

Glossary

- accelerator** A program intended to mentor founders and accelerate the growth and success of a startup company.
- accredited investor** As defined by federal securities laws, a person who is permitted to invest in startups and other high-risk private company securities based on the net worth and income level of the potential investor.
- acquisition** A transaction between two companies where one is buying the other.
- adverse change redemption** A type of redemption right whereby a shareholder gets the right to redeem his shares if something adverse happens to the company.
- advisers** People who advise startup companies. Normally, these people are paid some sort of compensation for their efforts.
- affirmative covenants** Action that the company promises to take during the term of the financing contract in a financing.
- agency costs** The costs associated in an agency/principal relationship that the principal incurs either directly or indirectly.
- alpha** The earliest of early prototypes of a product. This is before the beta, which is still a prototype, but with a lot more polish.
- amortization terms** Terms that debt lenders use to better align the debt with the capital strategy of the company.
- analyst** A very junior person at a venture capital firm, often a recent college graduate.

- angel investor** An individual who provides capital to a startup company. This person is usually independently wealthy and invests her own money in the company.
- antidilution** A term that provides price protection for investors. This is accomplished by effectively repricing an investor's shares to a lower price per share in the event that the company completes a financing at a lower valuation than a previous financing round.
- as-converted basis** Looking at the equity base of the company assuming that all preferred stock has been converted to common.
- assignment** The right of a preferred shareholder to transfer its shares to an affiliated entity without company consent.
- associate** A person at a venture capital firm who is involved in deal analysis and management. The seniority of this position varies by firm, but generally associates need a partner to support their activities.
- at-will employee** An employee who does not have an employment agreement and can be terminated by the company for any reason.
- barter element** The price at which a stock option may be exercised.
- basis of stock option** The price at which a stock option may be exercised.
- best alternative to negotiated agreement (BATNA)** A backup plan if no agreement is reached between two parties.
- beta** A prototype of a product, but more advanced than the alpha. It's not unusual for betas to be released to customers for feedback.
- blended preferences** When all classes of preferred stock have equivalent payment rights in a liquidation.
- board of directors** A group of people elected by a company's shareholders to represent all the stakeholders of a company. The board is responsible for company oversight including hiring and firing the CEO.
- bridge loan** A loan given to a company by investors with the intent that the money will fund the company to the next equity financing.
- broad-based antidilution** The denominator in weighted average antidilution calculations that takes into consideration a fully diluted view of the company. The opposite is called a narrow-based antidilution.
- burn rate** The amount of money that a company is consuming, usually measured over months, quarters, or a year. This is the net amount of cash that is leaving the bank account over the given time period.

- cap** The valuation ceiling that exists in a convertible debt deal.
- capital call** The method by which a VC fund asks its investors to contribute their pro rata portion of money being called by a VC fund to make investments, pay expenses, or pay management fees.
- capitalization table (cap table)** A spreadsheet that defines the economics of a deal. It contains a detailed description of all the owners of stock of a company.
- carry/carried interest** The profits that VCs are entitled to after returning capital committed to their investors. This typically ranges from 20% to 30%.
- carve-out (equity)** The concept whereby shareholders agree to give a preferential payment (usually to executives and employees of a company) ahead of the shareholders agreeing to the carve-out. Normally, one would see a carve-out used in the situation where liquidation preferences are such that employees of the company do not have enough financial interests in a liquidation event.
- carve-out (merger)** Within the merger context, these are certain representations and warranties that will be indemnified outside of the escrow.
- clawback** The provision in the limited partnership agreement that allows investors to take back money from the VC should they overpay themselves with carry.
- commitment period** The length of time a venture capital fund has to find and invest in new companies, usually five years.
- common stock** The type of stock that has the least amount of rights, privileges, and preferences. Normally employees and founders of a company hold common stock, as the price they pay for the stock can be much less than that of preferred stock.
- conditions precedent to financing** A list of items in the term sheet that must be satisfied before an investor will agree to consummate the financing. This can include anything but typically revolves around further due diligence into the company.
- control terms** Terms that allow a VC to exert positive or veto control in a deal.
- conversion** A process in which preferred stock is converted to common stock.

conversion price adjustment The mechanism by which an antidilution adjustment takes place. This allows the preferred stock to be converted into more common stock than originally agreed upon and thus allows the preferred to own more stock and voting rights upon converting to common.

convertible debt A debt or loan instrument that an investor gives to a company with the intent that it will convert later to equity and not be paid back as a standard bank loan would be.

corporate venture capital A venture firm that is sponsored and backed by a corporation, often but not always part of a publicly traded company.

co-sale The right of a shareholder (typically a VC) to sell shares alongside another shareholder that is selling some or all of its equity to a buyer.

cross-fund investment When a venture capital firm operates more than one fund and more than one fund invests in the same company.

crowdfunding When a group of individuals fund a company either through equity purchase, debt purchase, pre-sale ordering of a product, or gifting of money.

director A junior deal partner at a venture capital firm.

discount A standard mechanism in a convertible note agreement that allows noteholders the right to convert the amount of the loan, plus interest, at a reduced price (in percentage terms) to the purchase price paid by equity investors who later consummate a financing.

dividends An amount of money or shares of stock that is paid out to investors based on their holdings of stock in a company.

double-trigger acceleration A term that describes the situation in which a person would receive accelerated vesting. In a double-trigger situation, two events would trigger accelerated vesting, such as a merger of the company followed by a termination of a person's employment.

down round A financing round that is at a lower valuation than the previous round.

drag-along A term that sets up a proxy on one's stock ownership to vote the same way as others do on a particular issue.

draw period The time during which cash advances may be requested under a loan (also called the availability period).

due diligence The process by which investors explore a company that they are thinking of investing in.

- early stage funds** VC funds that invest in Seed and Series A financings.
- earn-out** An amount agreed upon by an acquirer and a target company that the former shareholders of the target company will get if certain performance milestones are met post-merger.
- economic terms** Terms that impact the returns of a VC's investment in a company.
- elevator pitch** A short synopsis of what your company does and why it's compelling.
- employee option pool** The shares set aside by a company to provide stock options to employees.
- enterprise value** The post-money valuation plus debt minus cash.
- entrepreneur** Someone who creates a new company, also known as a founder.
- entrepreneur in residence (EIR)** A person at a venture firm that is usually a former entrepreneur who is helping out the venture firm by finding deals to invest in, or working on his next company that the venture firm will one day fund.
- equity** Ownership in a company.
- equity crowdfunding** A financing process made legal by the JOBS Act in 2012 and popularized by AngelList.
- escrow** The amount of consideration that an acquiring company holds back following a merger to make sure that representations and warranties made by the purchased company are true.
- escrow cap** The amount of money in a merger that is set aside to remedy breaches of the merger agreement.
- executive managing director** A senior partner in a venture capital firm who is superior to a managing director or general partner.
- executive summary** A short summary document, normally one to three pages, that describes material facts and strategies of a company.
- exercise** The act of purchasing stock pursuant to a stock option or warrant.
- exercise period** The amount of time an employee can exercise her stock after she leaves a company.
- exercise price** The price at which a stock option can be exercised (and subsequently the price per share the employee pays for the stock option).

- fair market value** The price that a third party would pay for something in the open market.
- fiduciary duties** A legal and ethical duty that an individual has to an entity.
- final payments** A loan fee that is paid at the end of the loan.
- first right of refusal** A right that allows an investor to have the first ability to either make another investment in the company or acquire the company.
- flat round** A financing round done at the same post-money valuation as that of the previous round.
- founder** Someone who creates a new company, also known as an entrepreneur.
- founders' activities** A provision in the term sheet that mandates that founders spend all of their business time working for the company.
- founders' stock** Common stock issued to founders at a very low price at the formation of the company.
- founding general partner** A senior partner in a venture capital firm who founded the firm.
- full-stack venture capital firms** A venture capital firm that employs many people beyond deal professionals, such as marketing, operations, public relations, engineering, and financial executives, to attempt to help companies more than traditional venture capital firms.
- fully diluted** A term explicitly defining that all rights to purchase equity should be in the valuation calculation.
- fundamental rep** A representation made by the seller in an acquisition that survives longer than the escrow period.
- game theory** The concept that one's actions depend on what actions other persons may or may not take and the inherent incentives behind these actions.
- general partner (GP)** A senior partner in a venture capital firm.
- general partnership (GP)** The entity that manages the limited partnership.
- general solicitation** Fundraising to potential investors without a "substantial preexisting relationship." Some also consider this to be when a startup advertises for funding.

GP commitment The amount of money, usually between 1% and 5% of the fund, that the general partners invest in their own fund.

growth investors VC funds that invest in Series B and later financings.

holdback The amount of consideration that an acquiring company holds back following a merger to make sure that representations and warranties made by the purchased company are true.

indemnification The promise by one party to protect another party should something go wrong.

information rights The minimum amount of information the company must give its investors on a regular basis.

initial coin offering A fundraising mechanism where a company sells crypto tokens instead of equity.

initial public offering shares purchase A term sheet provision that allows the preferred stockholders to buy shares of the company in an initial public offering.

interest-only (I/O) period A length of time where only interest (and no principal) is paid on a term loan.

interest rate One of the key pricing mechanisms in a loan.

investment term The length of time that a venture capital fund can remain active, typically 10 years with two 1-year extensions.

IRS Internet Revenue Service (in the United States).

JOBS Act Formally known as the Jumpstart Our Business Startups Act, enacted in 2012. It created rules around crowdfunding, changed some dynamics around IPOs, and gave Congress a way to say they were helping startups.

key person clause Contractual provision within the limited partnership agreement that describes what will happen if certain partners leave the venture capital fund.

KISS An acronym for Keep It Simple Security, which can be an alternative for either a debt or equity financing. See <http://500.co/kiss/>.

late stage funds Entities, including VC funds and hedge funds, who invest in the last financing before an IPO.

lead investor The investor in a startup company who takes on the leadership position in a VC financing.

Lean Startup methodology A business methodology that posits businesses can reduce product development cycles by combining iterative releases and experimentations of their product. Popularized by Eric Ries.

letter of intent (LOI) A term sheet for a merger or acquisition.

light preferred A version of a preferred stock financing that has very simple and watered-down terms.

limited partners (LPs) The investors in a VC fund.

limited partnership (LP) The entity used by the limited partners to invest in a venture capital fund.

limited partnership agreement (LPA) The contract between a venture capital fund and its investors.

liquidation event/liquidity event When a company is sold and ceases to exist as a stand-alone company.

liquidation preference A right given to a class of preferred stock allowing that stock to receive proceeds in a liquidation in advance of other classes of stock.

liquidation preference overhang The cumulative amount of liquidation preferences that a company has agreed to during their existence. The amount of money owed to investors before common stock will receive proceeds.

loan fees A part of a loan agreement that charges a fixed fee for getting the deal done.

major investor A concept used in venture capital financings that allows a company to distinguish between shareholders who purchase more stock than others.

management carve-out An agreement between a company and its preferred shareholders to divert part of the proceeds that would normally flow (pursuant to liquidation preferences) to the preferred shareholders to management and employees upon an acquisition.

management company The entity that services each fund that a VC raises.

management fee The fee that the venture capital funds have a right to receive from their LPs as money to manage their business operations regardless of the performance of the fund.

managing director (MD) A senior partner in a venture capital firm.

- materiality qualifiers** Inserting the word “material” in front of things, such as protective provisions. Lawyers love to argue about this word.
- mentors** People who advise startup companies or their executives. Normally, these people are not paid.
- micro VC fund** A super angel who raises a small fund made up of professional investors.
- mid stage funds** Another name for growth investors who are VC funds that invest in Series B and later financings.
- minimum viable product (MVP)** The product with the least number of features necessarily to make it useful to ship and learn more about the users. This concept was made popular by Eric Ries as part of the lean startup methodology.
- most favored nation (MFN)** The right to get the equivalent terms to anyone who gets better terms than you in the future.
- multiplay game** A term in game theory that deals with a game or situation where there is a continuing relationship after the game is played, like a venture capital financing whereby after the transaction is completed the VC and the entrepreneur will join forces to work together.
- negative covenants** Behaviors and actions that the company may not engage in without the lender’s consent as a condition of the loan in a debt deal.
- nondisclosure agreement (NDA)** An agreement whereby one party promises not to share information of another party.
- nonparticipating preferred** A simple preferred stock that does not have a participation feature.
- no-shop agreement** One of the few binding terms in a term sheet, this provision prohibits a company from seeking other investors (unless approved by the term sheet-issuing VC) once a term sheet has been signed.
- operating partner** A position at a venture capital firm that is normally under managing director, but above principal.
- option budget** The amount of options a company plans to allocate to employees over a finite time period.
- option pool** The shares set aside by a company to provide stock options to employees.

outside director A member of a company's board of directors who is not an executive or major investor of the company.

pari passu When all classes of preferred stock have equivalent payment rights in a liquidation.

partners An investment professional at a venture firm that may or may not be an actual "partner" but has some level of deal-evaluation and deal-making authority.

party round A financing round with many participants, usually at small dollar amounts.

pay-to-play A term that forces VCs to continue to invest in future company financings or suffer adverse consequences to their ownership positions.

perfected lien A document that has been filed with the appropriate agency allowing for a legal claim to seize assets if a loan borrower defaults on the loan.

performance warrant A warrant that is exercisable if certain performance metrics are met by the holder of the warrant.

post-money The value of a company after an investor has put money into the company.

PowerPoint Throughout this book, we use PowerPoint to describe presentation software that was originally made famous by Microsoft. Many of the presentations we now see are in Google Docs or Apple Keynote, both competitive products to Microsoft PowerPoint. Oh, and we actually prefer PDF files.

preferred stock A type of stock that has preferential terms, rights, and privileges compared to common stock.

pre-money The value ascribed to a company by an investor before investing in the company.

prepayments The arrangement whereby a borrower can or cannot prepay a loan down before the maturity date. In venture debt, prepayments are generally allowed but may have some additional costs depending on when the prepayment is made.

pre-seed round The round before a seed round. This term is now used to refer to the very first financing round in a company.

price per share The dollar amount assigned to purchase one share of stock.

prime rate A specific reference index that a floating, or variable rate loan, is based on. Most venture loans are indexed to the prime rate, either the prime rate of the bank providing the loan or the published benchmark, such as the prime rate published by the *Wall Street Journal*.

principal A junior deal partner at a venture capital firm.

private placement memorandum (PPM) A legal document that is prepared by the company, its bankers, and its lawyers that is a long-form business plan created to solicit investors.

product crowdfunding An approach to funding product development by using customers to preorder products that was popularized by Kickstarter.

proprietary information and inventions agreement (also called proprietary rights agreement) This is a contract that should be signed by anyone who works for a company that specifically states that all intellectual property developed by the person is the property of the company. It also will have the person guarantee that they are not using anyone else's intellectual property while working at the company.

pro rata The right of a shareholder to purchase shares in a future financing equal to the percentage the shareholder currently holds at the time of such financing.

protective provisions Contractual rights that allow the holders of preferred stock to vote on certain important matters pertaining to a company.

ratchet-based antidilution A style of antidilution that reprices an investor's shares in previous rounds, usually through a conversion price adjustment, to the price paid in the current round.

redemption rights The ability of a shareholder to force the company to purchase his or her shares at a previously agreed-upon price.

registration rights The contractual rights allotted to investors pursuant to a financing that detail the ability of shareholders to force the company to register their shares on a public stock market.

representations and warranties Provisions in a financing purchase agreement or merger agreement whereby the company makes certain assurances about itself.

reputation constraints The impact that reputation has on one's behavior.

reserves The amount of money that a venture capital firm allocates for future investments in a particular portfolio company.

restricted stock units (RSUs) A substitution for traditional stock options that provides different tax accounting for the company that issues them.

restrictions on sales A right but not an obligation to purchase shares of another shareholder who wishes to sell.

reverse dilution The situation in which stock is returned to a company by departed employees whose stock has not vested, thus increasing the effective ownership of all shareholders in a company.

right of first refusal (ROFR) A right but not an obligation for an investor to participate in future rounds of financing.

right of rescission The right of shareholders to force the company to buy back their stock, usually given to people who were not supposed to buy the stock in the first place under federal securities law.

runway The number of months of cash remaining, based on the projected monthly cash burn.

safe Acronym for “simple agreement for future equity,” which is an alternative to the issuance of convertible debt. See www.ycombinator.com/documents/#safe.

safe harbor A legally defined way of escaping liability under a law if a party performs certain acts as defined by such law.

schedule of exceptions A list of exceptions to representations and warranties in a venture financing or acquisition agreement.

schmuck insurance Preferences, including ones that guarantee a return for an investor, especially in a situation where an investor has concerns about overpaying at a particular point in time.

secondary sale The sale by a VC of stock in a portfolio company or its entire portfolio to an outside party in a private transaction.

security A financial instrument that represents an ownership right in a company.

seed preferred Same as a light preferred: A simple watered-down version of a preferred stock financing.

seed rounds What Series Seed financings used to be called in the old days of venture capital.

seed stage A startup that is in its infancy.

seed stage funds VC funds typically focused on being the first institutional money in a company.

Series A financing The first or early round of financing that a company raises.

Series Seed financing A small financing that occurs before the Series A financing and is often the very first financing of a company.

simple preferred A very lightweight preferred stock, usually with only a liquidation preference and minimal rights.

single-play game A term in game theory that deals with a game or situation in which there is no continuing relationship after the game is played.

single-trigger acceleration A term used to describe the situation in which a person would receive accelerated vesting.

stacked preference When different classes of preferred stock have senior rights to payment over other classes of preferred stock.

stock option A right to purchase shares of stock in a company.

straight line amortization The principal balance of a loan is divided up equally among the number of payments.

strike price The price at which a stock option may be exercised.

structure Multiple liquidation preference or participation in a preferred stock. This is often found in late stage deals.

super angel A very active and experienced angel investor.

super pro rata rights The right of shareholders to purchase shares in a future financing equal to some multiple of the percentage they currently hold at the time of such financing.

syndicate The group of investors who invest in a startup.

term sheet A summary document of key terms in contemplation of a financing.

transactions costs The direct and indirect costs (time and money) associated with the creation of a business relationship.

unicorn A mythical beast that rides on a silver moonbeam and shoots rainbows out of its ass. Also, a private company that has achieved a \$1 billion valuation.

valuation The value ascribed to a company by an investor.

valuation cap A term in a convertible note deal that sets the maximum conversion price of the debt into equity.

venture capital fund (VC fund) The entities that make up the investment family of a VC.

venture capitalist (VC) A person who invests in startup companies.

venture debt Debt for an equity-backed company that doesn't have the cash flows to support traditional debt.

venture debt fund A provider of venture debt that is not a bank.

venture partner A position at a venture capital firm that is normally under managing director, but above principal.

vesting The notion that a stock award is not earned until some period of time or milestone is reached.

vesting cliff The length of time required for an employee to be at a company before any of her stock or options vest. This is typically a year.

voting rights The specific rights of how preferred stock and common stock vote.

walking dead portfolio company A company that has no growth, no exit opportunities, no financing options, but just enough revenue, cash, or cash flow to stay in business.

warrant A right to purchase shares of stock in a company.

weighted average antidilution A style of antidilution that reprices an investor's investment, usually through a conversion price adjustment, to a lower price per share, but considers the relative effect of the number of shares sold in the current round.

zone of insolvency When a company is nearly insolvent and doesn't have the assets to pay off its liabilities.