

**Date: 1 June 2016**

## **Upstart Term Sheet for ABC PTY LTD**

We, the Upstart Accelerator Fund, want to invest money in your company, ABC PTY LTD.

### **Structure of Financing**

We're making you an offer of a minimum of \$40,000 investment as your seed round in two equal tranches. This investment will be for a minimum 8% ownership in your company. Your company will issue to us Preference Shares (refer Liquidation Preference below) that convert to the same type of ordinary shares that you already have. A maximum of \$10,000 (i.e. 25%) of the invested money can be used for compensation to each founder in the company up to a limit of \$20,000.

Before giving you all the money we would like to ensure that you have a plan for how you are going to spend the money and systems to track how the money is being spent. The investment will be in two equal tranches. The first tranche will be paid on completion of due diligence, incorporation of your company and execution of the various legal agreements prior to commencement of the program. The second tranche will be paid at the end of the first month of the program providing you have completed the following:

- Attended the core components of the program
- Set up a cloud accounting system to the reasonable satisfaction of Upstart
- Provided a Year To Date Balance Sheet and Profit and Loss Statement
- Provided a forecast cash flow to the reasonable satisfaction of Upstart

We will provide you with help and assistance to complete all these tasks.

### **Option Pool**

Our offer assumes that you've already or will set up an employee share option pool (ESOP) before our money goes in, so that our ownership is "fully-diluted" after accounting for that option pool.

We think you'll need at least a 10% option pool after the investment round in order to hire some key management team members and senior people.

This means that at the time of our investment, Upstart will own 8.8% of the company. This will then "dilute" down to 8% after all ESOP are fully issued.

To make this really clear, see the capitalisation table at the back of this term sheet to see how this looks with actual shareholding and ownership percentages after the investment.

## Conditions to Close

Before we sign the paperwork and transfer our money, we have to do some basic due diligence on the company and also on you, the founders. This includes chatting to some of your business and personal referees.

At the same time, if you haven't already done so, you should also do a bit of due diligence on us. For example, speak to some of our mentors and prior participants and get a feel for what they think of us. We'd be glad to make introductions if it helps.

## Intellectual Property

We ask that you assign all the Intellectual Property including source code, design-rights, domain names, patents, trademarks etc for the business you pitched to us to the company we are investing in via an IP assignment agreement.

## Estimated Closing Date

We'll use our [standard legal agreements](#) which you should review, preferably with a lawyer to help. We hope that we can wrap this all up and finish the investment round with signed paperwork and money in your account no later than 8 weeks from today.

## Documentation and Warranties

It's worth mentioning that our standard investment docs will include some "representations and warranties". These are assurances that you give to us that the business we're investing in is what you say it is. Normally investors have the right to financial claims against the founders if they've misrepresented the business, but we limit our right to claim so that it's only against the company, not the founders, and the amount can't be more than the amount we're investing.

## Liquidation Preference

We're not asking for any complex preference rights (see pointers here [Venture Beat Liquidation Pref article](#) and here [Brad Feld on Liquidation Prefs](#)), but we do ask for a so-called simple 1x non-participating liquidation preference. This means that if the company is sold, we'll get the higher of either the amount of our investment or our ownership percentage of the sale value. In the worst case if the company is wound down with very little left, then anything left below our investment amount would be distributed to us as the investor.

## **Anti Dilution Rights**

As we are investing very early at a reasonably low valuation, Upstart will not be diluted from any future issue of shares below our investment valuation (other than under an authorised ESOP). As Upstart won't be able to stop you from issuing shares after the program starts, Upstart needs to be protected from the Company issuing millions of shares to founders/families/friends "for free" in a manner that dilutes Upstart unfairly. However, if you issue shares at a higher valuation, then Upstart will be diluted at the same rate as any other shareholder (unless it puts more money in, a right that every shareholder will have). We use the fairest anti-dilution mechanism being "broad based weighted average anti-dilution" so that Upstart will never get an increase in its equity if you do a "down round", but just a protection of its equity position prior to the down round.

## **Important Decisions**

We're here to support you, not to interfere in your day-to-day business operations. However as you are just starting out for the next 12 months any important decisions requiring a special resolution of the board or shareholders will require the approval of Upstart. This includes issuing new shares, raising new finance, selling the business, relocating the company or any material change to the business. After 12 months, you will need the consent of Upstart before you (i) do anything that changes the rights of Upstart's preference shares (ii) declare any special dividend, or (iii) undertake a share buyback.

## **Rights of pre-emption**

Before selling shares to a third party a shareholder must first offer shares for sale to existing shareholders.

## **Participation Rights**

We think all shareholders, including the founders, should have the right to invest in future financing rounds to avoid being diluted. This doesn't mean shareholders have to put more money in, but if they want to and are able to, they have that right to maintain their ownership in any future funding round. We ask that you allow us to participate in the capital raise either:

- a. as the Upstart Fund or
- b. through any of the investors in the Upstart Fund.

The participation right we ask for is double our then current equity percentage holding. This means that if we own 8%, and you want to raise \$1M, Upstart (or namely its investors) can invest the first \$160K. This gives the Upstart network the best opportunity to continue to back the company meaningfully as and when you raise capital

## **Tag Along**

If any shareholder owning more than 25% of the shares in the company wants to sell their shares to a third party then they must include the other shareholders in the sale.

## **Drag-Along**

If shareholders, which of course includes you, owning more than 60% of the shares in the company want to sell their shares (typically to accept an acquisition offer) then, as long as the board and a majority of the investors approve it, all other shareholders must also sell their shares. This protects all shareholders from, say, one small, stubborn shareholder refusing to sell their shares in an acquisition offer and blocking a deal everyone else wants to see happen.

## **Restrictive Covenants**

We don't want any of you to start a competitive business or to leave and take team members with you to another business even if it's not competitive. That's not why we are investing in the company and your co-founders wouldn't be very happy with you either. These restrictions apply for as long as you're employed by the company or hold at least 10% in equity and for 1 year after that.

## **Founder Share Vesting**

Even after our investment, you the founders will normally own the majority of the shares in the company. However, our nightmare scenario is that we invest and then the day after you skip off to the back of beyond and we're stuck as shareholders. It may sound far-fetched, but it happens. We are fundamentally investing in you and your co-founders for the long haul and we expect you to have the same view. Making your shares subject to reverse vesting protects us and your co-founders if one of you changes your mind. You will get 20% of your shares upfront with the balance earned monthly over 3 years. If you give up on the team before 3 years you forfeit the shares you have not yet earned (either by cancellation of the shares, or transfer of the shares to the other shareholders).

## **Board of Directors**

You should set up board with at least two directors. We generally do not take a board seat but reserve the right to nominate one director to the board so long as our shareholding is no less than 5% of the total shares on issue.

## **Advisory Board**

We will help you establish an advisory board of 3-4 people drawn from our mentor pool to provide advice and support to you and your fellow co-founders during the program and for the next 12 months. Advisory boards provide non binding strategic advice whereas formal boards of directors have legally defined responsibilities, advisory boards are not regulated under the Corporations Act. Advisory boards advise rather than direct. For more information on the role of advisory boards please see [Company Directors](#). If you don't successfully establish an advisory board, Upstart would be more inclined to appoint a director to assist with the governance of the company.

## **Information Rights**

We'd like to get regular status updates from you in whatever format makes most sense for us all. You are required to maintain an accounting system and give us read only access. For our own fund reporting purposes we'll need monthly financial reports from you during the program and quarterly thereafter.

## **Expenses**

You pay for your legal costs and we pay ours. We don't see why we'd invest cash in your business only for some of it to come straight back out in order to pay our legal bills. We see whatever this deal costs us as our cost of doing business.

## **Exclusivity**

If we both sign this term sheet, it means we'll all be putting time and effort into completing the investment over the next 8 weeks. We don't want you to keep pitching to other investors potentially to replace us during that period. If you decide to switch to another investor in that period and it's not because we've done anything wrong, then we might charge you for our costs.

## **Confidentiality**

We trust your judgement in deciding who to talk to about this offer and when. This is a non-binding offer and things can unfortunately always fall through, so it's really not in your interest nor ours to pre-announce anything until it's done.

## **Non-binding Effect**

This document isn't legally binding but we're still pretty excited about it and the prospect of working with you.

## **Expiry**

We hope you'll decide relatively quickly on whether or not you want to move ahead with us. Obviously it's a big decision so don't take it lightly, but time is your most valuable asset right now and the quicker we move forward and get cash into the company, the quicker you'll be able to focus on building a great business. This offer remains open until we email you to tell you that we've moved on or one week from today.

## **Transaction Documents**

The legal documents that you'll sign are available for your review here [Upstart Legal Documents](#). While we are open to minor variations to accommodate your unique circumstances, the major concepts in the the documents are not negotiable. Every Upstart participant comes into the program on the same terms as every other participant.

## Acceptance

If you're happy with all of this, sign below, or just tell us so in an email reply. Thanks for giving us the chance to pitch to you!

\_\_\_\_\_ Date: \_\_\_\_\_  
Offered by Robert Nathan  
Upstart Accelerator Fund

\_\_\_\_\_ Date: \_\_\_\_\_  
Signed and accepted above by

Name: \_\_\_\_\_ Company: ABC PTY LTD

## Sample Capitalisation Table

ABC PTY LTD

<b>Shareholder</b>	<b>Pre-investment</b>	<b>Post Investment</b>
Founders	82 Shares (89.13%)	82 Shares (82%)
ESOP Reserved	10 Shares (10.87%)	10 Shares (10%)
Upstart Fund		8 Shares (8%)
<b>Total</b>	<b>92 shares</b>	<b>100 shares</b>