MAPACHE
CAPITAL

High Level Explanation of Commonly Used Syndicate Investment Terms

Like everything these days there are many confusing terms and abbreviations in the world of investing. If you are already an experienced investor most of this stuff will not be interesting for you. If you are new to it however, this brief document – whislst being far from exhaustive - will hopefully clear *some* of the fog and assist in your understanding and decision making.

General Partner (GP)
The GP is the person leading the syndicate. Mapache Capital/Robert Mustarde is the GP for each syndicate that is created by Mapache Capital. The GP is responsible for identifying and securing investment opportunities, presenting them to the accredited investor network and filling the available investment allocation. They will also hold the direct relationship with the invested entity (the start-up) and provide feedback to the LPs as the business develops.

Limited Partner (LP)
An LP is an accredited investor who makes an investment in a specific opportunity offered by the GP. If you are planning on making investments with Mapache Capital then *you* are an accredited Angel investor (or plan to be) and you will become an LP if you invest in any opportunity that Mapache Capital presents to you.

Special Purpose Vehicle (SPV)
For each unique investment opportunity that Mapache Capital offers to its accredited investor network, a legal entity needs to be created for those investments. It is this legal entity which then invests in the opportunity. The legal entity is called a Special Purpose Vehicle (SPV). If an accredited investor invests in an opportunity they then become a Limited Partner (LP) in the SPV specific to that opportunity. The GP for each Mapache Capital SPV is Robert Mustarde/Mapache Capital.

Syndicate
This is a generic term. Essentially for each SPV which is created (i.e. for each new unique investment opportunity presented by the GP), the group of investors who actually become the LPs for that SPV are the syndicate. So Mapache Capital itself is *not* a syndicate. Mapache Capital will act as the GP of multiple syndicates, each of which is made up of a different group of accredited investors inside its own legal SPV entity.

Convertible Note

When a start-up first seeks investment – often with no paying customers, zero revenue and little traction - it is very difficult, if not impossible, to put a realistic or meaningful value on the company. The start-up founder(s) wants a higher valuation to limit the amount of equity they have to give up – and the investors are typically looking for a lower valuation to maximize the equity they can get for their investment. The traditional way of solving this conundrum is the convertible note. Essentially a convertible note is a loan to the company (or a debt taken out by the company) with an interest rate and a maturity date. There is however also an understanding that at some point down the road, the company and the investor will be in a position to put a meaningful valuation on the company – a fixed per share $ value - on which they can both agree. At that moment (typically done during a subsequent funding round) the value of the convertible note, taking into account any accrued interest, is converted into actual equity in the company.

Simple Agreement for Future Equity (SAFE)

The SAFE is based on a similar principle to the convertible note but it is not a loan/debt. It also works on the premise that a realistic valuation for a business at the time of the investment often cannot be made. The SAFE basically says that you are making an investment for equity and the quantity and value per share of the equity will be agreed at a future funding round when all parties can agree on the value. At that point the SAFE will be converted to actual equity.

The SAFE was developed by Y-Combinator as an open-source generic investment document that all parties can be familiar with, understand and trust. Aside from filling in the blanks - SAFE agreements are expected to be used without modification – meaning lawyers should not need to be involved!!

As its name suggests, the SAFE is designed to be simple and it is today broadly used for earlier stage investments. There are 4 types of SAFE.

- SAFE with Valuation Cap
- SAFE with Discount
- SAFE with Valuation Cap and Discount
- SAFE with no Valuation Cap and no Discount

When a SAFE has a valuation cap it means that regardless of the valuation agreed in the later priced funding round, the SAFE will convert at no-more than the agreed cap. For example – if a SAFE investment of $1M was made with a $5M post-money cap, then the worst case for the investor is that the SAFE will convert providing 20% equity to the investor ($1M/$5M = 20%) before the new money is then added. If this later priced equity round actually provided a pre-money valuation of $6M and if the SAFE had *not* been capped, the original investors equity would only have been worth $1M/$6M = 16.67% - hence they receive an extra 3.33% of the company equity by negotiating a cap. Also – if the later priced equity round provided a pre-money valuation of only $4M for example – then the SAFE would convert giving the original investors 25% equity ($1M/$4M = 25%). So a cap guarantees a minimum % of equity but it can still be more if the priced round down the road is actually less than the originally agreed cap.

If a SAFE has a discount it means that once there is a priced equity round the original SAFE investor can buy the shares at the agreed discount to that priced equity round. So if the priced equity round valued the per-share price at $1 and the discount was 20%, then the SAFE would convert at a rate of $0.80 per share to the SAFE investor.

If a SAFE has both a valuation Cap and a Discount then not both will apply. The SAFE will convert with either the cap or the discount, whichever gives the lower share purchase price (and therefore the greatest number of shares) to the SAFE investor.

Equity
Is the amount of something that you have. If you have equity in a company, you own some shares of that company. If you have 20% equity of a company, you own 20% of the shares.

Pre and Post Money Valuation
When a funding round is done and a hard value is agreed on the value of the business, that valuation can be described as either *pre-money* or *post-money* depending on whether the new investment capital is included or not. The "money" being described here is the new investment capital being brought in. For example – if an investor looks at a company and agrees it is currently worth $5M and he is prepared to invest $1M, then the pre-money valuation is $5M and the post-money valuation is $6M (pre-money value plus the invested amount = post-money value)

Pro-Rata Rights
By default, an investor does not automatically have the right to invest in later rounds as a company seeks more funding. If the company does not want your additional investment capital (perhaps because they have plenty being offered from what they may consider better sources) then that is their right. However, every time further investments are made, more shares are issued which means the earlier investors' overall equity % gets diluted, unless they are able to also buy more shares when the new funding is raised.

Pro-Rata Rights is an agreement - typically made at the time of investment - allowing the investor the right (but not the requirement) to invest in the subsequent funding round, on the same terms as everyone else, to maintain their overall % of equity ownership. This does not mean all funding rounds – just the subsequent round. You would need to again negotiate Pro-Rata Rights beyond the subsequent round.

Discount

The is the amount below the prevailing share price that you are allowed to buy shares. If the priced round equity share price is $1 and you have a SAFE investment with a 20% discount, you can buy shares for $0.80 when the SAFE converts. Do not confuse Discount with Discount Rate (see below) – they are the inverse of each other.

Discount Rate

This is (100% minus the Discount). The Discount Rate is what you multiply the priced equity share price by to get the discounted buy price. For example – if the Discount is 20% then the Discount Rate is (100% - 20%) = 80%. If the share price is $1 then the discounted purchase price is ($1 * 80%) = $0.80.

Carry

This is shown as a percentage and is the proportion of the entire investment *profit* that will be retained by the GP and any other named bodies *after* the original investment capital is paid back to the LPs. For example, consider a typical carry of 20%. Consider then if 10 LPs invested $10,000 each for a total investment of $100,000 (net of all set-up fees) and this grew to $1M over several years. As the investment became liquid (typically through IPO or acquisition) the LPs would each receive their $10,000 back consuming $100,000 of the total. Thereafter, for the remaining $900,000 - 80% would be distributed to the LPs (pro-rata to their investment) and 20% would be retained as the carry by the GP and any other named bodies.

Allocation

This is the size of the investment that is available for any given opportunity the GP presents. This will typically be a subset of the total amount that the company is looking to raise. Note that not all 100% of the defined allocation will be invested as some % will be needed to cover set-up fees and charges such as those made by AngelList. Mapache Capital itself does not charge any set-up fees.

Dilution

When a company raises a new round, they will issue new shares to provide the new investor(s) with their agreed % equity in the post-money company. If earlier investors do not also pro-rate invest in the new round, they will see their overall % equity decrease. They will still retain the same number of shares, but that number will be a smaller % of the new total. This is why Pro-Rata Rights are a nice option to have in an investment agreement if possible. When investing in early stage companies – at pre-seed, seed stage for example – be prepared to get diluted in later rounds if you do not invest further. Don't worry too much however – in successful companies you simply have a smaller % of equity in a bigger pie. As long as the money raising round was an "up" round (which means the price per share has increased) then your shares will be worth more, even if your % of equity has decreased.

If you have any questions on the above please email rob@mapachecap.com