Funding with SAFEs

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What is a SAFE?

A SAFE (Simple Agreement for Future Equity) is a financial instrument used by startups to raise capital. It allows investors to provide funds in exchange for the right to receive equity later, typically during a future financing round. SAFEs convert into shares at a predetermined valuation cap or discount. They are simpler than traditional equity financing, as they do not require immediate valuation or extensive legal documentation.

Why would a startup want to use a SAFE instead of a priced equity round?

A startup may prefer a SAFE (Simple Agreement for Future Equity) over a priced equity round because SAFEs are simpler and faster to execute, reducing legal costs. They allow startups to delay valuation discussions until a later funding round, which can be advantageous. SAFEs convert to equity automatically during future financing events, making them attractive to investors who want a straightforward investment structure.

Why would an investor want to use a SAFE rather than a priced equity round?

Investors may prefer a SAFE (Simple Agreement for Future Equity) because it offers simplicity and speed, avoiding lengthy negotiations typical in priced equity rounds. SAFEs allow for quick funding without determining a company’s valuation upfront. They also reduce legal costs and paperwork. Additionally, SAFEs convert into equity during future financing rounds, often at a discount or with a valuation cap, providing potential upside. This flexibility can be attractive in early-stage investment

How are SAFEs different from convertible notes?

SAFEs (Simple Agreements for Future Equity) differ from convertible notes in key ways. SAFEs do not accrue interest and lack a maturity date, meaning they don’t require repayment. In contrast, convertible notes are debt instruments that accrue interest and must be repaid if not converted by a certain date. SAFEs convert into equity during future financing rounds, while convertible notes have specific terms for conversion.

Why the name "SAFE"? Does it have anything to do with convertible notes being dangerous?

The name "SAFE" stands for "Simple Agreement for Future Equity." It was designed to be a straightforward funding instrument for startups. Unlike convertible notes, SAFEs do not accrue interest or have a maturity date, which reduces complexity and risk for both investors and founders. While convertible notes can be seen as "dangerous" due to their debt nature, SAFEs aim to provide a safer, more flexible alternative for early-stage funding.

Who invented SAFEs and when?

SAFEs, or Simple Agreements for Future Equity, were invented by Y Combinator in 2013. They were created to simplify early-stage fundraising for startups.

At what stage of a startup's life are SAFEs used?

SAFEs (Simple Agreements for Future Equity) are typically used in the early stages of a startup's life, particularly during seed funding rounds. They allow startups to raise capital quickly without setting a valuation. SAFEs are popular among early-stage investors and founders because they convert into equity

at a later financing round, usually when the startup raises more significant funding. This mechanism helps startups secure funds while delaying complex valuation discussions.

What are the events in which a SAFE converts to equity?

A SAFE (Simple Agreement for Future Equity) converts to equity during these events:

1. **Equity Financing**: When the company raises a new funding round, the SAFE converts into shares at a valuation cap or discount.

2. **Liquidity Event**: If the company is sold or goes public, the SAFE converts into shares or cash based on the terms.

3. **Dissolution**: If the company dissolves, SAFE holders may receive a payout before common shareholders, depending on the agreement.