

Term sheet explainer

Clause	Explanation
Key Man Exclusivity	This clause states that a specific person who is crucial to the success of the business deal cannot work with any other company during the term of the agreement. It is designed to ensure that the person stays committed to the deal and does not work for a competitor.
Non-Compete	This clause states that one party agrees not to engage in similar business activities as the other party for a certain period of time. It is designed to prevent one party from taking advantage of the other party's confidential information, trade secrets, and other valuable business information.
Non-Solicit	This clause states that one party agrees not to hire or solicit the employees, customers, or suppliers of the other party. It is designed to prevent one party from poaching valuable assets of the other party.
Promoter's Lock in share transfer	Investors want to make sure that the promoters are committed to the company and won't just sell their shares and walk away after they get the investment money. The lock-in period gives the investors some assurance that the promoters will be in it for the long haul.
Investors or Board Consent Matters	Investors or Board Consent Matters are certain actions that a company cannot take without the approval of its investors or the board. These actions could include selling the company, changing the business in a major way, or borrowing a lot of money. Investors put money into a company and want to make sure it is managed responsibly, so they (or nominate someone on the board to) may want to have a say in certain decisions. The term sheet outlines what decisions require investor or board approval and how much approval is needed. As an investor, this gives them some assurance over the company's direction and protects their investment.
Dilution	Dilution in a term sheet is when a startup company issues new shares of stock, which reduces the ownership percentage of existing shareholders. It's like cutting a pizza into smaller pieces, each piece representing a share of the company. Dilution is important for startups because it allows them to raise more money by selling new shares of stock to investors. However, it also means that existing shareholders will own a smaller percentage of the company. So, it's important for startup founders and investors to understand how much dilution will occur and how it will affect their ownership stakes.
First Pre-emptive rights	First pre-emptive rights in a term sheet are a type of protection given to current investors in a company. It means that if the

	<p>company decides to issue new shares or securities, the current investors have the right to buy those new shares before anyone else. This helps ensure that the current investors don't lose control or value of their investment by dilution.</p>
Pro rata rights	<p>Pro rata rights in a term sheet mean that if a company wants to sell more shares, existing investors have the right to buy more shares to keep their ownership percentage the same. For example, if an investor owns 10% of a company and the company issues new shares, the investor can buy enough new shares to maintain their 10% ownership.</p>
Right of First Refusal (ROFR)	<p>Right of first refusal is a term that gives someone the chance to buy something before anyone else can. For example, if you have a right of first refusal on a house, the owner has to <i>offer it to you first</i> before they can sell it to anyone else. It's important because it gives you a special opportunity to buy something you might really want, and it can also help you avoid getting into bidding wars with other buyers.</p>
Right of First Offer (ROFO)	<p>Right of First Offer (ROFO) is a clause in a contract that gives someone the first chance to buy something before others can. For example, if you have a ROFO on a house, you get to buy it before anyone else can.</p> <p>ROFO is important because it gives you a better chance of getting something you really want. It also gives you more control over the situation because you get to decide if you want to buy it or not. ROFO can be used in business deals to protect your interests and make sure you have the option to buy something before anyone else can.</p> <p>Usually given to promoters. This is important for the promoter because it allows them to maintain their ownership stake in the company and potentially increase it, without having to compete with others.</p>
Tag Along	<p>Tag-along rights are a provision in a business agreement that allows minority shareholders to sell their shares alongside majority shareholders (usually founders in case of very early stage company) in case of a sale of the company. It means that if the majority shareholder wants to sell their shares, the minority shareholder has the right to join the sale and sell their shares as well. This is important because it protects the minority shareholder's investment and ensures they are not left out of a potential profitable sale.</p>
Liquidation preference	<p>Liquidation preference is a term in a business deal that says if the company gets sold or shuts down, some people get their money back before others.</p>

	<p>For example, if an investor put in \$10 million and had a 2x liquidation preference, they would get \$20 million back before anyone else gets paid.</p> <p>It's important because it can affect how much money people get back if things go wrong. Investors want a high liquidation preference to protect their investment, but founders want a low liquidation preference to keep more money for themselves.</p> <p>There are a few common types of liquidation preferences:</p> <ol style="list-style-type: none"> 1. Non-participating: Investors get their money back first and then split the remaining money with everyone else. This is the most founder-friendly option. 2. Participating: Investors get their money back first, and then also get to split the remaining money with everyone else. This is less founder-friendly. 3. Capped: Investors get their money back first, and then split the remaining money with everyone else, but there is a cap on how much they can get back. This is a compromise between the founder-friendly and investor-friendly options.
<p>Anti-Dilution Protection</p>	<p>Anti-dilution protection is a term in a contract that helps protect investors from losing value in their investment if the company issues more shares in the future at a lower price than what the investor paid. It adjusts the number of shares the investor owns to keep the value of their investment the same. It's important because it gives investors confidence that their investment won't be diluted if the company raises more money in the future.</p> <p>There are two common types of anti-dilution preferences in a term sheet: full ratchet and weighted average.</p> <ul style="list-style-type: none"> • Full ratchet means that if the company issues more shares at a lower price than what the investor paid, the investor's ownership percentage is adjusted to the lowest price. • Weighted average is a more common and fairer type. It takes into account both the price and the number of shares issued in the new financing round and adjusts the investor's ownership percentage based on a formula that considers these factors. <p>Both types of anti-dilution preferences are important because they protect investors from losing value in their investment if the company issues more shares in the future at a lower price. However, the weighted average is usually preferred because it is more flexible and fairer to all shareholders.</p>
<p>Exit Rights</p>	<p>Exit rights in a term sheet refer to the rights of investors to sell their shares in a company in certain situations, such as when the company is acquired or goes public. These rights are important because they give investors the ability to cash out their</p>

	<p>investment and make a profit if the company is successful. Without exit rights, investors may be stuck with their investment for a long time, even if the company is not doing well. Exit rights help make investing in a company more attractive and can help the company raise more money to grow and expand.</p>
Information and Inspection Rights	<p>Information and inspection rights in a term sheet are rights that give an investor the ability to access a company's financial records and other important information. This includes the right to review the company's financial statements, business plans, and other relevant documents. These rights are important because they allow an investor to evaluate the company's performance and make informed decisions about their investment. Without these rights, an investor would have limited access to important information, which could lead to a poor investment decision.</p>
Conditions Precedent	<p>Conditions precedent in a term sheet are things that need to happen before a deal can be finalized. Imagine you and your friend want to trade your bikes. Before you both agree to trade, you might set some conditions like "my bike needs to be checked by a mechanic" or "your bike needs to be cleaned." These conditions are important because they make sure that everything is fair and agreed upon before the trade actually happens. In a business deal, conditions precedent are important because they protect both parties and make sure that everything is clear and agreed upon before the deal is finalized.</p>
Conditions Subsequent	<p>Conditions subsequent are terms in a startup agreement that need to be met in order for the agreement to become final. For example, if a startup wants to get funding, the term sheet might say that the investor will only give the money if the startup reaches a certain milestone. This is important for startups because it helps protect both parties. The startup knows what they need to do to get the funding, and the investor knows that their money will be used for a specific purpose. It also helps prevent misunderstandings or disputes in the future.</p>