



# Demystifying Term Sheets

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# Demystifying Term Sheets

- Convertible Preferred Stock
  - Why convertible?
  - Why preferred?
  
- Pre-Money Valuation
  - Treatment of option pool
  - Relationship to funds raised and ownership percentages
  - Impact on future rounds of financing

## Demystifying Term Sheets

- Fully Diluted Equity (as converted/common equivalent)
  - What's included?
  
- Standard Transaction Documents
  - Certificate of Incorporation
    - Rights and preferences of equity
  
  - Stock Purchase Agreement
    - Blueprint for transaction
    - Reps & warranties
    - Closing conditions

# Demystifying Term Sheets

## – Investor Rights Agreement

- Special contractual rights of investors (versus rights inherent in equity)
- Registration rights
- Information rights
- Pre-emptive rights for future equity financings
- Other covenants of Company

## – Right of First Refusal/Co-Sale Agreement

- Company/investor right of first refusal on proposed dispositions
- Investor right of co-sale on proposed dispositions

## – Voting Agreement

- Board composition and Board designation rights
- Drag along rights

# Demystifying Term Sheets

- Contemplated Exits
  - Sale of the Company: deemed liquidation
  - Public Offering: conversion
  - Redemption

# Demystifying Term Sheets

- Liquidation
  - Preference amount (1x, 2x, etc)
  - Participation
    - None
    - Capped
    - Full
  
- Conversion
  - Optional
  - Automatic
    - “Qualified IPO”: price & amount raised
    - Supermajority vote of series

# Demystifying Term Sheets

- Redemption
  - When?
  - Realistic?
  
- Anti-Dilution Adjustments
  - Weighted average
  - Full ratchet
  
- Other issues
  - Vesting of founder stock
  - Protective provisions/special voting rights
  - Dividends
  - Pay to play

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## ■ Resources

- NVCA Model Venture Capital Financing Documents: [www.nvca.org](http://www.nvca.org)
- Foley Hoag Emerging Enterprise Center Website:  
[www.emergingenterprise.com](http://www.emergingenterprise.com)
  - Ask The StartUp Lawyers
  - Glossary



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