CALIFORNIA STARTUP & INVESTMENT LAW

SAFEs vs. Convertible Notes: Startup Financing Explained

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Startups seeking early-stage funding often rely on flexible investment instruments rather than traditional equity financing. Two of the most common options are SAFEs (Simple Agreements for Future Equity) and convertible notes. While both are designed to delay valuation discussions, they differ in structure, risk, and investor protections.

What Is a SAFE?

A Simple Agreement for Future Equity (SAFE) is an agreement that allows an investor to provide capital in exchange for the right to receive equity in the future, typically during a priced funding round. SAFEs are not debt instruments—they do not accrue interest and generally do not have a maturity date. Instead, they convert into equity when a triggering event occurs, often at a discount or with a valuation cap.

What Is a Convertible Note?

A convertible note, by contrast, is a form of debt. It accrues interest and has a maturity date by which it must either convert into equity or be repaid. Like SAFEs, convertible notes often include a valuation cap and/or discount, but they also provide investors with additional protections due to their debt-like nature.

Key Differences

The primary distinction lies in risk allocation. Convertible notes offer investors more security because they are technically lenders until conversion occurs. SAFEs, on the other hand, are simpler and often more founder-friendly, but they provide fewer safeguards for investors.

Additionally, the absence of a maturity date in SAFEs can simplify negotiations, while convertible notes may introduce pressure if the maturity date approaches without a qualifying financing event.

Choosing the Right Instrument

The decision between a SAFE and a convertible note depends on the company's stage, investor expectations, and overall fundraising strategy. Each option carries legal and financial implications that should be carefully considered.

Final Thoughts

Both SAFEs and convertible notes can be effective tools for early-stage financing. Understanding their differences allows founders and investors to structure deals that align with their respective goals and risk tolerance.

About the Author

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