



## Lowenstein Sandler's Emerging Companies, Venture Capital Podcast: The Founder's Hour

### Episode 2

[Laura Cicirelli](#), [Eric Weiner](#)

APRIL 2026

- 
- Eric Weiner:** Hi, everybody. Welcome to *The Founder's Hour*, from Idea to Exit, Happy Hour Conversations on Forming, Growing, and Selling a Business, a Lowenstein Sandler podcast series. I am Eric Weiner.
- Laura Cicirelli:** And I'm Laura Cicirelli.
- Eric Weiner:** We're partners in Lowenstein's Emerging Companies and Venture Capital Group. Whether you're forming your first company, negotiating your first term sheet, or preparing for an exit, decisions you make early can shape your company's future.
- Laura Cicirelli:** Each month, we bring the conversations happening at our New York office to the broader founder and investor community, sharing practical, legal, and business insights to help you navigate every stage of your company's growth.
- Laura Cicirelli:** On today's episode of *The Founder's Hour*, we're going to be talking about SAFEs and convertible notes. So we're really excited about this one because I think every time we talk to founders, the topic of financing and SAFEs and convertibles comes up quite often. And so, I just want to take a step back, though, before we jump into the topic today and just talk about where we are so far in the podcast series, right. We've only had one episode where we've talked about founding your company, and so now we've started and we need to get money in the door to just run this company and operations. So, there's two general routes that you can take. The first is debt, and that's more traditional venture debt, which we're going to talk about in our next podcast episode.
- And the second route is issuing equity in your company and having investors come on board. And so that can be either a price round, which we're going to talk about in the future, or through a convertible instrument and, you know, in particular, SAFEs and convertible notes.

**Eric Weiner:** Commonly you'll see SAFEs.

**Laura Cicirelli:** Absolutely, yep. So the SAFE, why do we see that most often I think is the question.

**Eric Weiner:** Well, I mean, look, if you're going to be raising your first round of funding. You want to have some efficiency, maybe you're not raising a ton of money, and, you know, the goal is to get the money in quickly, to not spend too much time. And one of the great things about, you know, a SAFE is it's a very market-driven document, came out of Y Combinator. Most people in the startup ecosystem, even if they're not exactly sure what it is, I've heard of it. And know how to use it. And it's something we, you know, we do all the time, and it's an easy thing to get done.

**Laura Cicirelli:** Yeah, I mean, we're talking about on this episode, both SAFEs and convertible notes. And I want to be clear that the efficiency, the cost, both of those apply to notes and SAFEs. But I think even more so with SAFEs, because you've talked about Y Combinator and how there is a market standard form that is not the case with notes, and we'll get into that.

But certainly, usually most, you know, more efficient than a price round both of these. And then amongst the two of them, the SAFE is going to be even more so efficient.

**Eric Weiner:** I think that's right. I mean, oftentimes we asked, you know, "how long is this going to take?" And if it's an equity round I give my answer of 28 to 35 days. You know if it's a SAFE you might be able to do it in a couple of days. Which is a great thing. And it also is, you know, an instrument that you can, sort of, have a rolling closings with. You don't have to all do it in one shot. You can do an equity financing the same, but again, it's a pretty easy instrument.

Both SAFEs and convertible notes are kind of equity light. Neither of them are equity. A SAFE is effectively a forward contract. And a convertible note is debt, but it's convertible into equity. People invest in convertible notes for the upside. But a SAFE is and convertible note are kind of like preferred stock. A SAFE in particular acts almost exactly like convertible preferred stock in how it would be treated on, on a sale of the company.

**Laura Cicirelli:** Yeah. So in before we even get into, you know, how it's treated in the sale of the company, I guess you had talked about how they are convertible into equity of the company. So how are they converted into equity? I think maybe the next step to go.

**Eric Weiner:** That's a great question. So essentially, if you're going to do a SAFE financing, you're going to raise a particular amount of money, let's assume it's \$1 million. For our purposes on this podcast, we're going to assume the company is raising \$1 million on a \$10 million post-money cap. But what it's saying at the base, the base economics of a SAFE, are saying that if there is an equity financing in the future, so if the company raises preferred stock in the future, the SAFE will convert into a series of preferred stock that is almost exactly like the preferred stock that the company's selling later at a particular economic at a particular price that is set forth in the SAFE.

**Laura Cicirelli:** And you may hear that as shadow series often referred to. And that's when you have, you know, like a series seed and you seed 1, seed 2, that's often a trigger to know there were convertibles outstanding and that's what's happening there. And so you had mentioned the post-money valuation cap SAFE. I would say that's really the most common that I have seen as far as discount mechanisms within SAFEs. Most recently, we do also see, though, there are discount only SAFEs which we can talk about and then valuation cap and discount SAFEs and kind of what, what are those and what are those mean.

**Eric Weiner:** Right. So, I agree with you, by the way, that much more than 50% of the time, you're seeing a SAFE that has something called a post-money valuation cap, and that's the entire economic metric of the SAFE. And what that effectively means is that when the SAFE converts into preferred stock in the next round, and Laura mentioned you hear it as a shadow series, the SAFE is going to get a price per share that is the lower of the valuation cap price.

In our example, it will be assuming that the post-money value was \$10 million, or the price per share of the actual round. So, if I raise a SAFE, I'm a founder, I get \$1 million on a \$10 million post-money cap. I know that as of immediately prior to the equity financing, I've sold about 10% of my company, right? One over ten.

But if the actual price per share of the preferred stock financing into which the SAFE converts is \$8 million, for example, the SAFE holder's

getting a little bit better than that, they're getting a percentage of the company equal to one over eight.

**Laura Cicirelli:** Yeah. And I think that's one of the reasons why it's become so popular is that investors, as well as founders, kind of like to have a little bit more clarity into what is the percentage I'm giving away right now when I enter into this convertible. When you have a discount only, I think it's, you know, in meaning that's like what you think of when you go to the store and have a coupon, like you get a 20% discount off the next round's price. But we have no idea what that price is going to be and what your ownership is going to be of the company.

**Eric Weiner:** Right, because if you have a SAFE that does not have this valuation cap thing, we're talking about, and the only thing it has is a discount, let's assume it says at the equity financing to which the SAFE converts, there's going to be a 10% discount to the price. We talked about an equity financing of it with an \$8 million value. The SAFE would convert at \$7.2 million because 10% of 8 million is 800,000. So that's the discount. And to Laura, your point, it's an unknown. You don't know what the next round financing is going to be. So, you don't really know what the price of the SAFE is going to be. So, if you raise \$1 million on a discount only, what happens if you do it, and it's unlikely, but what happens if you do an equity round at a \$6 million post.

**Laura Cicirelli:** Exactly.

**Eric Weiner:** Like you just sold quite a bit of the company.

**Laura Cicirelli:** Absolutely. So, I think having that clarity is both good for founders, as well as investors, I think they do want to have a sense of, you know, what they are going to be purchasing, although the discount, you know, and discount is very beneficial to investors.

**Eric Weiner:** Very oftentimes I think what Laura and I hear from, you know, company side clients when they're raising their first round of funding by a SAFE or a convertible note is, you know, what's the right valuation.

**Laura Cicirelli:** Always, yeah.

**Eric Weiner:** And, you know, I think our answer is very commonly it's a little bit of art and science. And it's going to matter about how much the company is raising and I think it's important for companies and

investors, because I think this actually is equally important to both, that there's if you're successful, the company's successful, it's going to raise multiple rounds of financing in the future and after you get past this SAFE financing round, you're probably going to sell 20 to 25% of your company every time you raise an equity financing. I mean, I think that's a fair—

**Laura Cicirelli:** Yeah, I think that's pretty standard.

**Eric Weiner:** So, we would probably say to a client, you know, this round, a company side client, you know, in this round, 10 to 15% of the company, and you want that money to last how long?

**Laura Cicirelli:** 12 to 18 months.

**Eric Weiner:** Yeah, I would think that. So, if you're going to raise a million bucks, that's why we were using the example of the \$10 million post-money cap. But this is such an early stage of the company. If this is actually your first round of funding, that there's a little art and science you're just not going to be, usually there's not some performance metrics that you're showing to the market that you can value the company.

**Laura Cicirelli:** Yeah. And it's a confusing thing for founders to kind of wrap their heads around. I think that there's a valuation in here, but it's really for purposes of determining, you know, how much of the company are you giving away. It is an implied value of the company. Right. But it's not the same thing as going out and getting like a 409A valuation.

**Laura Cicirelli:** And I know we talked about that and we will talk about it in other podcasts. But it's not saying that this is the value of the company at this point in time. That's not what the purpose of that valuation cap is. It is to say in the future financing round, what is the discount that the investors are going to be receiving?

**Eric Weiner:** Yeah. And also, it makes clear to everybody what are we going to own. What does the investor or the investor group going to own as of one millisecond prior to the equity financing?

**Laura Cicirelli:** Yeah, and let's talk about that. I think that's important too. It's one millisecond before the financing happens. So, you are going to be diluted by the new money coming into that round. If you don't have anti-dilution protection on, you know, any new money that's coming in as the new rounds, you know, series seed cash, right. You are

protected though from any other convertible securities that are issued by the company after you while your note is still outstanding or your SAFE is still outstanding. So, you get that protection.

**Eric Weiner:** Meaning that if I invest \$1 million on the \$10 million post-money cap, I'm sticking at that 10% if the company goes out and raises other convertibles.

**Laura Cicirelli:** Exactly, regardless of what the company goes out and raises prior to that equity financing round. However, if the company then gets a term sheet from the lead investor that says, we're going to put \$10 million into this new round, you are diluted by the 10 million the same way that everyone else on the, you know, all people on the cap table are the founders, and maybe some service providers who have equity that will also be diluted by that new money.

**Laura Cicirelli:** One thing that we talked to founders a lot about is the idea of, well, what exactly is taken into account in that mathematical equation? What about the equity incentive pool? Are those shares included even though they're not issued in outstanding? And the answer is yes. So, if the company has an equity incentive pool, that is let's say 10% of the company.

**Eric Weiner:** And typically when the company is formed, as we talked about last time, they usually create some sort of an option pool.

**Laura Cicirelli:** Yeah, 10% is very standard. And so, if you have a 10% equity incentive pool, half of it is unallocated. So, at 5% you're not going to be diluted by that as the investor when the company goes and does its price round.

**Eric Weiner:** But the founder will.

**Laura Cicirelli:** Yes. And so usually in these financing rounds, we'll talk about it in a future podcast as well, there's going to be some type of equity incentive pool top off. So after this round you know the company agrees to increase its plan by, you know, an extra whatever percent to get the aggregate available pool to 10% after the financing, any type of increase of the plan that's done in connection with the financing, you will be diluted by that as the investor.

**Eric Weiner:** Yeah. And usually—when we get to that podcast, we'll talk about it—but you know it really ends up being a price negotiation between the

company and the investors. But this is a very important math to do. You know, these SAFEs are form based. They are available online. And even though they are, it doesn't mean that founders or investors should just use them, because there should be some discipline around how many of these SAFEs are issued, to whom they are issued to. But back to what we were talking about just a little bit earlier about, you know, the size of the round and how much you're taking in at the earliest stages.

There should be, and this benefits both the investor and the company, if you sell too much of your company at this very, very early stage, you might be setting yourself up for pain later. Because if after the next two or three financing rounds, the founders or management, the people who are making the business valuable are under equities because they've been diluted too much, like if you sell 30% of your company in your first pre-seed SAFE at a \$10 million valuation cap, that is a mistake not just for the company, but for the investors.

**Laura Cicirelli:** Yeah, the investors want to make sure that the founders are to be incentivized to get up and run this company. They're investing; they're not in the business of running these companies.

**Eric Weiner:** Correct. And just knowing you're going to be in a recap scenario in the future is not helpful. So, there should be a balance. There should be a balance of what the right number is for both sides.

**Laura Cicirelli:** Absolutely.

**Eric Weiner:** We've talked quite a bit about the SAFE, and it's funny because it's only a five page form. SAFEs do effectively operate economically like preferred stock. We talked about what happens if there's an equity financing. There's a conversion feature in the SAFE usually. What happens if the company is sold before there's ever an equity financing round?

**Laura Cicirelli:** And we get this question a lot because founders often ask us, well, why would an investor want invest in this instrument if there's no guarantee that that this thing is going to convert? And we say there are certainly protections for them in that situation.

**Eric Weiner:** And the SAFE explicitly states that for waterfall purposes on a sale of a company, if the company is sold prior to a conversion, prior to any equity financing, the SAFE's outstanding. It's just two founders and

the SAFE holder. The SAFE holder is paid out before the common stock held by the founders. SAFEs are number two in the waterfall. Debt and then SAFEs and they're treated same as preferred stock. And, by the way, like preferred stock, the SAFE holders get the greater of their investment amount back or the amount they would have received had they converted the SAFE to common stock at the valuation cap price or the discount price, or whatever it ends up being. If it has a discount and then the common get paid. And that's exactly how the basic preferred stock works.

**Laura Cicirelli:** Yeah. And it's also if there's a wind down of the company, right. So, they're really protected.

**Eric Weiner:** Yeah. It's the same downside.

**Laura Cicirelli:** Exactly right. So, and going off of the idea of it's very much equity like QSBS, which I know we spoke about on our first podcast in detail. There is specific language that's in the Y Combinator form of SAFE that you can see online. It's the last paragraph that has explicit language in there that for tax purposes, this instrument is being treated like equity. So, your QSBS holding period, that's going to start once you sign on to the SAFE.

**Eric Weiner:** Yeah. Which is an amazing benefit to investors. Now one thing that's not as amazing for investors is if you have a SAFE, you're not a stockholder. The company does not, as far as we know, up to this at this time, I don't know that there's, slew of Delaware Chancery Court cases on this, but the company does not own fiduciary, ow fiduciary duties to a SAFE holder.

**Laura Cicirelli:** And you don't get to vote, right, unless you have actual equity in the capacity of shares.

**Laura Cicirelli:** And you know, there's no, you know, statutory information rights that you as a shareholder are entitled to under Delaware law as a SAFE holder.

**Eric Weiner:** Yeah. I mean in many exit scenarios where a company, in which you are a SAFE holder of it, sells, you might get a SAFE cancellation agreement and say, here you go. Like, here's the consideration you're receiving, by the way, give us a release in this cancellation. But we're not really giving you any other information.

**Laura Cicirelli:** No merger agreement. No purchase agreement. Just sign this and here's your cash.

**Eric Weiner:** No waterfall. Like you don't get the information statement; you don't have to. I mean, for investors it's a great tool in that it's amazing that you're really not getting equity. It's equity light but you are getting the QSBS clock to start. But I think this is probably more important for an investor who invest in a SAFE, maybe as a bridge around in between an equity funds, like later on in the company's life. But they, investors, should know there's not fiduciary duties owed to you.

**Laura Cicirelli:** Yeah, absolutely. And so notes, convertible notes. And I think one of the things we hear often, we always correct both founders and investors and, actually, I've corrected accountants and other professionals, "SAFE notes" that term it is, they should not be used.

**Eric Weiner:** Literally like my biggest pet peeve.

**Laura Cicirelli:** Yeah. Those two words should not be used in a sentence next to each other unless a sentence is: "SAFE notes is incorrect."

**Eric Weiner:** Right. Well, I mean, what's interesting is for people who are sophisticated and are in our world, they'll know SAFEs are not notes. But sometimes you do see a wide variety of investors into these instruments. And someone who's told they have a SAFE note may be under the impression that they're getting debt and they're getting an interest rate and all this other stuff but they're not.

**Laura Cicirelli:** That's the big difference between the two instruments, right. So, the SAFE, very equity like, convertible notes, there's an interest rate, there's a maturity date usually—18 to 24 months I'd say is pretty standard. And it's treated as debt in the waterfall. Right so when we talked about the SAFEs, the SAFE holders getting paid out amongst, you know, the preferred shareholders of the company for notes, they're going to be paid out first with debt. So that's one of the big benefits of convertible notes is this ability to accrue interest as well as get paid out first.

**Eric Weiner:** Yeah, they're top of the stack. Safes are paid after debt. Convertible notes are paid with debt. They're at the top. So even if the company raises a convertible note after it's already sold preferred stock, the convertible note holders are paid before the holders of preferred stock. I mean, it is a better position on, in the waterfall than saves.

**Laura Cicirelli:** Absolutely. And I think when we talk about the conversion mechanics of a note into a future financing round, all that's very similar to a SAFE, right? You usually have the post-money valuation cap, a discount, or some combination of the two. The thing that's different is that notes are very bespoke and they can be customized. There's no Y Combinator or any real standard market form here. So, they are a bit more costly to put together because there is no form. You need to have counsel put that draft together. There are more robust reps that the company is making to the investors in these notes.

**Eric Weiner:** Potentially.

**Laura Cicirelli:** Yeah, usually. Usually, the SAFE has more fundamental reps. Convertible notes, you'll see, not always but often, I think sometimes more robust reps in there regarding cap table and things like that.

**Eric Weiner:** Yeah, I think it's when you're company side. I think, and you know you're raising by a SAFE. I think it's easier for the company to say to the investors, "Investors, we're using the form. The form has five reps. Those are the reps you're getting. We're done." When it's a note round, there is no god; there's no investors. We're using the form. There is no form. There's precedent. But you're not going on the World Wide Web and finding the form.

**Laura Cicirelli:** Yeah. Exactly right. And I think the conversion into preferred stock is, you know, very similar to what you see with the SAFE. But there are a lot more opportunities to build in these protections and things into a convertible note. For example, what happens at maturity? Do we have the ability as an investor to say, "company, I want you to pay me back plus interest at maturity if nothing has happened to this note." Do we want to say, "I want the right to convert into common stock at maturity, or even an existing series of preferred stock, or a completely new series of preferred stock? And here's the term sheet, and I'm going to attach it."

**Eric Weiner:** We've literally seen at maturity, we're going to convert into the preferred stock on the terms in the term sheet, attached here too is exhibit A.

**Laura Cicirelli:** Yeah.

**Eric Weiner:** And so now you've got this note; you've had to negotiate the note and the preferred stock financing round.

**Laura Cicirelli:** That's when it can get super pricey, right, and time-consuming and things like that I think are a bit of outliers. You don't usually see that, but I've certainly seen it.

**Eric Weiner:** Yeah. I mean I think what we would say is if you're thinking about your first round of funding and it's through a convertible instrument, greater than 90% of the time, you're seeing it as a SAFE.

**Laura Cicirelli:** Would you say notes are more later stage more?

**Eric Weiner:** Yeah, I think so. And it makes sense because there's it makes sense that investors at a later stage, if there's a bridge—and we'll talk about this at a later podcast, I don't want to get into it too much—that the additional downside protection, the interest rate being top of the stack, thinking about all the different things that can happen. That's why you have maturity stuff and you know what happens on conversion. It makes sense that that maybe be a note and maybe the company's a little bit more mature then. And it makes sense to have more reps and warranties and things like that.

**Laura Cicirelli:** I agree. I think I see notes a lot in more distressed situations where we need to get money to the company quickly. The investors want to have that downside protection, like you said, but we don't want to do the full price round at this time.

**Eric Weiner:** Agreed.

**Laura Cicirelli:** And so, what about QSBS in the position there with notes? Because I know there's differing positions, views on that.

**Eric Weiner:** Right. So we were saying one of the, you know, pound for pound, the economics of a convertible note are better for the investors. They just are. Top of the stack, interest rate, all that stuff we talked about. We have seen people take the position that a convertible note, since it is meant to convert, people invest in convertible notes because they want to ride upside. They don't want to just get their money back plus interest. They want to get the equity.

**Laura Cicirelli:** They're not looking for the 7% interest.

**Eric Weiner:** Correct. So, we have seen people take the position that the note for income tax purposes, QSBS will be treated as equity. People argue against that position. I don't think people argue against the position in the SAFE. So, investors might have a trade off, right? I want to get I

want to make sure I'm getting the top of the stack protection of having a note. But if I want to take the position this is QSBS, I may not be able to do that.

**Laura Cicirelli:** Yeah, absolutely. May still try, but it's not a certainty that that position is going to be upheld.

**Eric Weiner:** But it better be in the note, like the language that we're taking this position better be in the note for you to then try to take that position.

**Laura Cicirelli:** And it's similar language to what we talked about with the SAFE. That last paragraph in the SAFE of, you know, this is going to be treated for.

**Eric Weiner:** Yeah, but it must be identical.

**Laura Cicirelli:** Yeah. Exactly right. And so before we leave the topic of convertible notes, I often get this question of, there's different ways that this can be drafted. Sometimes you see a note purchase agreement with an accompanying note. Sometimes you see a single convertible note where it has everything layered into it. So it could really take different forms. It could be two separate documents: the purchase agreement itself, coupled with a series of notes, or it could just be, you know, a single document that has everything in it. So just be on the lookout for that. There's different forms that it could take.

We should talk about side letters quickly. You see them with both convertible notes and SAFEs. But I say most often you see them with SAFEs. And the reason being is that the convertible note, like we said, it's customizable, right? So, if there's any real rights that you want to have there, you can layer it in. The one time that you're going to have it through a side letter is because you don't want everyone who's coming into the round to have that right, maybe just the lead investor or a few investors to have these special rights. And so what do we often see inside letters?

**Eric Weiner:** One of the reasons to do a SAFE is because it's inexpensive, right? It's easy, inexpensive, and you're negotiating the principle economic terms, right. We were talking about the valuation cap, \$1 million investment, \$10 million post-money cap. You're selling 10% of the company. It's going to be like preferred stock economics. Pure, pure, pure economics. And you're punting the stockholder rights and voting rights and all these types of negotiations that you're going to have in connection with an equity round to the equity round.

And presumably you're doing that because you're not raising a tremendous amount of money, not raising \$5 million or \$10 million. And maybe you're raising money from multiple parties.

**Laura Cicirelli:** Yeah. There's not a true lead, maybe, who's putting in \$2 million? It's a bunch of people putting in \$400,000 or something like that.

**Eric Weiner:** Yeah, but there might be a lead or 2 or 3 who may ask for a side letter that usually what we see at the earliest stages, sometimes you see people ask for more, but usually what we see is what they want a pro-rata right.

**Laura Cicirelli:** Into the next round. It's usually limited just to that next financing round where the SAFE's going to convert or the convertible notes are going to convert. I'd say sometimes you'll see some information rights.

**Eric Weiner:** Yes. Some funds just need those for reporting purposes.

**Laura Cicirelli:** Sometimes you'll see, and we'll get into discussions about this I think in the equity financing round, some funds need management rights because of the type of funds that they are investing. So those could be things like the right to consult with management to, you know, talk to them about the day-to-day business operations, things like that.

So, those are really the type of rights that we see. Sometimes we see most favored nations provisions, MFNs. And those are when your company side founder's a bit dangerous and I'd say to be wary of and just to know the implications of what that exactly means and how can we limit them.

**Eric Weiner:** Right. So, if we're on the company side, and that basically means that if the company ever raises money before the equity financing via another convertible instrument, so it raises money by another SAFE or another convertible note the investor, if they have an MFN, would get the option to change their SAFE or convertible note into the better SAFE or convertible note that the company sells in the future.

When we are company side and representing the company, and we try to limit that to economic rights only, so if there's a better valuation cap for the investor, okay, they get the better valuation cap. Or if there's a better discount for the investor, okay they get the better discount.

**Laura Cicirelli:** But would not pick up things in like a side letter, better information rights, things like that. If you limit it truly to economic terms and that's the point of that notation.

**Eric Weiner:** And there is some form language on MFNs on the YC SAFE that when we're company side, we do change. We change to make this clear. Look, when we're on investor side, we may say different things. We may say if you issue anyone anything better ad that might include a side letter that has more rights than my side letter, I get that too. So MFNs are something that really should be focused on very, very intently by both sides.

**Laura Cicirelli:** And there should be carve outs to it in the Y Combinator form will have those carve outs. And when I say carve outs, I mean things like it's not all type of instruments that are issued during the time that you're SAFE is outstanding.

**Eric Weiner:** Like an option grant.

**Laura Cicirelli:** Exactly. Things like that. Those should not be included. So you shouldn't get any benefit or adjustment because of those type of issuances.

**Eric Weiner:** But, you know, the last thing I'll say about side letters is the point we were talking about earlier. Safes and convertible notes generally are meant to be efficient and fast, inexpensive. So if you end up doing a SAFE with eight investors and all eight get side letters, it's not going to be that fast. It's not going to be that efficient. And so you want to, you know, the lead, someone is running a real check, someone's giving you \$700,000 and they want a side letter. Okay. You know, it makes sense. Someone's giving you \$15,000. They want a side letter. Maybe not.

**Laura Cicirelli:** Yeah, and think about it too, right? I know that you want to get money in the door quickly, but you have to think of it for precedent setting purposes. It's not going to be a great look when you want to push back on other investors, or even in a future round when people are looking at your data room with all these side letters and saying, you know, well, "I want a side letter, you issued it to someone who gave you \$15,000 in your convertible round. Why are you not giving it to me now? I'm putting in 50."

**Eric Weiner:** You got to give it to everyone.

**Laura Cicirelli:** Yeah, exactly. Right. So there's certainly tons of benefits that you mentioned about doing a convertible round, but there's also some pitfalls that we want to just flag and talk about. One is the idea of stacking. And you often hear it as SAFE stacking, convertible note stacking. What does that mean? I think that there's a psychological trap for these convertibles that is just easy money.

**Laura Cicirelli:** And so, you want to go and, you know, get as much money as you can in the door because you have to operate this company, but you don't realize how much you're giving away. So, you do one round of financing with a \$10 million post-money valuation. Then you do, you know, a year later, 15 million, 20 million. What am I actually selling at the end of the day? And that's really important. We talked about wanting to make sure the founders are incentivized, and you're not giving away your entire company because it's going to lead to an expensive recap situation.

**Eric Weiner:** I mean, it doesn't happen as much as it used to, but yeah, when SAFEs were first really becoming popular, we used to see, I used to look at it like it was like Halloween. Founders were giving out SAFEs like they were candy. And, you know, you have a SAFE with a 5 million cap, a 6 million cap, a 7 million cap.

**Laura Cicirelli:** Even on the same day, sometimes I've seen, unfortunately.

**Eric Weiner:** Which you cannot do because that's not going to be the securities laws aren't going to love you if you do that. So, do not issue different securities to different investors on the same day, meaning, don't issue a \$10 million cap and a \$12 million cap to two different investors on the same day. Don't do it.

But what founders were being very surprised by was how diluted they were getting by issuing these SAFEs like candy. And even though there are forms online, there should be discipline attached to raising these SAFE finances. Amazing to have to have built a company in its early stages where someone is willing to give you money for it. That is an incredible achievement, even if it's not a lot of money. There's not a lot of people in the world who've created a company that people want to give them money for, but you got to be careful.

**Laura Cicirelli:** Yeah. And the discipline point, that's something really important. We speak to our founder clients about it all the time. When you're

approving as the director, maybe it's just you as the sole founder, sole director, but maybe there's a group of directors when you have the board approving this series, this SAFE financing round, we like to put in that board consent some type of a dollar figure.

So we are raising 2 million, \$3 million on this form of SAFE. And it gives you that discipline that if you go above that 3 million you have to go and get another board consent, but also take a pause and think, what does this mean? It means now I'm going above that 10% threshold that I had spoken about with my counsel, and I'm approaching 15% of my company.

**Laura Cicirelli:** And, you know, giving yourself time to think about that is very important and to just breathe a bit.

**Eric Weiner:** I think sometimes even our clients may ask why we're doing it. It's the discipline. Point is, you want to make sure that everybody and I do want to reiterate that both sides, I think, are protected by these early, early rounds not being too dilutive because you want to think about the long game and what the what the ultimate end is and that should benefit everyone.

**Laura Cicirelli:** Yeah, absolutely. And so the idea of just issuing a bunch of different securities, we often get questions about "what is the right check size?" And, you know, "how many investors should I be going out to?" "Is a best practice to go and get four investors on this form of a SAFE or is it okay to get ten?" And I think it's really a case-by-case basis. There's no real science to this, right. But I think that you just need to keep in mind what happens with these SAFEs. They're going to hopefully convert in a price round. In connection with that price round, the lead investor is going to want each of these SAFE holders to now, as shareholders of the company, sign on to the documentation, the shareholders agreements, that you're putting into place.

**Eric Weiner:** Shareholders, the company because they'll be converting into that.

**Laura Cicirelli:** Absolutely.

**Eric Weiner:** Yeah, you don't want to add friction to the equity financing because if you have to chase 15 people to sign on to these documents because the investors are, I think, correctly saying, we want these people signing up to these documents, you might not be able to close your equity round until you get everybody.

So not every investor's the same. And, you know, you may have, your best friend from high school may want to give you \$5,000 on the SAFE. Now, that friend better be accredited to take the money. So, you have to be an accredited investor to invest.

**Laura Cicirelli:** We still have to comply with securities laws, right? These are securities.

**Eric Weiner:** The QSBS positioning. We're taking the position that it's a security, you know that might not be money worth taking. And if that person's going to be hard to find or be difficult, like not all dollars are the same. And, you know, it's great if you need the money and someone's willing to give it to you, but you should think about who you're taking it from, how much you're taking from them. Usually some real minimum to know that the investor is for real, I think, makes sense.

**Laura Cicirelli:** Yeah. I mean, not every dollar is the same, like you said. I've had very small investors in a convertible round ask for the most robust side letters where the lead hasn't even asked for half of the rights.

**Eric Weiner:** I have seen very small investors be the most difficult people on the cap.

**Laura Cicirelli:** So, something to think about for sure.

**Eric Weiner:** No professional investors, for the most part, operate within the market. And because of that, behaviorally, there's a market here. And, you know, it's a small community. And there's a behavior set, which is great. I mean, it's great to be part of that venture community. You know, your friend may not have that same sensibility. And by the way, your friend might not be your friend forever.

**Laura Cicirelli:** Absolutely.

**Eric Weiner:** And any hold up value gives that person leverage. And look, just to, just to summarize, SAFEs and convertible notes effectively serve like, preferred stock, except notes are at a higher level of the waterfall than SAFEs. The SAFEs will convert, and the notes, to add some value to the next round or some discount, some valuation cap in the next round or some discount to the price per share in the next round.

In both cases, if the company is sold prior to the company raising an equity financing, so prior to conversion, those instruments will get paid based upon the economics in the instruments and they're gonna

be paid kind of like they are preferred stock, generally. That's usually how it works. There are some bells and whistles that come along with these instruments. We talked about side letters, MFNs, and all this other stuff. Main point being they are simple, relatively simple compared to an equity financing. They should be less expensive and easier to do. But they are complicated as well and there are nuances as well. So, make sure you're speaking to your advisors about it if you're thinking of raising money by either of these instruments.

**Laura Cicirelli:** Absolutely.

**Eric Weiner:** Thank you so much for joining us for *The Founder's Hour*. If you enjoyed this episode, be sure to subscribe on Apple Podcasts, Spotify, YouTube, wherever you listen so you don't miss future conversations.

If you would like to join *The Founder's Hour* events live in our New York office, you can contact [TheFoundersHour@lowenstein.com](mailto:TheFoundersHour@lowenstein.com) for details. You can also contact Laura or me.

**Laura Cicirelli:** Next time we're going to be talking with our partner Raquel Smith, who's a member of our debt team, about different types of venture debt facilities.

**Eric Weiner:** Until then, thanks so much for joining us.