SAFE Investment Details

What is a SAFE?

A Simple Agreement for Future Equity (SAFE) is an investment contract that's very commonly used by early stage startups.

Investors in SAFE contracts will get equity in the company they're investing in at a future date when there is a firm valuation on the company — typically when the company raises a follow-on financing round from professional investors (e.g. Venture Capital firms), or when the company "exits" (e.g. is acquired, or goes public).

Regular equity investment contracts (called "Priced Rounds") might involve a 50 page document, and $50,000+ in legal fees — which don't make any sense for early stage startups to incur. So in 2013, the Y Combinator accelerator pioneered the SAFE investment structure, to make things a lot quicker, easier and cheaper for startups in their portfolio. Since then, SAFEs have become widely adopted by startups throughout America.

How might I earn a return?

Table of Examples

The following table demonstrates how investment will convert to equity in different scenarios. The key variables at play are:

- Amount of investment
- Valuation cap
- Discount
- Future valuation when the SAFE converts to equity

Pay special attention to rows 7 and 9 -these are the terms of QuestRead’s crowdfunding campaign.

Note a couple of things:

- The % of equity received has a lower bound (good for investors) regardless of how high the valuation gets. You can see that in the light-blue highlighted cells. As the valuation increases (moving to the right), the equity hits a lower bound and stays there.
- The discount will increase the amount of equity received at valuations around or lower than the valuation cap. This acts as a bonus for investors where the future valuation at time of conversion to equity is not as high.

					Valuations (Priced Round or Sale/Liquidation Event) Triggering SAFE -> Equity Conversion					
				$4,000,000.00	$4,500,000.00	$5,000,000.00	$6,000,000.00	$7,000,000.00	$8,000,000.00	$9,000,000.00
	Investment	Valuation Cap	Discount							
	$10,000	$4,500,000	0.00%	0.25%	0.22%	0.22%	0.22%	0.22%	0.22%	0.22%
Early Bird ->	$10,000	$4,500,000	10.00%	0.28%	0.25%	0.22%	0.22%	0.22%	0.22%	0.22%
	$10,000	$5,000,000	0.00%	0.25%	0.22%	0.20%	0.20%	0.20%	0.20%	0.20%
Standard ->	$10,000	$5,000,000	10.00%	0.28%	0.25%	0.22%	0.20%	0.20%	0.20%	0.20%
	$10,000	$6,000,000	0.00%	0.25%	0.22%	0.20%	0.17%	0.17%	0.17%	0.17%
	$10,000	$6,000,000	10.00%	0.28%	0.25%	0.22%	0.19%	0.17%	0.17%	0.17%
	$10,000	$7,000,000	0.00%	0.25%	0.22%	0.20%	0.17%	0.14%	0.14%	0.14%
	$10,000	$7,000,000	10.00%	0.28%	0.25%	0.22%	0.19%	0.16%	0.14%	0.14%

Long-Form Example

Imagine that you invest **$10,000** in a SAFE contract with a **$5M valuation cap**. This means you are guaranteed at least **0.2% equity ownership** in QuestRead.

Now, the company raises an additional **$5M** on a **$20M pre-money ($25M post-money)** valuation.

You have **0.2% ownership**, so your investment is now worth **$50,000** based on the pre-money valuation.

The additional $5M of investment dilutes your ownership stake by **20%**, so now you have **0.16% ownership** of the company, compared to the original 0.2%. But **0.16%** of the **$25M post-money valuation** is still worth **$50,000**, meaning the value of your investment has **doubled** on paper.

However, while the value of your investment has increased on paper, you still haven't realized a rate of return yet.

Now, let's say QuestRead is acquired for **$250M**. You, with **0.16% ownership**, will receive **$400,000**. That's a **40X return** on your initial **$10,000** investment.

While this example is a best-case scenario, most startup investments don't work out like this. Many early-stage startup investments go to **$0**, or the returns are significantly smaller than 40x. Investing in startups has high potential upside, but it's also highly risky. So, you should never invest more than you can afford to lose.