A Few Things to Know About Founders Preferred Stock

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What is Founders Preferred Stock?

Founders Preferred Stock (also called Series FF Stock or Starter Stock) is one way to facilitate liquidity for founders in connection with future equity financings while providing investors with a way to purchase preferred stock. Founders Preferred Stock carries the same rights as Common Stock and does not have any dividend or liquidation preference over Common Stock. Essentially the only difference between Founders Preferred Stock and Common Stock is that the Founders Preferred Stock has a conversion feature so that if the founders sell it to investors in connection with a future equity financing it will convert into the class of preferred stock sold in such financing. This allows the holders of Founders Preferred Stock to receive liquidity while allowing an investor to acquire Preferred Stock instead of Common Stock.

It is important to note that Founders Preferred Stock, like all two-tiered common structures, is not the norm and is somewhat atypical.

When can you issue it?

Generally, Founders Preferred Stock can only be issued at the time of formation when shares are initially issued to founders.

Can it be subject to vesting?

For tax reasons, Founders Preferred Stock must be fully vested at the time of issuance and cannot be subject to forfeiture or repurchase. Generally, this results in founders being issued a mix of Founders Preferred Stock and Common Stock with the Common Stock subject to vesting.

How does it compare to other paths to liquidity?

Setting aside the sale of a company or an IPO, a founder can receive liquidity through the sale of shares to the company, a third party, or to investors in connection with a financing (a secondary sale). A secondary sale is not always possible or desirable because it can be viewed as misaligning the founder's interests with those of the company, the other shareholders, and investors. Purchasing Common Stock may also not be desirable from an investor's perspective because it will put them at the bottom of the capital stack.

What about Founder Stock? How is this different?

As a matter of law, there is no such thing as "Founder Stock." When people refer to Founder Stock, they are generally referring to the shares of stock that founders purchase at the time of incorporation. This is almost always Common Stock issued at a very low price because the

company has just been created and in theory has very low value.

Why doesn't everyone incorporate with Founders Preferred Stock?

Founders Preferred Stock does introduce some additional complexity into a company's certificate of incorporation for an uncertain benefit. In addition, like all other two-tiered common structures (i.e. super voting Common Stock), it is not currently the norm.

For more information on Founders Preferred Stock, please contact Dan Wilcox.