVID-19 pandemic is creating challenges for businesses across the world and fintech is no exception. As funding sources evaporate and exit options change significantly, fintech firms will find themselves scrutinised on profitability, customer demand, working capital, business models and the ability to retain talent, all while they are trying to put customers first.

In these times of uncertainty, every fintech business is at risk. At the time of surveying, 68% of founders stated COVID-19 has had an impact on their ability to secure funding. On average, founders estimated that they had lost out on approximately £1.2m. With the UK home to over 1,600 fintech companies, that spells as much as £1.9bn in lost investment across the industry due to the crisis.



Conclusion

UK fintech has been one of the fastest growing and most successful sectors in the world and we haven't yet hit the ceiling.

This report shows there is a great future ahead as more fintechs are better able to manage equity through the adoption of online platforms, they will dedicate more time to their business, cut costs, and continue to raise investment.

It ties in with COVID-19 leading to the rise of all forms of digitisation. We've taken our workplaces and meetings digital and now it is time to take our cap tables digital.

The UK, and the world, has the challenge of innovating out of the recession we are just entering. This is just one way we can decrease the time and cost of managing equity, making it easier to raise finance, keeping businesses alive, providing employment, and growing our economy.

A simple, quick, and inexpensive way of managing capital could be one part of a solution that ensures UK fintech remains funded and continues to thrive. These platforms will also help germinate the start-ups that will drive future innovation and growth.

“ Fintech is capable of making fintech work for them.

Fintech is capable of making fintech work for them. The appetite is there, but founders just aren't equipped with the right tools. Fintech founders are spending time they don't have and diverting critical resources to managing company equity, despite the widespread belief that time could be better invested elsewhere in the business.

There is a huge opportunity that lies in using a cap table management platform. The industry needs a new way of doing things and fintechs must embrace fintech if they are to manage equity effectively, especially during this turbulent time.





Strategic considerations

How can companies begin to address the inefficiencies within equity management that could be costing them vital company progress? Here are five strategic considerations for founders and their companies as they look to streamline operations:

- 1 **Review cap table requirements in line with business trajectory, and whether current functionality can support ambitions for growth or innovation.**

If a fintech business has big ambitions, its cap tables need to match. Will your current equity structure support or hinder growth? Is equity management holding a business back? These are very important questions for founders to consider as they look to grow their company..

- 2 **Evaluate current cap table and equity management processes and review which elements of the process can be automated and what tools are at founders' disposal to achieve this.**

The study painted a clear picture; fintechs want and need to consider digital solutions when it comes to managing equity. Spreadsheet calculations are painful, time-consuming, and prone to inaccuracies which can cause issues further down the line. Conduct an audit of your cap table needs which will depend on company size, the complexity of your equity structure, and anticipated changes in the pipeline. Use these factors to identify the tool that is most suitable. This will save time and money in the long-run.

- 3 **COVID-19: provide clarity and reassurance to stakeholders during impactful market events.**

COVID-19 is front of mind as the market tries to anticipate what this will mean for the future of fintech. Regular communication, timely updates following new developments and reassurance is essential for assuaging the concerns of investors and other stakeholders. Doing so relies on a real-time understanding of ownership and an effective way to present the numbers so fintechs can ensure their stakeholders give them the room they need to to deliver new products, and become profitable.

- 4 **Cap table and equity management needs to be integrated from the beginning. The right cap table does not need to take a lot of time or cost a lot of money to be right for your company.**

A little time and money investment will pay dividends in the future. Businesses should use the tools available to them so they can focus on innovating and delivering value to customers. Some companies require more complex arrangements, but not all.

5. **Assess if the responsibility for cap table and equity management can be managed by other members of the business, to ensure founders can focus on strategic activities while avoiding costly legal fees.**

Accounting and finance teams, with your guidance and equipped with the right technologies, have skills that would make them well placed to support with execution. Founders need to ensure they are conserving their time for activities that are critical to their core business which means delegating the ongoing management where they can. The company's cap table is important and will require oversight but shouldn't distract the founding team from their focus on strategy and innovation.



How Qadre can help



Our QCap solution manages your cap table, so you can manage your business, with:

- Simple and intuitive onboarding, and a no-jargon approach
- Automated real-time cap table building, hosting, reporting, and management
- Easy shareholder onboarding and engagement, allowing your shareholders real-time visibility of their investment
- Simple business modelling
- Tools to attract future investors

As serial entrepreneurs, the Qadre team has experienced many of the pain points faced by modern businesses. Like many business owners, we have spent a significant amount of working capital on legal fees and many hours manually calculating equity positions and producing share certificates when raising funds. That's why we created QCap. Our platform easily and quickly creates your cap table, automates investor and government reports and helps you model your next investment round.

If you'd like to learn more, please get in touch - we'd love to hear how we can help solve your business challenges.

Find out more at qad.re/qcap/ and contact us by email contact@qad.re.

About Qadre

Qadre is a high-growth fintech trusted by leading institutions to deliver certainty and modernise financial markets with blockchain technology.

The company's modular platform, Huski, monitors, records, and reconciles any transfer of value and ownership with greater efficiency, reduced risk, and at lower cost than traditional methods. It offers a range of pioneering applications across equity management, market infrastructure, payments, and fund distribution designed to remove friction, improve security, and enhance the user experience for both the business and its customers.

The Qadre team is behind the earliest and most innovative blockchain projects to date in the fintech sector. Huski is the first blockchain technology to be approved by the UK government.

Qadre is a member of techUK and Innovate Finance.

For additional information, visit qad.re



About techUK

techUK is a membership organisation that brings together people, companies and organisations to realise the positive outcomes of what digital technology can achieve. We collaborate across business, government and stakeholders to fulfil the potential of technology to deliver a stronger society and more sustainable future. By providing expertise and insight, we support our members, partners and stakeholders as they prepare the UK for what comes next in a constantly changing world.

For additional information, visit techuk.org



This survey was conducted by FinTech Connect, an independent research partner. A total of 59 UK fintech founders were surveyed between the 25th March 2020 and 3rd April 2020. visit qad.re



If you'd like to get in touch to learn more, we'd love to hear how we can help solve your business challenges. Get in touch at contact@qad.re

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