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Pumping & Dumping in the 21st Century or: The Biggest Turd Ever Sold

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Pumping & Dumping in the 21st Century or: The Biggest Turd Ever Sold

On January 6, 2014, I wrote a letter to the shareholders of a different company [to remain nameless], "*Recently, I found out that [so-and-so] is no longer working with Goldman Sachs and instead has hired Sandler O'Neill to represent it to new investors. While on the surface, the replacement of a Tier 1 investment bank (Goldman Sachs) with a Tier 3 firm known for pumping and dumping junk companies into the public markets is troublesome enough, what lies beneath the surface of this regrettable decision confirms yet again the loss of credibility of our senior management team*."

Two days later, I received a call from a senior executive at Sandler O'Neill who wanted to know why I would disparage his firm. I mentioned the words "2013 IPO" and he immediately knew what I was talking about. It was not even necessary to utter the name of the company. He invited me to his office the next day to continue our conversation and I gladly accepted.

They were pissed. They took offense to the words *pump and dump*. Sandler O'Neill's head of capital markets made a distinction between "underwriting" and "advising". Even though they were the only name on the front of this company's prospectus, he claimed that because a minimal amount of the deal was sold to institutions the deal was somehow less of a discredit.

"That sounds worse," I shot back, "if you dumped it on retail."

He quickly clarified. Almost all of the shares sold were to friends and family – which was their ultimate justification for underwriting the sale of $28.575 million of common stock. Sandler O'Neill made no promises to this company that they would raise any capital, he said. It was pre-bought by friends and family and therefore they were merely processing the transaction or "advising". Innocent bystanders.

On the characterization of Sandler O'Neill as a pump and dump shop, I asked rhetorically, "*If you commit murder, does that make you a murderer?*"

Friends & Neighbors

On a quiet August afternoon, I was studying the list of recent IPOs at www.renaissancecapital.com when an issue from July 26, 2013 caught my attention. It was priced at $9.00 per share yet closed its first day of trading at $7.64, down 15.1% (red flag #1). There was only one underwriter (red flag #2). And finally, red flag #3 – the market capitalization was nearly $200 million yet revenues were ~$2 million. **100x revenue**!

As I read through the prospectus, I couldn't believe what I was reading. *Pumping and dumping in the 21st century*, I thought. The gross proceeds from the offering were $28,575,000 yet net proceeds to the company were only approx. $17,400,000. That means IPO expenses were $11,175,000, representing an unprecedented 39.1% of IPO proceeds, or at least unprecedented since the boiler room days of D.H. Blair and Stratton Oakmont.

And then I was stunned by what I discovered next. My neighbor and friend, [to remain nameless], is this company's General Counsel and Secretary. When I later confronted him about his new job, he said the opportunity to take a company public is what drew him in. He knew nothing about the software his company developed and asked me to evaluate it.

Not only am I the target customer for this software but also I founded a software company in January 1998, Blackwood, that developed a very similar product. The company I co-founded with the late great Craig Schlifstein developed electronic direct access trade execution software and was the first company to offer smart order routing to institutions. Products included applications for single order entry, list trading, and index arbitrage as well as a FIX enabled API connecting incumbent front-end applications to Blackwood's smart order routing servers. While I was CEO of Blackwood, our proprietary technology executed over 100,000 trades and 30 million shares per day on behalf of its professional and institutional customers.

During the years I spent managing technologists on a day-to-day basis, I learned not only how to talk to technologists but also to discriminate between who is real and who is fake. As a direct result, I have an edge over other technology investors who have never been involved in the building of technology. Moreover, my specialty is trading technologies, market participants, and what I call *the evolution of market structure*. The story of Blackwood is a boom and bust morality tale I save for another day. Instead, I focus my analysis on the current state of trading technology, a segment within technology that hasn't evolved since 2003. I personally use or have used the following trading technologies – RediPlus (Goldman Sachs), Neovest (JP Morgan), Cybertrader (Schwab), Anvil/Hammer/Blackwood (SunGuard), LiquidTrade (LIQD) – and I cannot discriminate between them. Innovation arrested ten years ago when all of the technology talent on Wall Street was hired away by the high frequency traders (HFT), leaving basic trade execution technology to the turd polishers.

These days I use Neovest for my electronic trading, simply because I get it for free from the brokerage firm I clear trades through – Pershing/Bank of New York Mellon (BK)[1]. While Neovest is a fine product, it is virtually unchanged in more than a decade and no different than anything else out there. Standard practice for an executing broker is to bundle the execution software for free. No one pays for trading software. I never have. I pay a penny per share executed, the service is decent, and I'm happy to pay it.

Is there anything that would convince me to pay out of pocket for trading software that I otherwise get for free? Perhaps a technological breakthrough? How about a ***quantum leap in hedge fund technology?***

The day after I read the prospectus for **Liquid Holdings (LIQD)**, where my neighbor works, I met after the market closed with a friend [who shall remain nameless] who is a hedge fund manager who focuses on the technology, media, and telecommunications (TMT) industries. He told me about a new client, QuantX Management, a multi-strategy fund that opened a $5 million separate account with one caveat – my friend must use LiquidTrade to execute his trades.

When I heard the word *LiquidTrade*, I flipped out. This is predestined, I thought.

“Let me get this straight,” I was breathless. “They gave you $5 million of trading capital and you only have to use their software..?”

“I keep 50% of the profit.”

“50%,” I repeated in awe.

[1] Pershing/Bank of New York Mellon (BK) licenses Neovest from JP Morgan (JPM).

"Less a 1.5% asset fee."

"So you get 48.5%..."

"Yes. And they pay quarterly."

"Sign me up."

My friend introduced me to the Chief Investment Officer of QuantX who eagerly signed me up. At first, I was allocated $1 million, which was soon bumped to $2 million. By February 2014, I was up to $5 million in buying power. I am paid 48.5% of my profit generated on a quarterly basis, less certain market data and other expenses[2], after which I turn around and pay Liquid $1,845 on a monthly basis ($5,535 quarterly).

I was scheduled to go live on LiquidTrade on Monday November 4, 2013. As I waited for the URL and login/password information, I was eager to test drive new software. At around 11:00am, I was given instructions to download the software and was immediately perplexed. Why am I downloading anything? Nevertheless, I followed the instructions and downloaded this monster piece of software on my desktop computer – the biggest turd I ever saw. It swallowed processing capacity and slowed everything down. I couldn't connect to Liquid's servers, of course, and as the minutes ticked away I became progressively confused. I called tech support and asked about ***the cloud***.

"There is no real cloud version of the software," tech support explained.

"Huh? I don't understand."

"There is no real cloud version **yet**," he re-explained.

"When will it be ready?"

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[2] In the first quarter of 2014, I was paid $40,430.54 out of gross trading profit of $104,222.90.

"I have no idea."

"More or less than 6 months?"

"More."

"How am I supposed to trade on my laptop? This piece of shit will kill it."

"You can use Citrix."

"Explain."

"You can download a Citrix receiver and we can set up a virtualized instance of the software for you."

"That means the software is located in the cloud and not on my machine, correct?"

"Yes."

"But I still need to download a Citrix receiver, which is still a piece of software."

"Yes."

What I learned that day, the day I was supposed to start trading with Liquid/QuantX, is that in order to use LiquidTrade, you must download physical software. There is no simple website to log into, no cloud to access. I asked tech support if I would be able to access LiquidTrade from someone else's computer, for example, from the computer at the hotel in Mexico where I would be staying with my family over the holidays.

Of course the answer was no. Liquid's self-proclaimed "Born in the Cloud" technology is a complete fraud. Not only was the software not born in the cloud, there is no cloud today.

As far as the other two pieces of Liquid software, they are fraudulent as well. LiquidMetrics is a generic website that shows basic account and trading information in real time. It appears to have been developed by a hobbyist or an auto program. There is no way to query information, customize reports, or personalize anything. The description of it on the website is a series of lies, or hopes for what this basic website could become. LiquidView is what they call their *proprietary shadow accounting, reporting, fee management and transaction cost analysis database*. This may be the biggest fraud of them all. LiquidView is not even software. Every day I receive an email from Liquid that has an excel workbook attached containing updated account and trading information. It's exactly the same information I can get from LiquidMetrics, the only difference is how that information is distributed – via website or email. The generation of a report from a database does not constitute software in the same vein that a Citrix receiver does not constitute cloud. Parsing words is one thing, this is pumping and dumping in the 21st century.

When I returned to my neighbor, he was sadly not surprised. He thanked me and we hugged.

Back at the meeting at Sandler O'Neill's office, when I mentioned the name of my friend and neighbor, the Sandler O'Neill executive's eyes widened. I said, "I'm worried about him. I'm worried about my friend."

"I understand," he said with solemn sincerity. "If what you say is true then you should be."

A Classic Pump & Dump

The founders of **Liquid Holdings Group, Inc. (LIQD)** (“Liquid” or the “Company”), formed January 17, 2012, contributed $1,511,969 of capital to fund the acquisitions of the pieces of technology that cobbled together would become Liquidtrade, LiquidMetrics, and LiquidView, three products that sold together constitute the Liquid Platform.

LIQD Capitalization as of 12/31/13	
Price as of July 26, 2013 IPO	**$9.00**
Price at end of 1st day of trading	**$7.64**
Price as of December 31, 2013	**$6.94**
FD Shares Outstanding	24.8
Market Capitalization	**171.9**
Cash	8.5
Debt	0.0
Enterprise Value (EV)	**163.4**
EV / Revenue - 2013A	55.9x
EV / Revenue - 2014E	27.2x
EV / Revenue - 2015E	23.1x

In addition to the $1.5 million of capital contributions, Liquid raised $4.3 million in September 2012 via the acquisition of an entity called LTI, LLC, formed by the founders, Messrs. Schaeffer[3], Ferdinand and Keller. This transaction was followed by the sale of $12.5 million of common stock to an entity controlled by Mr. Douglas Von Allmen in July 2012. Liquid also raised $3.3 million in aggregate via six transactions completed in January 2013, February 2013 and March 2013.

“Why did you go public?” I asked my friend and neighbor.

He sighed, but then replied with sincerity, “I was told it would help with marketing. The larger companies that we could do business would prefer us to be a publicly traded currency.”

[3] Mr. Schaeffer resigned from the Board of Directors on December 23, 2013.

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"That is nonsense."

In order to complete Liquid's IPO in July 2013, insiders purchased $16,200,000 of the $28,575,000 of common shares sold – an extremely unusual (and phony) source of demand – leaving $12,375,000 of shares sold to the unwitting public. Net proceeds as a percentage of gross proceeds equal to 60.9% (39.1% of IPO and related expenses) is so low it evokes D.H. Blair, Stratton Oakmont, and the other boiler rooms of the 1980s and 1990s.

The Liquid Holdings (LIQD) IPO - Use of Proceeds	
Cash Contributed prior to IPO (LTI = 4.3M; Von Allmen = 12.5)	18,850,000
Cash at 3/31/13	4,166,196
Gross Proceeds @ $9 per share (1)	28,575,000
6.5% Underwriting fee payable to Sandler O'Neill	1,857,375
Proceeds, before expenses	26,717,625
Use of Proceeds	
Repayment of Loan to Mr. Schaeffer	251,000
Repayment of Loan to Ferdinand Holdings	251,000
Repayment of Loan to Thomas Ross	250,400
Repurchase Shares from Mr. Storms	883,575
One-time Payment to Messrs. Ferdinand, Schaeffer and Keller	1,021,000
IPO Bonus paid to Mr. Schaeffer	250,000
IPO Bonus paid to Mr. Ferdinand	250,000
IPO Bonus paid to Mr. Keller (approx)	40,000
Accumulated Consulting Fees (approx)	6,120,650
Net Proceeds (approx)	17,400,000
Total IPO expenses	11,175,000
as a % of Gross Proceeds	39.1%
Translation: 39% of the IPO proceeds are spent on day one.	
(1) Brian Ferdinand and Douglas Von Allmen, purchased an aggregate of $16.2 million of shares in the IPO.	

By the time of its IPO, Liquid's balance sheet had expanded to $50.0 million of total assets, a sizable sum that at first blush appears substantial and possibly even worthy of an initial public offering. Upon closer inspection, though, $40 million of these assets are worthless, consisting of goodwill and other intangibles created via the acquisitions of old pieces of trading-related software paid for with contingent consideration (common stock).

They artificially inflated the balance sheet in order to make the company appear larger to potential IPO investors than it really is, and therefore more attractive.

Bogus Assets, Bogus Revenues, & Bogus Margins

I. Bogus Assets

Balance Sheet Items	**12/31/2012**	**Prospectus**	**12/31/2013**
Goodwill	13,182,936	21,198,936	13,182,936
Other Intangibles, gross	21,482,643	21,482,643	21,482,643
Net of Amortization	2,742,518	2,742,518	9,976,790
Other Intangibles, net	18,740,125	18,740,125	11,505,853
Total Intangibles	31,923,061	39,939,061	24,688,789
Total Assets	41,948,631	49,964,631	36,043,885
Intangibles as a % of Assets	*76.1%*	*79.9%*	*68.5%*

The balance sheet in Liquid's prospectus lists $21.2 million of goodwill and $18.7 million of other intangible assets. With total assets of only $50.0 million, the $40.0 million of intangibles represents 80% of asset value – a high proportion of intangible assets-to-total assets, calling into immediate question their quality.

Digging deeper into the footnotes of the prospectus, on page F-23, we find an explanation of the valuation of assets under the section header, Founders' Contributions, Business Combinations and Asset Acquisitions – F-23. Liquid Holdings was formed in 2012 to acquire a group of technology companies that together would be sold under the Liquid brand. The $40 million of intangibles was created from these acquisitions.

Goodwill is created when an acquiring company pays more than the value of the tangible assets on the balance sheet. There is nothing inherently wrong with goodwill, in fact we expect acquirers to pay a premium; however, when goodwill ends up representing a substantial proportion of the assets of a company it raises a red flag. Similarly, the high amount of "other intangibles" deserves further diligence. Included in this catch-all category is the estimated value of IP licenses, software including the trading platform, customer relationships, trade names and non-compete agreements.

Liquid Holdings is mainly the result of three acquisitions: (1) Green Mountain Analytics, LLC, (2) Liquid Partners, LLC (formerly known as Centurion Capital Group, LLC), and (3) Fundsolve Limited.

Green Mountain Analytics, LLC. (GMA) is *the foundation of our trading technology*, according to Liquid's prospectus. Mr. Ferdinand and Mr. Keller initially acquired their equity positions in GMA in 2008 and together acquired a majority, but non-controlling, interest in GMA in 2011. Liquid Holdings subsequently acquired GMA on August 27, 2012 for **NO** cash. Shares were issued in the amount of $19,973,374 for a company with stretched payables and accrued expenses of $210,543, a balance due that erases the $84,717 of cash on the balance sheet. In other words, Green Mountain was in desperate need of an infusion of cash or other transaction to continue as a going concern. Furthermore, $20,672,948 of total intangibles and goodwill was magically created, comprised of $16,332,333 for the IP (trading platform + trade name) and $4,338,615 of goodwill.

Green Mountain Analytics, LLC	
Acquisition Date: August 27, 2013	
Consideration:	
Contingent consideration payable	19,973,374
Recognized amounts of identifiable assets acquired and liabilities assumed:	
Cash	84,717
Deposit	77,000
Fixed Assets	2,625
Accounts payable and accrued expenses	-210,543
Identifiable intangible assets:	
Trade Name	**2,000**
Trading Platform	**16,332,333**
Goodwill	**4,338,615**
Deferred tax liability	-653,373
	19,973,374

Is the Green Mountain software, rechristened LiquidTrade, worth $20 million? I will show later in this report in the section titled **Valuation** that the LiquidTrade software is worth no more than $1 million to $2 million, and maybe nothing. This discrepancy will lead to the inevitable write-down that will crush non-existent earnings and right-size a tiny balance sheet.

The next largest acquisition was of a company called Centurian Capital Group, renamed Liquid Partners, LLC. Again, **NO** cash was paid, yet $10,300,000 of stock was issued. Included in the $10.3 million, was $8,580,157 of goodwill created out of the ether, along with customer relationships and a non-compete agreement that was arbitrarily valued at $1,993,000.

Liquid Partners, LLC (formerly known as Centurion Capital Group, LLC)	
Acquisition Date: May 11, 2012	
Consideration:	
Contingent consideration payable	10,300,000
Recognized amounts of identifiable assets acquired and liabilities assumed:	
Cash	482
Due from affiliates	300,000
Accrued expenses	-4,452
Due to affiliates	-407,766
Loan payable	-81,700
Identifiable intangible assets:	
Customer relationships	**1,254,000**
Non-compete agreement	**739,000**
Goodwill	**8,580,157**
Deferred tax liability	-79,721
	10,300,000

The third acquisition was Fundsolve Limited, through which, according to the prospectus, *we acquired our risk management technology*. In this case, Liquid created a total of $1,755,986 of goodwill and intangibles despite again paying with no cash whatsoever.

Fundsolve Limited	
Acquisition Date: April 23, 2012	
Consideration:	
Contingent consideration payable	1,690,000
Recognized amounts of identifiable assets acquired and liabilities assumed:	
Cash	7,698
Fixed Assets	2,188
Prepaid Expenses	13,487
Accounts payable and accrued expenses	-27,373
Identifiable intangible assets:	
IP Licenses	**12,000**
Software	**1,537,658**
Goodwill	**206,328**
Deferred tax liability	-61,986
	1,690,000

Other acquisitions listed in the prospectus include:

Tragara Alpha Partners, LLC. *We acquired certain intellectual property assets forming a component of our trading technology, including an algorithmic trading program, from Tragara Alpha Partners, LLC, or Tragara Alpha Partners, owned by Samuel Gaer, our former Chief Executive Officer and a former member of our Board of Directors, on April 27, 2012.*

LiquidView. *We acquired the LiquidView software tool, which forms a component of our accounting technology, from entities controlled by Messrs. Ferdinand and Keller on July 30, 2012.*

In summary, Liquid grossed up the value of the assets of the companies it acquired by claiming the assets were worth much more than what it said on their balance sheets. While this is typical, especially when acquiring technology companies with intellectual property (IP), it opens the door wide open for accounting/valuation abuse. Liquid says the Green Mountain Analytics (GMA) trading platform is worth $20 million, the valuation is approved by some accountant who is getting paid to say whatever his client wants him to say, and voila $20 million of value is created for the benefit of Liquid. The write-down of this $20 million is inevitable. LiquidTrade is garbage. I'm looking at it right now. I have Neovest (a competing product) open on another screen. I use Neovest for my long/short fund because (a) it's free, and (b) it's more user friendly than LiquidTrade. LiquidTrade was designed by day-traders for day-traders. Adapting it for portfolio managers is like adopting it for the cloud – they have to start all over and redesign it and reengineer it with their customers in mind. The LiquidTrade software is so old and poorly architected that it cannot be adapted for the cloud; the best they can do is set up a virtual network using Citrix that requires the download of a piece of software called a receiver. If Liquid ever launches a cloud version of its software then that version would have to be a completely different one than the polished turd that is soiling my screen.

One of Liquid's tag-lines is, *Born in the Cloud*. Given the fact that there is no cloud version, this is a ridiculous lie. When the CTO defends the Citrix installation as "cloud", remind him that Citrix still requires the download of software and therefore by definition is neither software-as-a-service nor cloud. It is local software, nothing more nothing less. I went to Mexico over the holiday season and asked him if I could access LiquidTrade from the hotel's computer, or someone else's computer, in case something unfortunate happened to mine.

He stared at me with a blank expression.

There is no cloud. I repeat there is no cloud.

II. Bogus Revenues

For the years ended December 31, 2012 and December 31, 2013, 56% and 39 %, respectively, of revenues were attributable to commissions and fees from broker-dealer operations, while 44% and 61%, respectively, came from subscription fees, primarily from QuantX, an entity with which Messrs. Ferdinand, Schaeffer and Keller are affiliated.

The over-the-counter brokerage operations were discontinued June 1, 2013, leaving software as the only source of revenue. Total software revenue in 2013 was $2,925,650, of which $2,387,825 were from QuantX, the related party. That means there was **only $537,825 of arms-length revenue generated in 2013**.

The following chart shows key operating metrics as reported by Liquid. Note that QuantX accounts for 421 of the 517 software units licensed, equal to 81.4% of unit sales. If that level of related party sales weren't troublesome enough, what makes it absurd is the fact that these numbers are made up. Assuming every QuantX trader licenses all three products: LiquidTrade, LiquidMetrics, and LiquidView, that would imply there are 140 1/3 QuantX traders (421 divided by 3). Being a QuantX trader myself, with intimate knowledge of the QuantX operation, I can attest that there are not 140 1/3 traders. At the end of the year, the number was in the vicinity of 75. The near-term goal is 100.

Annual contract value (ACV) at the end of 2013 equal to $4.52 million ostensibly represents a floor level of revenue upon which new sales can build. We use this premise as a Base Case assumption.

Key Operating Metrics	**12/31/2012**	**3/31/2013**	**6/30/2013**	**9/30/2013**	**12/31/2013**
Contracts - Contributing to Current Revenue					
Number of Customers	20	25	23	27	48
Number of Units	327	351	385	455	517
Number of Units - QuantX (1)	274	290	304	378	421
Contracts - Expected to Contribute to Future Revenue (2)					
Number of Customers N/A N/A 7 21 29	N/A	N/A	7	21	29
Number of Units N/A N/A 35 110 139	N/A	N/A	35	110	139
Number of Units - QuantX (1)	N/A	N/A	8	13	14
Contracts – Total					
Number of Customers	20	25	30	48	77
Number of Units	327	351	420	565	656
Number of Units - QuantX (1)	274	290	312	391	435
Annual Contract Value (in millions)	N/A	N/A	1.707	3.158	4.520
(1) QuantX is an affiliated entity					
(2) Contracts that have been signed but are not yet generating revenue.					

III. Bogus Margins

Reported Gross Margin for QuantX (related party) is an insane 96%. Meanwhile, gross margin on revenue generated from arms-length transactions is *negative 21%.* This may be the most brazen accounting shenanigan I have ever seen in my life. This company is not a software company. It is a proprietary trading company that forces its traders to use its software.

In theory, losses at Liquid can be financed by profits at QuantX, and I personally contribute to that potential. I made $105,154.32 of gross trading profit in my QuantX account in the first quarter of 2014. After the 1.5% asset fee and other fees, I took home $40,430.54. I then used $7,381.72 to pay four months of Liquid software fees at $1,845.43 per month. The people who own QuantX are the same people who own the majority of Liquid, and they can take the profit generated from my trading and turn around and lend it to Liquid. In fact, that is precisely what they did on February 26, 2014 when the Company executed a Revolving Promissory Note with each of its two largest stockholders, Brian Ferdinand (who is also a director and officer of the company) and Douglas J. Von Allmen. Under each Note, the company is able to borrow, and the lender has committed to lend, up to a principal amount of $3,750,000 on a revolving basis ($7,500,000 in the aggregate under the Notes), with interest payable quarterly on any amounts borrowed at a rate of 4% per annum. Any amounts borrowed under the Notes are repayable at maturity on April 30, 2015 and are optionally repayable at any time without the payment of any premium or penalty. The company agreed to pay a commitment fee on any undrawn amounts at a rate per annum equal to 0.50%, payable quarterly. The Notes contain certain customary covenants, including covenants relating to the Company's ability to incur indebtedness and make restricted payments, and provide for certain customary events of default. The company may terminate the commitment under the Notes at any time.

A $7.5 million note payable in a little more than one year at a friends and family rate of 4% is clearly mispriced given Liquid is burning approximately $5 million per quarter. With only $8.5 million of cash, survival through 2014 will depend on the deep pockets of the founders/insiders.

According to Liquid's 2013 10-K, five months after an IPO and a year of growth, total assets are down to $36,043,885. There is no misunderstanding here. The reason assets are down is because the assets are bogus. In the prospectus, pro forma goodwill was $21.2 million. Now it is down to $13.2 million and surely headed to near zero. The write-off of $8 million of goodwill a year after it was created reeks of accounting fraud.

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Financial Summary Analysis	2012A	2013A	2014E
# of Customers		77	
# of Contracted Software Units		656	
Units per Customer - implied and impossible given only 3 units are available		8.5	
This number is skewed by QuantX			
Related Party Transactions (QuantX)			
Monthly Software Subscription Fees:	Rate	# of Instances	Fees
LiquidTrade	695	1	695
LiquidView *	1,000	1	1,000
LiquidMetrics	1,950	0	0
Total Monthly Software Subscription Fees	3,645	2	1,695
* I pay a thousand dollars a month for a once a day email summarizing my basic account information: equity, P&L by posi			
# of QuantX Traders - maxes out around 100	NM	NM	94
Monthly Fees per Trader (assume QuantX pays full price on all its traders)			14,580
Fees per Period			14,580
Related Party Revenue (QuantX):	890,432	2,387,825	4,100,625
as a % of Total Software Revenue	*86%*	*82%*	*68%*
Cost of Revenue	154,900	270,561	163,148
Gross Profit	735,532	2,117,264	3,937,478
% Margin	*83%*	*89%*	*96%*
Arms Length Revenue:			
Software Revenue	142,102	537,825	1,900,000
as a % of Total Software Revenue	*14%*	*18%*	*32%*
Cost of Revenue	233,960	1,182,240	2,290,799
Gross Profit	-91,858	-644,415	-390,799
% Margin	*-65%*	*-120%*	*-21%*
Total Revenues:			
Software - 2014 is based on ACV	1,032,534	2,925,650	6,000,625
% Growth		*183%*	*105%*
Brokerage - discontinued June 1, 2013	1,295,248	1,872,647	0
Total Revenues	2,327,782	4,798,297	6,000,625
Total Cost of Revenues:			
Software	388,860	1,452,801	2,453,947
Brokerage	817,559	1,248,192	0
Total Cost of Revenues	1,206,419	2,700,993	2,453,947
Gross Profit:			
Software	643,674	1,472,849	3,546,678
% Margin	*62%*	*50%*	*59%*
Software ex. Related Party Transactions	**-91,858**	**-644,415**	**-390,799**
Brokerage	477,689	624,455	0
% Margin	*37%*	*33%*	*NM*
Total Gross Profit	1,121,363	2,097,304	3,546,678
% Margin	*48%*	*44%*	*59%*
Operating Expenses:			
Compensation	28,285,420	18,885,418	15,825,820
Consulting fees (outsourcing)	3,081,002	12,727,112	2,178,780
Depreciation and amortization (tied to capex)	2,761,703	7,407,062	7,755,599
Professional fees (legal, accounting, tax)	1,651,232	3,676,863	5,659,364
Rent	629,400	1,211,693	1,139,928
Computer related and software development	414,048	2,472,539	3,332,816
Other	790,747	2,436,736	3,259,660
Impairment of goodwill and intangible assets	1,550,652	0	0
Total Operating Expenses	39,164,204	48,817,423	39,151,967
Loss from Operations	-38,042,841	-46,720,119	-35,605,289
Non-operating Income (Expense):			
Registration rights penalty (Doug Von Allmen)	-1,674,704	0	0
Unrealized gain on contingent consideration payable	129,000	0	0
Gain (loss) on settlement of contingent consideration payable	1,545,000	-649,688	0
Interest and other, net	-306,659	60,500	-303,592
Total non-operating income (expense)	-307,363	-589,188	-303,592
Loss before income taxes	-38,350,204	-47,309,307	-35,908,881
Income tax benefit	-104,340	-697,260	-1,822,957
% tax rate	*0%*	*1%*	*5%*
Net loss	-38,245,864	-46,612,047	-34,085,924
NOPAT (no taxes)	-38,042,841	-46,720,119	-35,605,289
+ D&A	2,761,703	7,407,062	7,755,599
+ Stock Comp	29,379,820	21,075,377	7,982,388
as a % of revenue	1262%	439%	133%
+/- Change in WC:			
Accounts receivable	497,848	42,311	0
Prepaid expenses and other current assets	-1,137,946	900,373	0
Accounts payable and accrued expensers	2,816,055	303,721	0
- Capex	-89,399	-738,633	-400,000
= Free Cash Flow	-3,814,760	-17,729,908	-20,267,302

Final Thoughts

Ultimately, an analysis of any technology company is an analysis of technology. After five months of use, and fifteen years of experience I can honestly say LiquidTrade is the worst piece of shit I've ever traded on. It is cumbersome to trade and limited in its flexibility. There are so many steps to take, and fields to fill that I wonder if Rube Goldberg had a hand in its design. Over ten years ago, I managed the building of trading technology that was more advanced than LiquidTrade. LiquidTrade was bought from day traders, and built for them, not built for the cloud, nor born in the cloud.

The Liquid story is a replay of *The Emperor's New Clothes*[4]. The most magnificent fabrics imaginable are *a Quantum Leap in Trading Technology*. The technology in fact is so advanced that its utility is invisible to anyone unfit for Wall Street (or unusually stupid). Since no one wants to lose their cushy jobs, everyone assures the Emperor that the silk is fine and thread pure.

"I'd like to know how those weavers are getting on with the cloth," the Emperor thought, but he felt slightly uncomfortable when he remembered that those who were unfit for their position would not be able to see the fabric. It couldn't have been that he doubted himself, yet he thought he'd rather send someone else to see how things were going. The whole town knew about the cloth's peculiar power, and all were impatient to find out how stupid their neighbors were. I'll send my honest old minister to the weavers," the Emperor decided. "He'll be the best one to tell me how the material looks for he's a sensible man and no one does his duty better."

My friend and neighbor is a sensible man who knows nothing about technology. He makes $350,000 per year base salary and would like to maintain this level of income.

"Heaven help me," he thought as his eyes flew wide open, "I can't see anything at all". But he did not say so.

Before the procession (the IPO), the swindlers sat up all night and burned more than six candles, to show how busy they were finishing the Emperor's new clothes. They pretended to take the cloth off the loom. They made cuts in the air with huge scissors. And at last they said, "Now the Emperor's new clothes are ready for him." Then the Emperor himself came with his noblest

[4] By Hans Christian Andersen.

noblemen, and the swindlers each raised an arm as if they were holding something. They said, "These are the trousers, here's the coat, and this is the mantle," naming each garment. "All of them are as light as a spider web. One would almost think he had nothing on, but that's what makes them so fine."

"Exactly," all the noblemen agreed, though they could see nothing, for there was nothing to see.

"If Your Imperial Majesty will condescend to take your clothes off," said the swindlers, "we will help you on with your new ones here in front of the long mirror."

The Emperor undressed, and the swindlers pretended to put his new clothes on him, one garment after another. They took him around the waist and seemed to be fastening something - that was his train - as the Emperor turned round and round before the looking glass.

"How well Your Majesty's new clothes look. Aren't they becoming!" He heard on all sides, "That pattern, so perfect! Those colors, so suitable! It is a magnificent outfit."

Then the minister of public processions announced: "Your Majesty's canopy is waiting outside."

The noblemen who were to carry his train stooped low and reached for the floor as if they were picking up his mantle. Then they pretended to lift and hold it high. They didn't dare admit they had nothing to hold.

So off went the Emperor in procession under his splendid canopy. Everyone in the streets and the windows said, "Oh, how fine are the Emperor's new clothes! Don't they fit him to perfection? And see his long train!" Nobody would confess that he couldn't see anything, for that would prove him either unfit for his position, or a fool. No costume the Emperor had worn before was ever such a complete success.

"But he hasn't got anything on," a little child said.

"Did you ever hear such innocent prattle?" said its father. And one person whispered to another what the child had said, "He hasn't anything on. A child says he hasn't anything on."

"But he hasn't got anything on!" the whole town cried out at last.

The Emperor shivered, for he suspected they were right. But he thought, "This procession has got to go on." So he walked more proudly than ever, as his noblemen held high the train that wasn't there at all.

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