Venture Capital Transactions

Evolution of Venture Capital Deals

- Venture capital deals have evolved significantly since the 'heyday' of the late 1990s
- Term sheets were once very favorable to the entrepreneur as a number of VCs competed for Series A deals
- Post the 'internet bubble', the pendulum swung in favor of the VCs and have pretty much stayed that way to-date

Negotiating and Structuring the Deal

- Revolves around the type of equity and terms of the security
- Typical equities of a VC deal:
  - Preferred stock: the equity of choice for VCs
  - Convertible debt:
    - Fixed returns and tax advantages
    - Used for higher risk investments
    - Bridge financing to equity raise (then converted)
    - May be subordinated to allow institutional debt

Additional Equity Types

- Debt security with warrants:
  - Debt protects downside with fixed return
  - Warrants protect upside by allowing stock purchases at discount
  - Allows stock purchase without sacrificing preferred position as a creditor
- Common Stock
  - Rarely used by VCs
  - No special rights or preferences, no fixed returns, no control, no liquidity to protect downside

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After Security Is Agreed

- Authorization and issuance in accordance with state laws
- May require charter amendments, requiring board and shareholder approval
- Negotiate rights, preferences, privileges:
  - Voting rights, dividend rate
  - Redemption, conversion, liquidation preferences
  - Anti-dilution, pro rata rights

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Summary – Venture Capital Deals

- Have evolved significantly since the late 1990s
- Term sheets more in favor of VCs due to tighter capital markets and more deals looking for VC money
- Various equity forms may be used, but preferred stock is most common
- Equity structure may require charter amendments

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