EARLY STAGE VENTURE INVESTMENT STRUCTURES

PROVIDED BY JACKSON WALKER LLP

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The following chart outlines the different approaches an entrepreneur and investor can take to structure the first capital infusions into a startup.

	Equity or Debt	Conversion to Stock	Holder's Rights	Pros	Cons
SAFE	Equity	• Automatically upon the next equity round with no minimum threshold, after a liquidity event, or dissolution of the company for an agreed upon multiple (such as 1X of the amount invested).	• Standard form provides for no additional investor rights until conversion, unless a major investor, which is afforded most favored nations rights.	• Simplistic, efficient, and easy to transact. • Permits company to raise capital without incurring debt. • Removes maturity and interest features from a	• Lacks certain forms of investor protections, including lack of conversion if no future financing round occurs.

	Equity or Debt	Conversion to Stock	Holder's Rights	Pros	Cons
		• Conversion is typically at a discount to the price paid by investors in next round (often in a range from 10% to 30% of the price paid in the equity round) and typically the valuation at which the debt is converted is capped at a certain pre-money valuation.		traditional note.	
KISS Debt	Debt	• Automatically upon a qualified dollar amount threshold (such as $1 million being raised in the form of equity), or a liquidity event for a return of an agreed upon multiple (such as 2X of the amount invested).	• Information rights, rights to participate in future financings of the company, and most favored nations rights.	• Additional investor rights are included. • Provides certain options for non-payment at maturity (creation of new class of stock).	• Does not remove all of the complexities/ negotiations. • Phantom gains on interest which is converted into equity. • Maturity date results in risk to the entrepreneur if further funding has not been received.
KISS Equity	Equity	• Automatically upon a qualified dollar-amount threshold (such as $1 million being raised in the form of equity), or a liquidity event for a return of an agreed upon multiple (such as 2X of the amount invested).	• Information rights, rights to participate in future financings of the company, and most favored nations rights.	• Additional investor rights. Provides certain options for non-payment at maturity (creation of new class of stock). • Removes maturity and interest features from KISS Debt.	• Does not remove all of the complexities/ negotiations.

	Equity or Debt	Conversion to Stock	Holder's Rights	Pros	Cons
Convertible Note	Debt/ Equity	• Typically, converts with a qualified dollar-amount threshold (such as $1 million being raised in the form of equity). • Conversion is typically at a discount to the price paid by investors in next round (often in a range from 10% to 30% of the price paid in the equity round) and typically the valuation at which the debt is converted is capped at a certain pre-money valuation.	• Prior to conversion, the holder may have the right to participate in future rounds and other negotiated for protections. • Once converted to equity, the same as the equity holders of such financing round. • Since this is debt, the noteholder is paid prior to equity holders on liquidation.	• Defers company valuations. • Has been utilized for a number of years, so serial early stage investors are familiar with document terms.	• Cap price negotiations and discount negotiations can be challenging and increase costs. • Phantom gains on interest which is converted into equity. • Maturity date results in risk to the entrepreneur if further funding has not been received.

	Equity or Debt	Conversion to Stock	Holder's Rights	Pros	Cons
Seed Round	Equity	• Convertible to common stock upon certain events or the decision of the investor.	• Preferred returns, board seat, voting rights, and conversion rights.	• Post-money dilution is agreed upon.	• Costly, often longer negotiations than a traditional note round.
Preferred Round	Equity	• Convertible to common stock upon certain events or the decision of the investor.	• Preferred returns, board seat, voting rights, anti-dilution protection, and conversion rights.	• Post-money dilution is agreed upon.	• Costly, many terms involve heavy negotiations. • Requires a portfolio of documents.[1]

[1] *See, e.g.* model documents made available at nvca.org.