Venture Capital Report

2023

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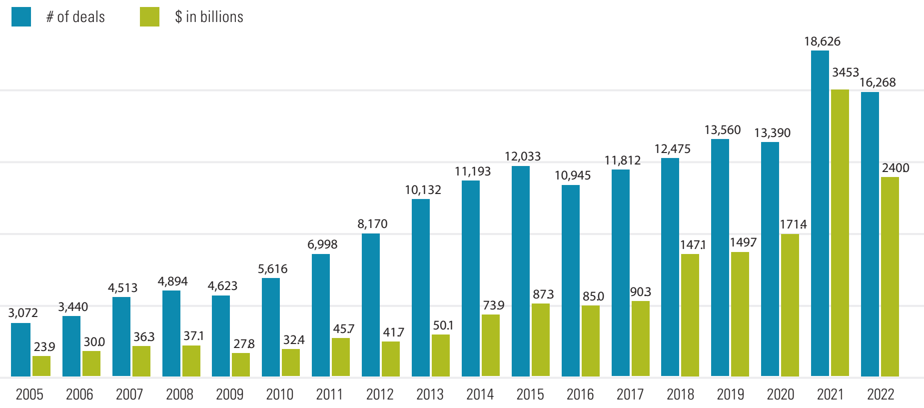
2023 Venture Capital Report – What's Inside

Venture capital financing and liquidity activity contracted in 2022 from the record-breaking levels of the prior year, in the face of declining equity markets, rising interest rates and continuing geopolitical uncertainty.

Although financing activity in 2022 was strong by historic measures, the fall-off in deal flow and valuations from the first quarter of the year to the fourth quarter points to a challenging environment in 2023.

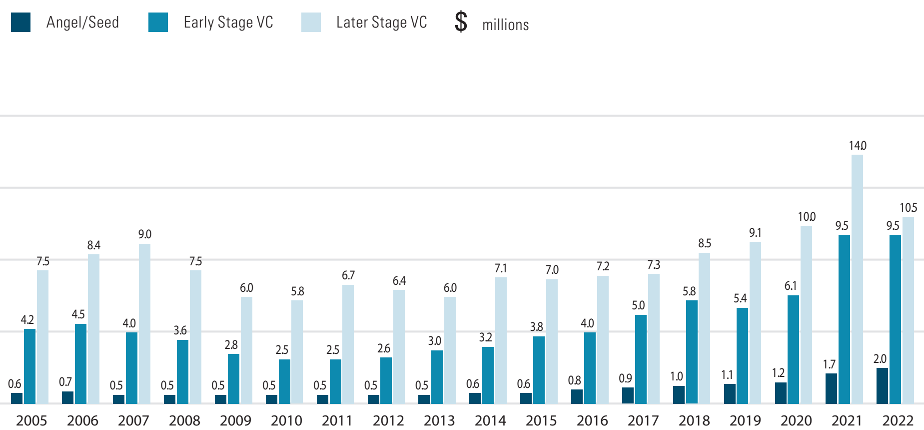
VC-backed company liquidity results were more mixed in 2022. IPOs fell to their lowest level since 2009 but the number of acquisitions of VC-backed companies reached its second-highest total on record, trailing only 2021.

US Venture Capital Financings – 2005 to 2022



Source: PitchBook

Median Size of US Venture Capital Financings – 2005 to 2022



Source: PitchBook

EQUITY FINANCING ACTIVITY

The number of reported venture capital financings decreased by 13%, from 18,626 in 2021 to 16,268 in 2022. Total reported financing proceeds dropped 30% from the record $345.3 billion set in 2021, falling to $240.0 billion. Although down from 2021, the totals for 2022 still beat the 2020 deal count by 21% and 2020 proceeds by 40%.

Overall, the median size of venture capital financings increased by 5%, from $4.0 million in 2021 to $4.2 million in 2022—the highest median since 2006, when angel and seed financings comprised a smaller portion of the market.

The median size of angel and seed financings rose by 16% year-over-year, from $1.7 million to $2.0 million, while the median size of early-stage financings remained flat. After increasing each year since 2015, the median size of later-stage financings decreased by 25%, from $14.0 million to $10.5 million.

The median financing size for life sciences companies dipped from $5.1 million in 2021 to $5.0 million in 2022—still the second-highest level since 2007. Among technology companies, the median financing size grew by 21%, from $4.1 million to $5.0 million, its highest level since 2006.

After spiking in the preceding five years, the number of large financing rounds contracted sharply in 2022. Financing rounds of $50 million or more declined by 32%, from 1,618 in 2021 to 1,097 in 2022, while $100 million-plus rounds fell by 35%, from 840 to 544. The number of financing rounds of at least $250 million posted an even sharper decline, dropping 48%, from 209 to 108, as interest in super-sized rounds by growth equity, crossover and hedge fund investors waned in the soft IPO market.

There were seven billion-dollar venture financing rounds in 2022, compared to 20 in 2021. Altos Labs, with its record-setting $3.0 billion early-stage financing, led this elite club, followed by Epic Games ($2.0 billion), SpaceX ($1.7 billion) and Gopuff ($1.5 billion). All but two of the billion-dollar rounds, including the four largest, occurred in the first half of the year.

Continuing its decade-long upward trajectory, the median pre-money valuation for all venture financings increased again, climbing 15%, from $26.0 million in 2021 to $30.0 million in 2022. The median pre-money valuation increased by 12% in angel and seed rounds, from $9.0 million to $10.0 million, and increased by 19% in early-stage rounds, from $42.0 million to $50.0 million. The median pre-money valuation in later-stage rounds—which tend to be more prone to economic uncertainty given their proximity to public exits—declined by 11%, from $90.0 million to $80.0 million.

The median pre-money valuation in the life sciences sector increased 7%, from $28.0 million in 2021 to $30.0 million in 2022. Among technology companies, the median pre-money valuation increased by a similar percentage, from $30.0 million to $32.0 million.

Angel and seed financings accounted for 40% of all venture financings in 2022 (down from 42% in 2021) and represented 9% of all venture capital financing proceeds (up from 6% in 2021). Early-stage financings accounted for 30% of all financings in 2022 (up from 29% in 2021) and 29% of all proceeds (up from 25% in 2021). Later-stage financings accounted for 31% of all financings in 2022 (up from 30% in 2021) and 62% of all proceeds (down from 69% in 2021).

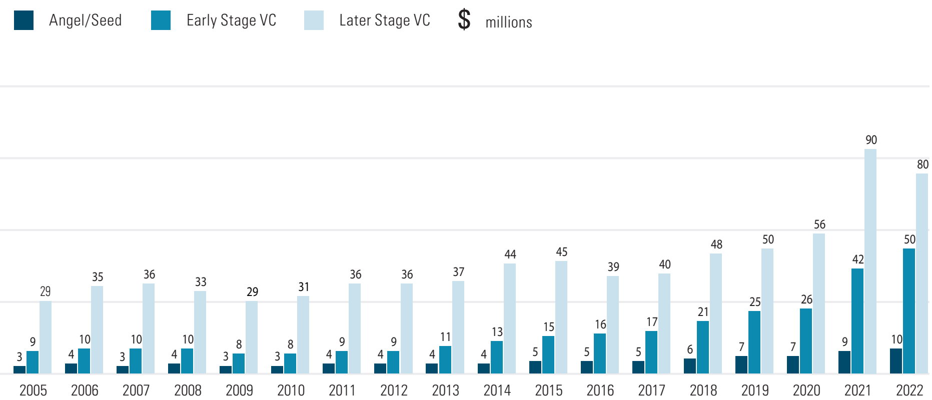
The technology sector accounted for 43% of the year's financings in both 2021 and 2022. The life sciences sector's market share decreased to 19% in 2022 from 21% in 2021. Year-over-year, the market share for consumer goods and services companies declined from 18% to 17%, while business services companies saw their market share increase from 13% to 14%.

Repeating a familiar pattern, California produced 32% of all venture financings in 2022 (5,172 financings) and 43% of the year's proceeds ($104.0 billion). New York, home to companies with 2,151 financings raising $29.1 billion in 2022, finished second in the state rankings, followed by Massachusetts (with 984 financings raising $21.2 billion). Texas (with 862 financings raising $10.1 billion), Florida (with 689 financings raising $7.1 billion) and Washington (with 547 financings raising $8.0 billion) rounded out the state rankings.

LIQUIDITY ACTIVITY

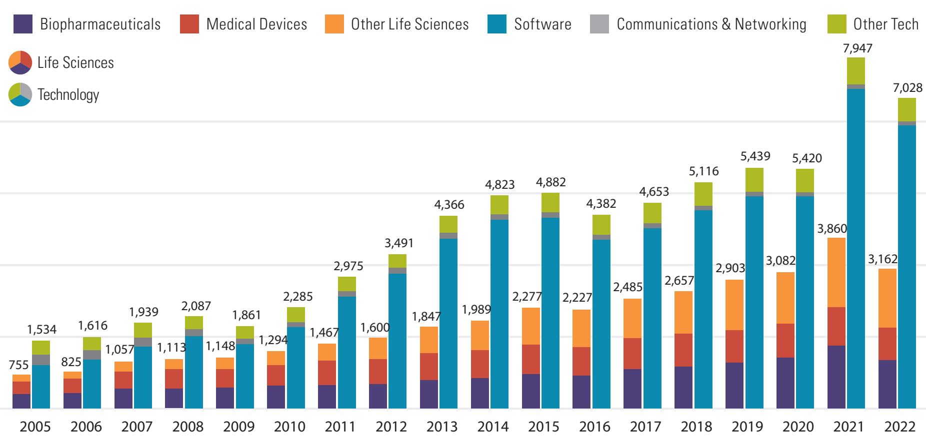
The number of US-issuer VC-backed IPOs plunged by 87%, from 157 in 2021 to 20 in 2022—the lowest annual figure since 2009. VC-backed companies accounted for 42% of all conventional IPOs by US issuers in 2022, down from 56% in 2021 and 64% in 2020. This decrease in market share from 2020 to 2021 was largely due to the large number of PE-backed IPOs in 2021, while the drop that occurred between 2021 and 2022 reflects an IPO market dominated by smaller, non–VC-backed companies.

Median Pre-Money Valuation in US Venture Capital Financings – 2005 to 2022



Source: PitchBook

US Venture Capital Financings by Industry – 2005 to 2022



Source: PitchBook

Gross IPO proceeds raised by VC-backed US issuers plummeted from $60.1 billion in 2021 to $1.6 billion in 2022. Following a year that saw 13 billion-dollar IPOs by VC-backed US issuers (up from six in both 2019 and 2020), 2022 brought no VC-backed IPOs of this size. The largest VC-backed IPO in 2022 was the $200 million offering by HilleVax, followed by the IPOs of CinCor Pharma ($194 million), Amylyx Pharmaceuticals ($190 million), Third Harmonic Bio ($185 million) and Prime Medicine ($175 million).

The median offering size for US VC-backed IPOs fell by 70%, from $176.0 million in 2021 to $52.3 million in 2022.

In 2022, life sciences companies accounted for 56% of all VC-backed IPOs, equal to their market share in 2021 but below the average of 62% that prevailed over the five-year period from 2016 to 2020. The VC-backed IPO market share for technology companies was 30% in 2022, down from 38% in 2021 and below their 35% share of the VC-backed IPO market between 2016 and 2020.

The median time from initial funding to IPO decreased from 5.8 years in 2021 to 5.1 years in 2022—the second-lowest figure since 2008, reflecting the influx of less-seasoned companies into the IPO market.

The median amount raised prior to an IPO dropped 55%, from $160.5 million in 2021 to $72.5 million in 2022, while the median pre-IPO valuation fell by 77%, from $710.0 million to $160.7 million. As a result, the ratio of pre-IPO valuation to the median amount raised prior to an IPO declined from 4.4:1 in 2021 to 2.2:1 in 2021—the lowest level in more than 20 years (a higher ratio means better returns to pre-IPO investors).

VC-backed US issuer IPO companies ended 2022 down a median of 41% from their offering price, in sharp contrast to the median loss of 11% in 2021 and the median gain of 67% in the prior year. At the end of 2022, 37% of the year's VC-backed IPO companies were trading above their offering price, up from the 27% in 2021 but below the average of 63% that prevailed over the five-year period from 2016 to 2020.

The number of reported acquisitions of VC-backed companies decreased by 26%, from 1,594 in 2021 to 1,174 in 2022. With softening M&A valuations, total reported acquisition proceeds fell by 44%, from $112.5 billion to $63.2 billion.

The median acquisition price decreased by 15%, from $66.9 million in 2021 to $57.0 million in 2022—the lowest annual figure since 2017. The median time from initial funding to acquisition in 2022 held steady at 5.1 years, in line with the previous two years.

The median amount raised prior to acquisition declined by 11%, from $9.1 million in 2021 to $8.1 million in 2022.

The ratio of median acquisition price to median amount raised prior to acquisition dipped from 7.4:1 in 2021 to 7.1:1 in 2022 (a higher ratio means higher returns to pre-acquisition investors). Despite this decrease, the 2022 figure of 7.1:1 was the fourth-highest ratio since 2000, behind only the ratios for 2016 (8.8:1), 2019 (8.5:1) and 2021 (7.4:1). The historically high ratio in recent years reflects a combination of significantly higher acquisition prices and lower levels of pre-acquisition investments.

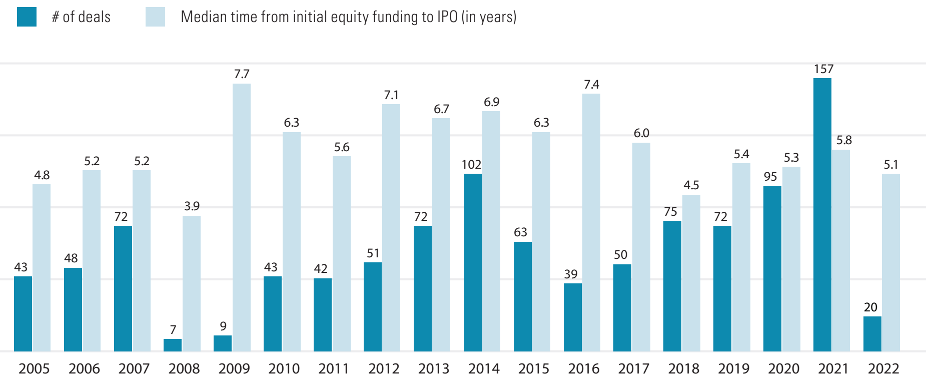
There were 21 VC-backed company acquisitions of at least $500 million in 2022, representing declines of 64% from the 58 in 2021 and 30% from the annual average of 30 that prevailed during the five-year period from 2016 to 2020.

The year also produced six billion-dollar acquisitions of VC-backed companies, well below the average of 21 over the last three years and the lowest annual tally since 2013. The largest deal of 2022 was the $3.0 billion acquisition of Affinivax by GlaxoSmithKline, followed by the $2.1 billion acquisition of Deliverr by Shopify, the $1.9 billion acquisition of Pensando Systems by Advanced Micro Devices and the $1.0 billion acquisition of MoPub by AppLovin.

Based on the valuations achieved in company sales and IPOs compared to the financing amounts required to achieve each type of liquidity event, 2022 marked the tenth consecutive year in which returns to venture capital investors were higher in M&A transactions than in IPOs. In 2022, the median time of 5.1 years from initial funding to acquisition was equal to the median time from initial funding to IPO, although in recent years liquidity has typically occurred more quickly from acquisitions. This pattern, combined with the tendency of M&A transactions to yield the bulk of the purchase price in cash at closing—whereas IPOs generally involve a post-IPO lockup period and market uncertainty as to the timing and prices of subsequent stock sales—makes it easy to see why investors often prefer a company sale to an IPO.

With IPO numbers plummeting in 2022 while company sales remained plentiful by historic standards, the ratio of M&A transactions to IPOs for VC-backed companies soared from 10.2:1 in 2021 to 58.3:1 in 2022—the highest ratio since the 58.7:1 in 2008 during the Great Recession.

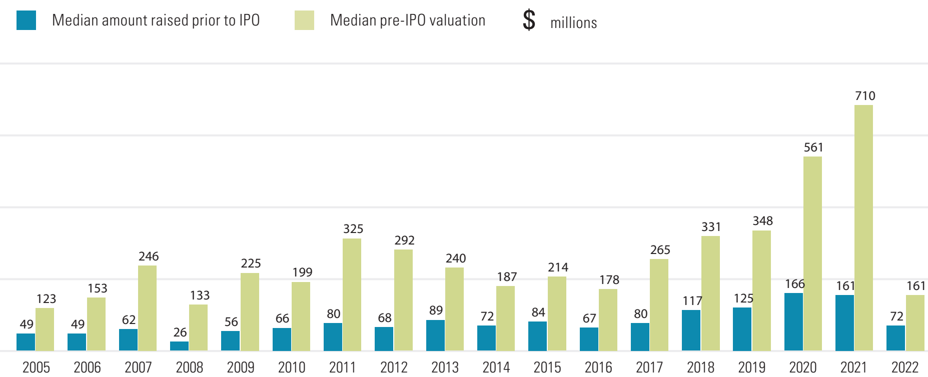
Venture Capital–Backed IPOs and Median Time to IPO – 2005 to 2022



Source: SEC filings and PitchBook

The above chart is based on US IPOs by VC-backed US issuers.

Median Amount Raised Prior to IPO and Median Pre-IPO Valuation – 2005 to 2022



Source: PitchBook

OUTLOOK

The stunning March 2023 collapse of Silicon Valley Bank—the dominant banking player in the venture capital ecosystem—and the fallout among other financial institutions is likely to have a significant effect on VC-backed companies and venture capital financing and liquidity activity. Results over the coming year will also depend on a variety of other factors, including the following:

— ***Financing Activity:*** Venture capital fundraising in 2022 surpassed the record high set in 2021, increasing by 6%, from $154.1 billion to $162.6 billion. The portion of the 2022 fundraising total attributable to commitments made before the economic slowdown became apparent is hard to discern. Heading into 2023, macroeconomic challenges appear likely to tamp down valuations, especially in late-stage deals, and startups will be incented to delay capital raises if terms are unfavorable. The slowdown in financing activity and contraction in valuations that became evident in the second half of 2022 has not yet shown signs of reversing.

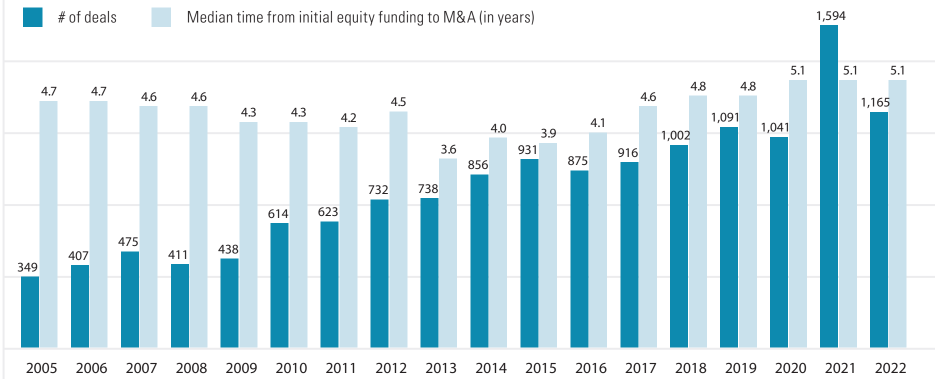
— ***Attractive Sectors:*** While many aspects of consumer behavior have reverted to pre-pandemic patterns, companies capitalizing on the broad digital transformation of business processes—including changes driven by the use of artificial intelligence—should continue to be attractive financing candidates. Persistent labor shortages should boost opportunities for companies that leverage robotics, automation, machine learning and voice technology. Opportunities also exist for companies transforming the broader healthcare industry. Innovative life sciences companies, including those in the fields of cell therapy, gene therapy, precision medicine and machine learning–enabled drug discovery, should continue to appeal to investors. Agtech and climate tech—particularly those companies aiding the economic transition away from fossil fuels—are among the other sectors that are likely to garner investor interest.

— ***IPOs:*** The IPO market had few bright spots for VC-backed companies in 2022 and the current macroeconomic climate provides little hope for a quick rebound. The continuing ability of some VC-backed companies, especially in the technology industry, to raise "IPO-sized" private rounds can extend financing runways—sometimes indefinitely—but companies needing a capital infusion in the face of an inhospitable IPO market may find private financing terms less favorable than those available in recent years.

— ***Acquisitions:*** M&A activity was remarkably resilient in 2022. The continued rise in interest rates and the resulting increase in the cost of capital is likely to temper acquisition activity by financial buyers, absent a reduction in target valuations. Conversely, the tepid economic outlook is likely to heighten companies' interest in strategic acquisitions to gain market share or to accelerate the adoption of new technologies that improve efficiency and reduce costs. As a result, strategic acquisitions should help offset a broader decline in M&A activity in the coming year.

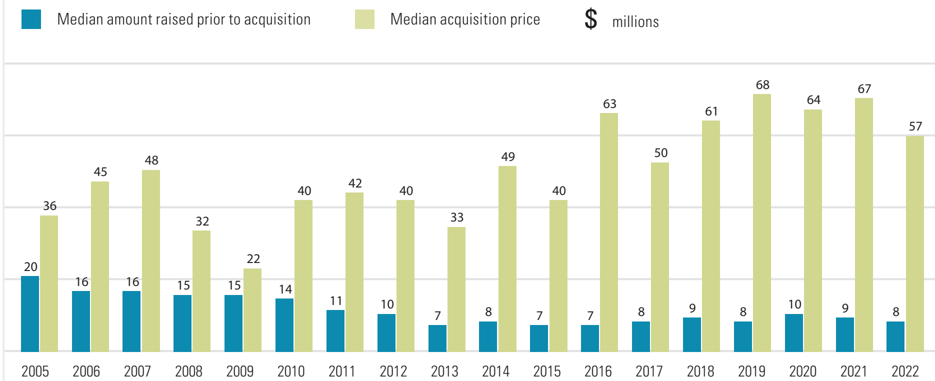
— ***Impact of Reverse Mergers:*** Despite retrenchment of the SPAC IPO market in 2022, the year ended with 386 SPACs seeking business combinations, many of which face deadlines to complete a business combination or return funds to investors. In these circumstances, some VC-backed companies may find a business combination with a SPAC a tempting alternative to a traditional IPO. Other VC-backed companies may elect to pursue reverse mergers with publicly held life sciences companies whose clinical research programs have suffered serious setbacks or failures. ■

Acquisitions of US Venture-Backed Companies and Median Time to M&A – 2005 to 2022



Source: PitchBook

Median Amount Raised Prior to Acquisition and Median Acquisition Price – 2005 to 2022



Source: PitchBook

CALIFORNIA

California-based companies reported 5,172 venture capital financings in 2022, 17% below the 2021 tally of 6,258. California was responsible for 32% of all US financing transactions in 2022, down from 34% in each of the prior two years.

Total reported proceeds declined 36%, from $162.8 billion in 2021 to $104.0 billion in 2022, partly due to a decrease in very large financings. California's share of all financing proceeds nationwide dipped from 47% to 43%.

The number of rounds raising $100 million or more fell by 36%, from 404 to 258, while the number of rounds of $250 million or more dropped by 55%, from 114 to 51 (each metric equal to 47% of the US total in 2022).

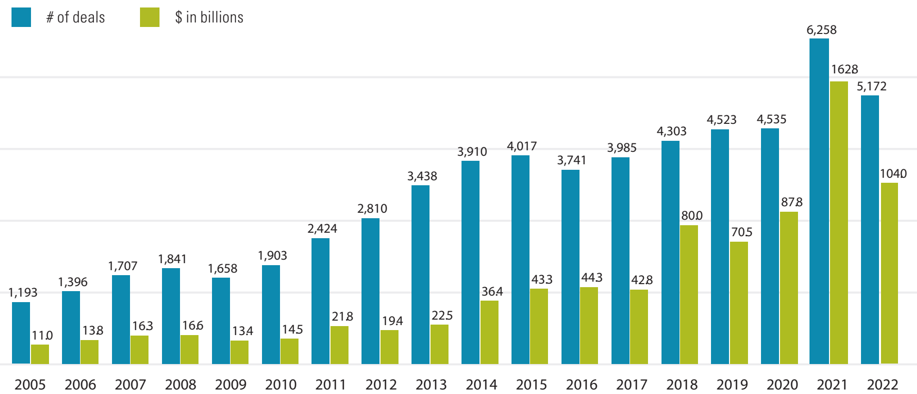
Technology was the largest sector in the state, producing 49% of all California financings in 2022, followed by consumer goods and services and life sciences (each with 16%) and business services (13%).

After increasing for five consecutive years, the number of IPOs by California-based VC-backed companies plunged from 69 in 2021 to six in 2022. The state's largest VC-backed IPO of 2022, by AN2 Therapeutic ($69.0 million), was only the tenth-largest US-issuer VC-backed IPO of the year. In 2021, California was home to six of the ten largest US-issuer VC-backed IPOs.

The number of reported acquisitions of California VC-backed companies decreased by 30%, from 575 in 2021 to 400 in 2022. The state's largest deals were the $2.1 billion acquisition of Deliverr by Shopify, the $1.9 billion acquisition of Pensando Systems by Advanced Micro Devices, and the $1.0 billion acquisition of MoPub by AppLovin.

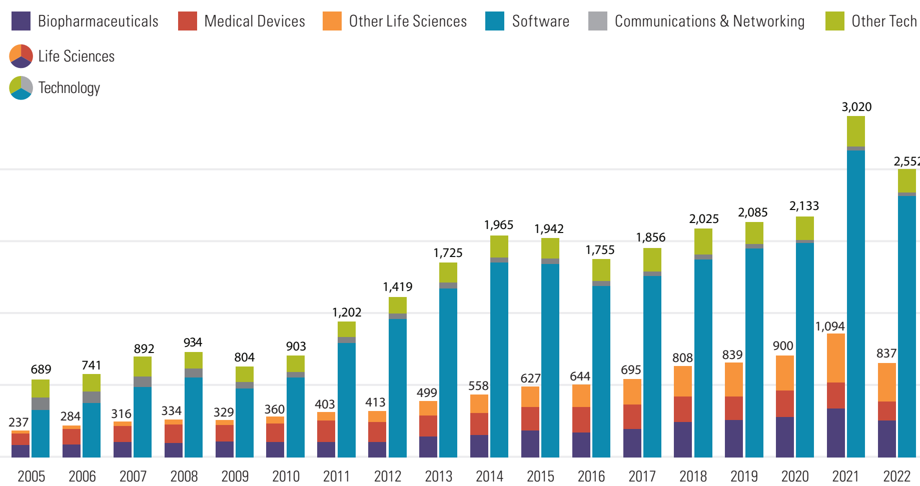
California will undoubtedly maintain its venture capital leadership in the coming year. The extent to which financing and liquidity activity rebounds will depend on macroeconomic and IPO market conditions and the willingness of strategic buyers to pay attractive prices, among other factors.

California Venture Capital Financings – 2005 to 2022



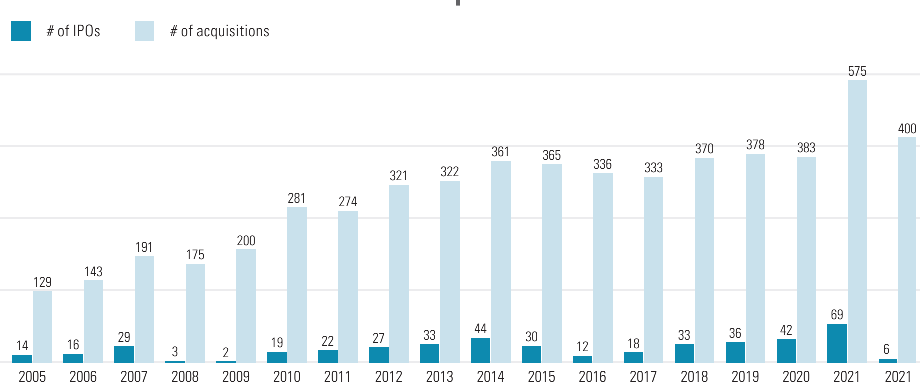
Source: PitchBook

California Venture Capital Financings by Selected Industry – 2005 to 2022



Source: PitchBook

California Venture-Backed IPOs and Acquisitions – 2005 to 2022



Source: SEC filings and PitchBook

MID-ATLANTIC

The number of reported venture capital financings in the mid-Atlantic region of Virginia, Maryland, North Carolina, Delaware and the District of Columbia declined by 9%, from 1,448 in 2021 to 1,319 in 2022.

Total reported proceeds in the mid-Atlantic region decreased by 15%, from $14.6 billion to $12.5 billion. The number of mid-Atlantic rounds raising $100 million or more fell from 31 in 2021 to 21 in 2022.

North Carolina was the mid-Atlantic region's top performer for the third consecutive year, with 302 financings raising $4.4 billion, led by Epic Games' $2.0 billion financing round.

Technology companies accounted for 45% of all mid-Atlantic financings in 2022—extending the sector's longstanding leadership in the region—followed by life sciences (20%), consumer goods and services (15%), and business services (14%).

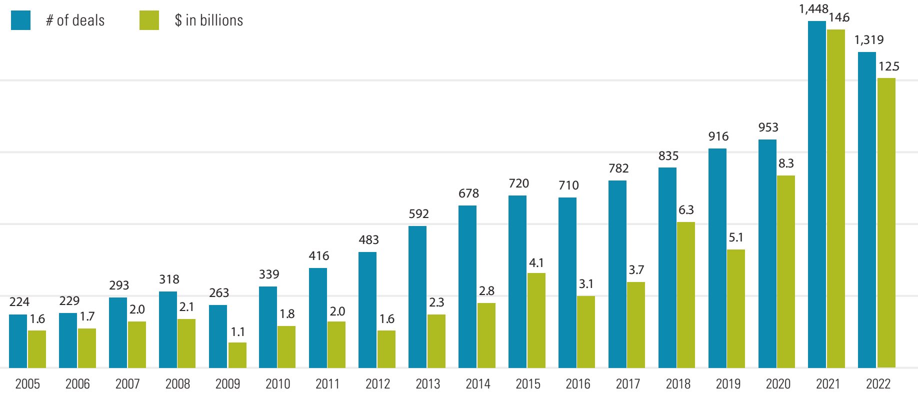
The mid-Atlantic region generated a single VC-backed IPO in 2022, down from eight in 2021 and three in both 2019 and 2020. The 2022 tally was the mid-Atlantic's smallest since 2011, when the region also produced a solitary IPO. The lone 2022 IPO, by Maryland-based Arcellx, raised $123.8 million.

The number of reported acquisitions of mid-Atlantic VC-backed companies decreased by 22%, from 93 in 2021 to 73 to 2022. Virginia generated 22 deals, while Maryland produced 19 deals and North Carolina 17 deals.

The region's largest M&A transaction of the year was the $575 million acquisition of Personal Genome Diagnostics by Labcorp, followed by the $525 million acquisition of Axios Media by Cox Enterprises and the $470 million acquisition of ReKTGlobal by Infinite Reality.

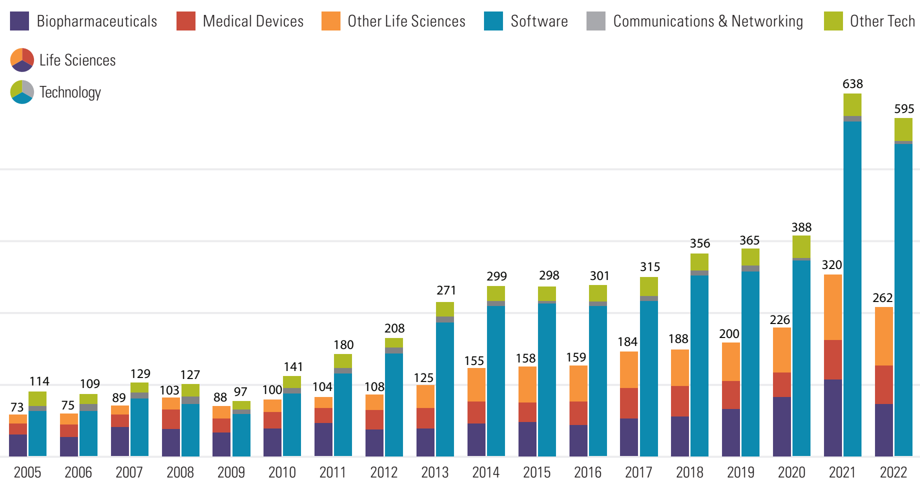
With a strong venture capital ecosystem, the mid-Atlantic region should continue to generate promising startups in the coming year, although the region's ability to match or exceed its financing and liquidity tallies of 2022 will depend on market conditions and other factors.

Mid-Atlantic Venture Capital Financings – 2005 to 2022



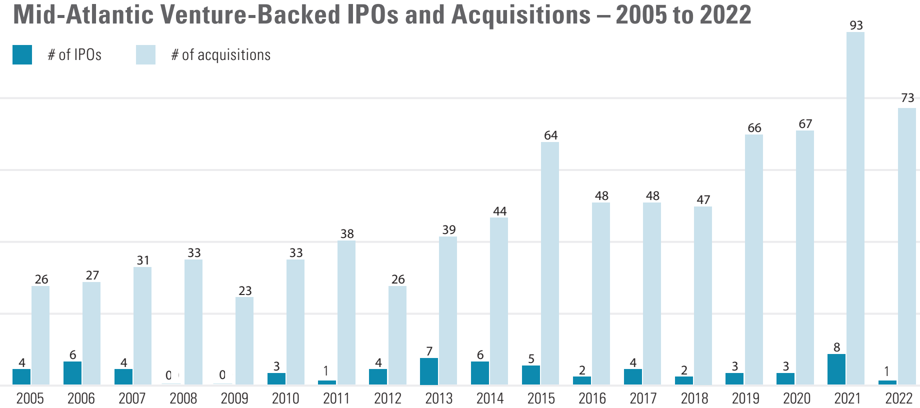
Source: PitchBook

Mid-Atlantic Venture Capital Financings by Selected Industry – 2005 to 2022



Source: PitchBook

Mid-Atlantic Venture-Backed IPOs and Acquisitions – 2005 to 2022



Source: SEC filings and PitchBook

NEW ENGLAND

New England companies reported 1,306 venture capital financings in 2022, a decrease of 14% from the 1,518 financings in 2021. Total reported proceeds were $24.2 billion, down 36% from the $38.0 billion in the prior year.

Massachusetts, the perennial leader in New England and the nation's third-largest source of VC financings, produced 984 financings and $21.2 billion in proceeds.

The number of rounds raising $100 million or more declined by one-third, from 100 in 2021 to 67 in 2022, while the number of rounds raising $250 million or more fell by 54%, from 26 to 12. The largest rounds in 2022 came from Form Energy ($450 million), Circle ($403 million) and Beta Technologies ($375 million).

The life sciences sector accounted for 36% of New England venture capital financings in 2022, followed by technology (30%), consumer goods and services (15%), and business services (12%).

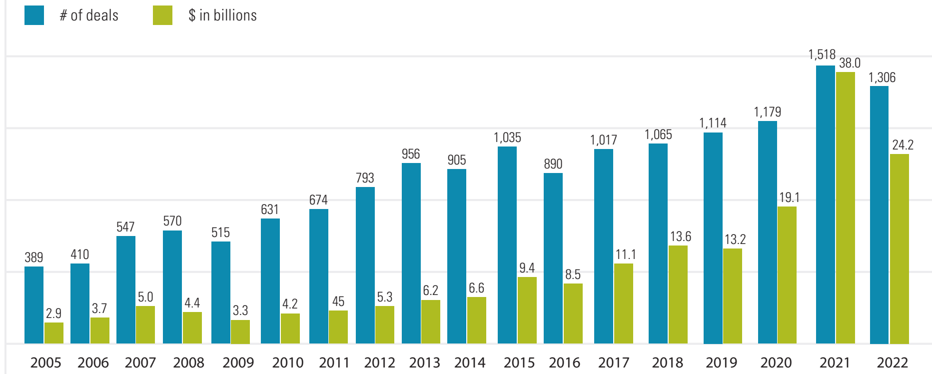
The number of VC-backed IPOs by New England–based companies plummeted from 30 in 2021 to eight in 2022—the lowest annual tally since 2012, when there were seven. All of the region's VC-backed IPOs were by life sciences companies based in Massachusetts. The largest offerings were by HilleVax ($200 million), CinCor Pharma ($194 million) and Amylyx Pharmaceuticals ($190 million).

The number of reported acquisitions of VC-backed companies in New England dropped by 30%, from 149 in 2021 to 105 in 2022. Despite the decline, the 2022 figure was the second-highest total on record. Massachusetts produced 81 of the region's deals in 2022, down 34% from the 123 acquisitions in the prior year.

The region's largest M&A transactions were the $3.0 billion acquisition of Affinivax by GlaxoSmithKline and the $675 million acquisition of Affera by Medtronic.

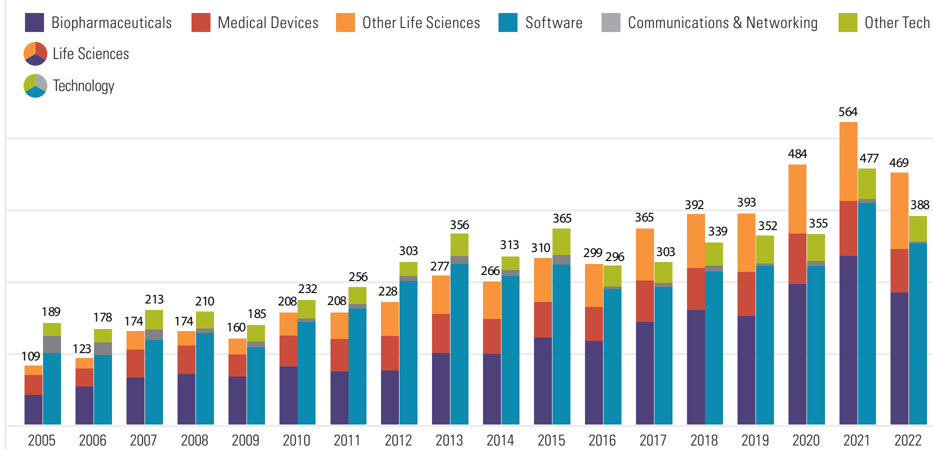
With its concentration of world-renowned universities and research institutions, New England—and Massachusetts in particular—should remain a hub of financing and liquidity activity during the coming year, although deal flow in the region will depend on market conditions and other factors.

New England Venture Capital Financings – 2005 to 2022



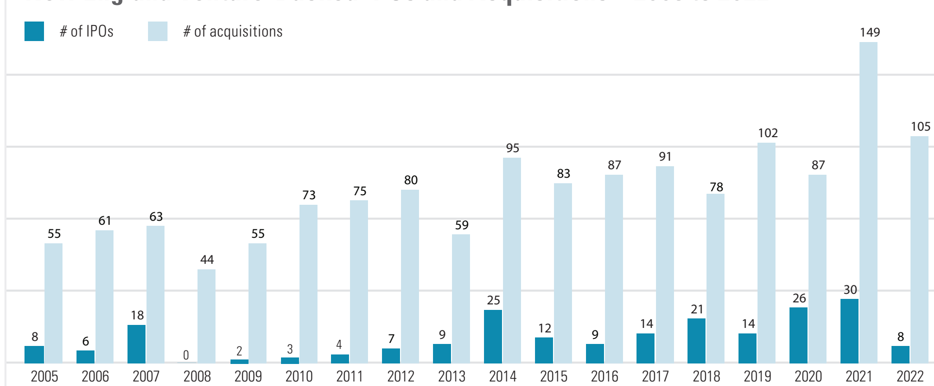
Source: PitchBook

New England Venture Capital Financings by Selected Industry – 2005 to 2022



Source: PitchBook

New England Venture-Backed IPOs and Acquisitions – 2005 to 2022



Source: SEC filings and PitchBook

TRI-STATE

The number of reported venture capital financings in the tri-state region of New York, New Jersey and Pennsylvania decreased by 13%, from 3,196 in 2021 to 2,792 in 2022, while total reported proceeds declined 41%, from $61.2 billion to $36.1 billion.

New York, the nation's second-largest source of VC financings, led the region with 2,151 financings and $29.1 billion in proceeds.

The number of rounds raising $100 million or more fell by 47%, from 154 in 2021 to 81 in 2022, while the number of rounds of $250 million or more contracted from 37 to 14. The region's largest financings came from Gopuff ($1.5 billion, in the form of a convertible note), Ramp ($748 million) and Fireblocks ($550 million).

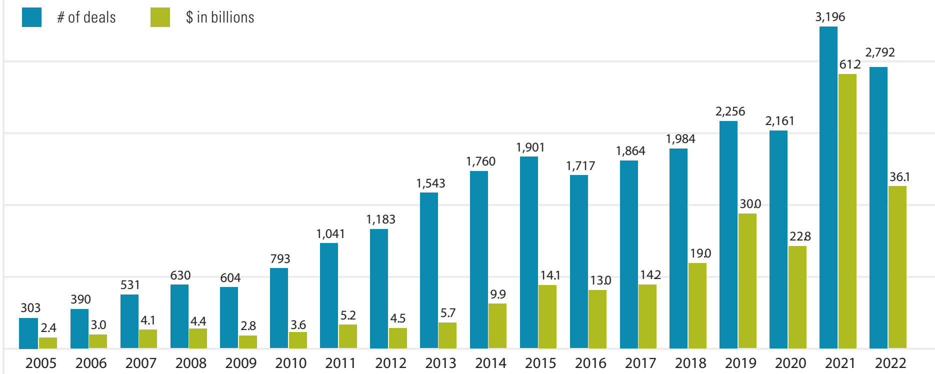
Technology companies accounted for 45% of the tri-state region's VC financings in 2022, followed by consumer goods and services (19%), life sciences (18%) and business services (12%).

In 2022, the region saw its lowest number of VC-backed IPOs since 2011, producing only two, down from 20 in 2021. The region's pair of IPOs came from New Jersey–based Nuvectis Pharma ($16 million) and Pennsylvania-based Lipella Pharmaceuticals ($7 million).

The number of reported acquisitions of VC-backed companies in the tri-state region decreased by 30%, from 277 in 2021 to 194 in 2022. New York generated 149 deals, followed by Pennsylvania with 24 and New Jersey with 21. The largest 2022 deals were the $1.0 billion acquisition of Xandr by Microsoft, the $500 million acquisition of Siemplify by Google, and the $500 million acquisition of Flow Commerce by Global-e.

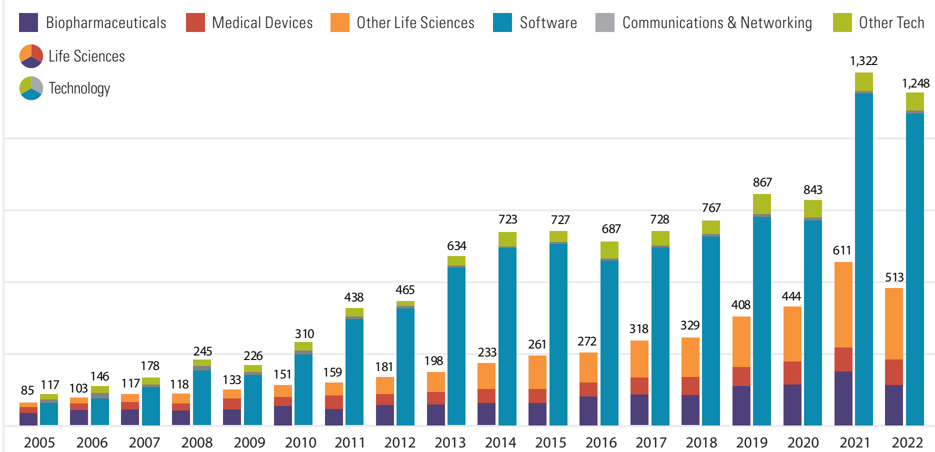
Due to its strength across a broad array of industry sectors, the tri-state region should continue to produce large numbers of financings and liquidity events. The level of deal activity in the coming year will depend on macroeconomic and market conditions, among other factors. ■

Tri-State Venture Capital Financings – 2005 to 2022



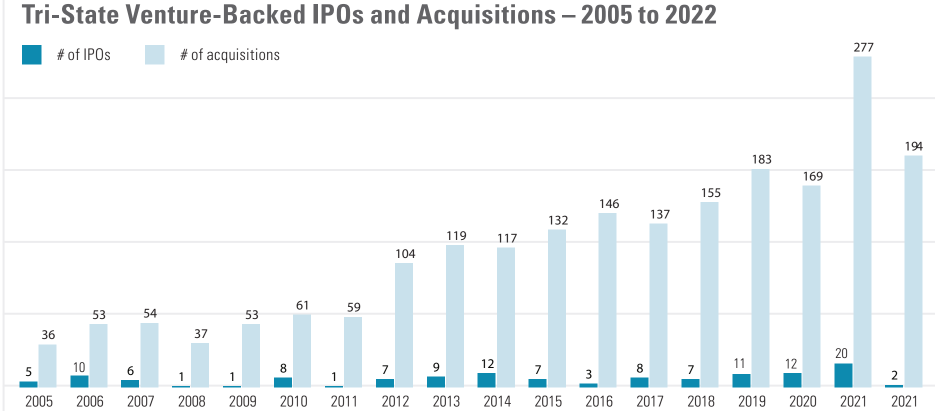
Source: PitchBook

Tri-State Venture Capital Financings by Selected Industry – 2005 to 2022



Source: PitchBook

Tri-State Venture-Backed IPOs and Acquisitions – 2005 to 2022



Source: SEC filings and PitchBook

Counsel of Choice for Venture Capital Financings

Serving market leaders in technology, life sciences, financial services and a wide variety of other industries

GiveCampus	$50,000,000	*First Round*	July 2022
gentibio	$157,000,000	*First Round*	August 2021
atom computing	$60,000,000	*Second Round*	December 2021
atVenu	$30,000,000	*Third Round*	August 2022
IMMUTA	$100,000,000	*Late Stage*	June 2022
X-BOW	$27,000,000	*First Round*	April 2022
ORNA	$221,000,000	*Second Round*	August 2022
Dedrone	$60,500,000	*Third Round*	December 2021 and July 2022
BandLab	$53,000,000	*Second Round*	December 2021
Rectify Pharma	$100,000,000	*First Round*	August 2021
Infinium	$69,000,000	*Second Round*	September 2021
fw	$72,000,000	*Fourth Round*	February and May 2022
Workit Health	$118,000,000	*Third Round*	September 2021
respira	$25,900,000	*First Round*	November 2022
DriveWealth	$450,000,000	*Fourth Round*	September 2021
tenderly	$40,000,000	*Second Round*	December 2021
Sonde	$19,250,000	*Second Round*	May 2022
introhive	$100,000,000	*Third Round*	June 2021
butlr	$20,000,000	*First Round*	May 2022
Flare Therapeutics	$123,000,000	*Second Round*	February 2023
WorkRamp	$40,000,000	*Third Round*	March 2022
Verana Networks	$28,000,000	*Second Round*	February 2022
Owl Labs	$25,000,000	*Fourth Round*	May 2022
Phantom Neuro	$6,000,000	*Seed Round*	September 2022
Alethea	$10,000,000	*First Round*	October 2022
truera	$25,000,000	*Second Round*	March 2022
Preveil	$20,000,000	*Third Round*	June 2022
RightHand Robotics	$66,000,000	*Third Round*	February 2022
Equii	$6,000,000	*Seed Round*	September 2022
Auron Therapeutics	$48,000,000	*Second Round*	July 2022
LogRocket	$25,000,000	*Third Round*	March 2022
Verdox	$80,000,000	*First Round*	December 2021
Fervo Energy	$138,000,000	*Third Round*	August 2022
thirdweb	$24,000,000	*First Round*	July 2022

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Beginning in January 2024, many companies will be required to report to the US government certain information about their beneficial owners and others involved in the establishment and control of the company. These requirements flow from the Corporate Transparency Act (CTA), with which preexisting companies will have until January 2025 to come into compliance.

WHAT'S THE CTA?

Enacted on January 1, 2021, the CTA marks a significant step in updating the US anti–money laundering framework. At its core, the CTA sets forth beneficial ownership reporting requirements for a wide swath of private companies established in the United States and directs the Financial Crimes Enforcement Network (FinCEN) of the Department of Treasury to create and maintain a secure, centralized, non-public database of beneficial ownership information (BOI) with the goal of aiding law enforcement efforts to counter illicit finance and protect national security.

Although FinCEN plans to issue three separate final rules to fully implement the CTA—one setting forth BOI reporting provisions (the Reporting Rule), one governing access to and disclosure of BOI (the Access Rule), and one revising FinCEN's existing customer due diligence requirements (the CDD Rule)—to date only the Reporting Rule has been finalized.

WHAT'S NEW ABOUT BOI REPORTING?

Previously, financial institutions were required to obtain personal identifying information (PII) about the beneficial owners of legal entity customers directly from the legal entity customers themselves. Under the CTA, millions of domestic and foreign businesses operating in the United States will now be required to disclose PII *to FinCEN* about their beneficial owners, senior officers and other individuals who exercise control over the business.

FinCEN estimates that more than 32 million entities will be required to file initial BOI reports in the first year, with approximately 5 million initial and 14 million updated BOI reports to be filed every year thereafter.

WHO'S REQUIRED TO FILE A BOI REPORT—AND WHO'S NOT?

The Reporting Rule identifies two types of "reporting companies." In general, a *domestic reporting company* is a non-exempt corporation, limited liability company or other entity created by the filing of a document with a state governmental official. A *foreign reporting company* is a similar entity formed under the law of a foreign country and registered to do business in the United States.

NO EXEMPTION APPLIES TO MY BUSINESS. WHAT EXACTLY DO I NEED TO REPORT?

If yours is one of the millions of companies not eligible for an exemption, you must report detailed information identifying your entity, all of the company's beneficial owners, and all company applicants.

— A *beneficial owner* is a natural person who either owns or controls at least 25% of the ownership interests of the reporting entity or exercises "substantial control" (defined broadly) over the reporting entity. For example, indicia of substantial control may include an individual's service as a senior officer of the reporting company; authority over the appointment or removal of senior officers or a majority of the board of directors or similar body; and direction or determination of—or substantial influence over—important decisions made by the reporting company.

— A *company applicant* is an individual who files the documents that form the company (for domestic reporting entities) or who files the document that registers the entity to conduct business in the United States (for foreign reporting entities).

For each beneficial owner and company applicant, reporting companies must disclose to FinCEN the individual's full legal name, date of birth, current residential or business street address, and a unique identifying number from an official document, such as a passport or a FinCEN Identifier (available upon request). Entities formed or registered before the requirements go into effect on January 1, 2024, are *not* required to report information on company applicants (only beneficial owners).

EXEMPT ENTITIES

The Reporting Rule exempts 23 types of entities from the definition of "reporting company." Entities exempted from the BOI reporting requirement include public companies, tax-exempt entities, registered investment companies and advisers, venture capital fund advisers, pooled investment vehicles and large operating companies.

Of particular interest, the exemption for "large operating companies" is available to any entity that:

— employs more than 20 employees in the United States on a full-time basis;

— filed a federal income tax return in the previous year showing greater than $5 million in gross receipts or aggregated sales from US operations; and

— has an operating presence at a physical office located in the United States.

Many early-stage companies and many life sciences companies will not qualify for this exemption and thus will be subject to BOI reporting.

WHAT HAPPENS IF I'M REQUIRED TO REPORT BUT DON'T?

Violations of the CTA, including failure to comply with the BOI reporting requirements, can result in civil penalties of up to $500 per day or criminal fines of up to $10,000 and/or a maximum of two years' imprisonment.

WHAT'S NEXT?

The BOI reporting requirements will become effective on January 1, 2024. FinCEN is in the process of drafting the BOI report forms which will then be published in the Federal Register for public comment. FinCEN has published a proposed Access Rule (for which the public comment period recently ended) and is expected to finalize it in the near term. FinCEN is required to finalize the CDD Rule by January 1, 2025, but this rulemaking process has not yet begun. ■

Over the past few years, a growing number of states and cities have passed laws requiring employers to include wage ranges and other benefit-related information in job postings. These laws are part of an ongoing effort by lawmakers to increase transparency around wages as a means to reduce pay gaps, particularly for women, people of color and LGBTQ+ workers. Employers should familiarize themselves with the new salary disclosure laws and adapt their hiring practices to best position their business for success while complying with applicable requirements.

CALIFORNIA

As of January 1, 2023, employers with 15 or more employees (and at least one employee in California) must provide the anticipated pay scale—the salary or hourly wage that the employer reasonably expects to pay for a position—in new job advertisements. This requirement applies even where an employer engages a third-party recruiter to post job openings. The pay disclosure requirement applies for any job that could be filled in California, including fully remote positions. The pay scale must be included within the job posting itself; hyperlinks or QR codes which bring applicants to a different webpage with wage information are not permitted.

NEW YORK CITY/NEW YORK STATE

Similar to California, New York City's pay transparency law (which took effect on November 1, 2022) requires employers to post the minimum and maximum annual salary or hourly wage in any job advertisement. The law covers all employers with four or more employees—as long as at least one employee works in NYC—and applies to any position that can be performed in NYC, including positions that can be performed remotely. The law also explicitly applies to postings seeking independent contractors.

Following NYC's lead, New York has enacted a statewide pay transparency law that will take effect September 17, 2023, and will also apply to employers with at least four employees. The statewide law goes even further than the NYC ordinance, requiring that employers also include a job description in the advertisement (if a job description exists) and mandating that employers keep and maintain records related to compliance with the law, including the history of compensation ranges for each position and the corresponding job descriptions.

COLORADO

Colorado, the state that passed the first pay transparency law in 2019, has the most robust job posting requirements. Any employer with at least one employee in Colorado must disclose in each job posting the range of salary or hourly wages, along with a general description of all benefits and other compensation for the position. This means the posting must state whether the applicant would be entitled to bonus and equity compensation and must list all benefits for which the person would be eligible, including healthcare benefits, retirement benefits and paid days off. Similar to the laws in California and New York, the pay disclosure requirement applies to any position that could be performed in Colorado, including fully remote positions.

WASHINGTON

Effective January 1, 2023, Washington employers with at least 15 employees (including at least one based in Washington) must disclose the wage scale or salary range for each job opening, along with a list of all specific benefits (such as medical, dental, vision and basic life insurance), the number of available vacation or PTO days, and all other compensation for the position. Like in Colorado, the "other compensation" requirement can be satisfied by listing the types of additional compensation for which the applicant would be eligible (for example, bonuses, commissions and stock options) without providing specific dollar amounts.

OTHER JURISDICTIONS

Other jurisdictions, including Connecticut, Maryland, Nevada and Rhode Island, have adopted pay transparency laws that do not mandate anticipated salary ranges to be included in job advertisements but do require other pay disclosures, such as wage information upon an applicant's request or prior to providing a job offer.

NEXT STEPS

The patchwork of pay transparency laws across jurisdictions can pose an administrative challenge for all employers, from small startups to large public companies, especially for employers that operate in multiple states or have embraced a virtual workplace model.

Before posting a job advertisement, an employer should assess its hiring strategy and determine which laws apply. Under most pay transparency laws, an employer may find itself subject to a jurisdiction's pay transparency law as soon as it hires one remote employee in that jurisdiction. Employers cannot evade job posting rules by stating in the advertisement that residents of specified states are ineligible to apply for remote positions—the guidance from both Colorado and Washington specifically prohibits this tactic, and other jurisdictions are likely to follow suit.

Employers that are (or expect to become) subject to pay transparency laws should be thoughtful about how best to comply. Before posting a job advertisement, employers may want to consider how the anticipated salary range for the open position compares to the range for existing positions. For example, if the wage range posted for a new opening exceeds the pay ranges for similar positions filled by current employees, it may be prudent to evaluate and potentially adjust the salaries of those employees before advertising the new position. Additionally, to manage applicant expectations, it is advisable to state in job postings that the specific salary offered within the posted range depends on various factors, including the applicant's experience and qualifications.

The pay disclosure trend appears to be gaining steam, and additional states and localities are expected to pass similar laws. Moreover, as pay transparency in job advertising becomes more prevalent, applicants may come to demand such disclosures even in the absence of specific legal requirements. Employers should take steps now to prepare themselves for this reality. ■

Perhaps the most vexing part of the IPO journey for management is the "quiet period," during which a company—against all natural instincts—must rein in its publicity activities. Lawyers lecture their clients about the rules, underwriters fret over the consequences of a misstep, and companies chafe at the restrictions—which begin long before the IPO is completed.

WHAT'S THE QUIET PERIOD?

Section 5 of the Securities Act of 1933 is generally intended to ensure that offers are not made prior to the filing of a registration statement and that sales of securities are made only pursuant to a prospectus that meets all SEC disclosure requirements. The SEC has broadly construed the term "offer" to include many types of public communications that have the intent or effect of promoting a company to prospective investors or otherwise generating interest in the company or its securities. Section 5 therefore limits a company's ability to publicly release information about itself or otherwise engage in promotional activities—for example, through press releases, media interviews, website postings or social media—even if the communications do not specifically reference the company's contemplated IPO.

Section 5 has the effect of imposing a quiet period on a company throughout the IPO process. The quiet period ends 25 days after the IPO offering date. The quiet period is generally considered to commence not later than the organizational meeting and probably as early as the company's selection of the lead managing underwriters.

"TEST-THE-WATERS" COMMUNICATIONS

A company going public may engage in oral or written "test-the-waters" communications with eligible institutional investors to determine their interest in a contemplated securities offering. "Test-the-waters" communications are permitted at any time during the IPO process. Originally available only to emerging growth companies (EGCs) under the JOBS Act, SEC rules now permit any company—regardless of EGC status—to engage in "test-the-waters" communications.

The quiet period is divided into three parts, with different restrictions applicable to each. Notwithstanding these restrictions, oral and written "test-the-waters" communications with eligible institutional investors are permitted at any time during the IPO process.

Pre-Filing Period

Prior to publicly filing the Form S-1 registration statement, a company is prohibited from making any offers—whether oral or written—to sell its securities. The submission of a draft Form S-1 to the SEC does not constitute public filing of a Form S-1 for this purpose.

Waiting Period

During the period of time between the Form S-1's filing and its effectiveness (which usually occurs shortly before pricing), a company cannot effect any sales, but it can make:

- oral offers (such as statements made during road show presentations);
- written offers by means of a preliminary prospectus that contains an estimated offering price range and meets other SEC rules; and
- written offers pursuant to a written communication called a "free writing prospectus."

Post-Offering Period

During the period beginning on the offering date and ending 25 days later, oral offers remain permissible, written offers may be made, and sales may be effected.

WHAT *CAN* WE SAY?

Pre-IPO companies are not completely muzzled while preparing to go public. The JOBS Act and several SEC safe harbors provide relief for many types of communications during the quiet period.

Rule 163A—Communications More Than 30 Days Before Public Filing

Rule 163A establishes a broad exemption from quiet period restrictions for communications made more than 30 days prior to the initial public filing of the Form S-1 if:

- the communication is made by or on behalf of the company (communications by underwriters and other IPO participants do not qualify);
- the communication does not reference the IPO; and
- the company takes reasonable steps to prevent the communicated information from being further distributed during the period beginning 30 days prior to public filing and ending 25 days after the offering date (for example, by inquiring about the publication schedule before agreeing to an interview).

Rule 169—Factual Business Communications

Rule 169 enables a company to continue to disseminate regularly released, ordinary-course information both prior to and during the IPO process if the communication:

- consists of factual information about the company, its business or financial developments, or other aspects of its business, or advertisements and other information concerning the company's products or services;
- is of a type regularly released by the company in the ordinary course of business;
- is released or disseminated by employees or agents of the company who historically have provided such information;
- is consistent in all material respects with the timing, manner and form of release or dissemination of similar past releases or disseminations;
- does not include information about, and is not released in connection with, the IPO; and
- is intended for use by persons (such as customers, suppliers or business partners) other than investors or potential investors in the company.

Rule 169 does not cover "forward-looking" statements, such as financial forecasts or information about future plans, expectations or objectives.

Rule 135—Announcement of Intent to Conduct Public Offering <u>Before</u> Filing Registration Statement

Rule 135 permits a public announcement that a company is planning a public offering. The announcement must include specified disclaimers and legends, and be limited to the following information:

— the name of the issuer;

— the title, amount and basic terms of the securities offered;

— the amount of the offering, if any, to be made by selling stockholders;

— the anticipated timing of the offering;

— a brief statement of the manner and purpose of the offering, without naming the underwriters; and

— whether the issuer is directing its offering to only a particular class of purchasers.

Rule 134—Announcement of Proposed Public Offering After Filing Registration Statement

Rule 134 permits a public announcement that a company proposes to make a public offering of securities. The announcement cannot be made until the company has publicly filed a registration statement for the offering, must include specified legends, and must be limited to:

— specified factual information about the legal identity and business locations of the company;

— a brief indication of the general type of business of the company;

— specified factual information about the terms of the offering, including the security offered, the anticipated offering timetable, the price or price range and the intended use of proceeds, and the identity of the underwriters;

— instructions for obtaining the preliminary prospectus, once available, and purchasing the shares offered; and

— procedural information for participation by the company's officers, directors and employees in a directed share program.

Price and price-related information must be excluded until an estimated offering price range has been disclosed in the Form S-1.

WE'RE STILL PRIVATELY HELD—WHY SHOULD WE CARE?

Violations of the quiet period restrictions can have various consequences, some imposed by the SEC staff and others self-imposed.

If the staff believes that a violation has occurred, several sanctions may be invoked:

— ***Cooling-Off Period:*** The staff may impose a "cooling-off period" that forces the company to delay its IPO for a period of time determined by the staff. Although imposed infrequently, a cooling-off period can jeopardize any IPO, given market volatility.

— ***Rescission Risk Disclosure:*** The company may be required to include "rescission risk disclosure" in its Form S-1—an acknowledgment that the company could be required to repurchase the shares sold in the IPO at the original offering price for a period of one year following the date of the violation.

— ***Corrective Disclosure:*** The company may be required to include as part of its Form S-1—and therefore assume legal responsibility for—the statements that were made in violation of quiet period restrictions or to cite the impermissible public statements and explain why the statements are or may be inaccurate. This disclosure can be embarrassing and may require the prospectus to disclose projections or other forward-looking information that would not otherwise be included. The process of agreeing with the staff on the exact wording of the disclosure could also delay the offering.

— ***Civil Penalties:*** The SEC can seek monetary penalties against a company and its directors and officers, or seek the imposition of a cease-and-desist order against future violations.

Apart from the possibility of SEC sanctions for violations, the effect of the quiet period rules is felt through the ongoing monitoring of public communications to avoid violations, the modification or curtailment of communications that would present concerns, and, in some cases, self-imposed cooling-off periods—such as a deliberate delay in the initial public filing of the Form S-1 for a period of 30 days so that a published article can qualify for the Rule 163A safe harbor.

HOW CAN WE LIVE WITH THE QUIET PERIOD?

The quiet period is not a time for bold experimentation in publicity practices, but it need not be completely suffocating either. Careful planning can help a company avoid the mistakes that are commonplace—and potentially harmful to its IPO—while maintaining a program of necessary public communications. Important planning steps include:

— ***External Communications Policy:*** The company should adopt an external communications policy that designates the only representatives authorized to publicly communicate on behalf of the company, and instructs employees to refer external inquiries regarding the company to the authorized company spokespersons.

— ***Legal Review:*** Counsel should review all press releases and other written communications prior to dissemination and the company should consult with counsel before engaging in any other public communications, such as conference speaking engagements.

— ***Adherence to Established Disclosure Practices:*** The company should adhere to an established and consistent pattern of routine disclosure practices. The Rule 169 safe harbor—which the company will rely on for most of its public communications beginning 30 days before the initial public filing of the Form S-1—is limited to factual business communications in the ordinary course of business that are consistent with past practices in timing, manner and form.

— ***Coordination with Underwriters:*** The company should review all proposed press releases and other publicity activities with the managing underwriters. ■

DETECTING VIOLATIONS

After a company submits its Form S-1, the SEC staff, as part of its review process, routinely conducts internet searches on the company; browses its website; looks at press releases, newspapers and magazine stories mentioning the company; and reviews relevant industry publications and databases. These activities, which continue throughout the SEC review process, help the staff uncover potential violations of the quiet period restrictions.

Section 1202 of the Internal Revenue Code (the Code) permits non-corporate investors to exclude from federal taxable income a portion of the gain realized from the sale or exchange of "qualified small business stock" (QSB stock) held for more than five years, subject to certain caps.

For QSB stock acquired after September 27, 2010, the exclusion is 100% of the gain, but the amount an investor may exclude with respect to the stock of a given issuer cannot exceed the greater of $10 million or ten times the investor's adjusted basis in the stock. For QSB stock acquired on or before September 27, 2010, the percentage of gain that may be excluded is either 50% or 75%, depending on the date of acquisition, and the gain not excluded is generally subject to federal income tax at the rate of 28% rather than the reduced rates otherwise applicable to net capital gains.

The Section 1202 exclusion for QSB stock provides a powerful federal tax incentive and can be a significant factor in investment decisions by venture capitalists and other non-corporate investors. However, investors should also understand and consider the state tax treatment of QSB stock, which can vary depending on where the investor is located or resides and may subject the investor to state taxes on the sale or exchange of QSB stock even where federal income taxes do not apply.

ELIGIBILITY FOR QSB STOCK TREATMENT

Generally, stock is treated as QSB stock for federal income tax purposes only if the following requirements are satisfied:

— The issuer is a domestic C corporation as of the date of issuance, and neither it nor any predecessor corporation had aggregate gross assets in excess of $50 million at any time prior to or immediately after the issuance.

— During substantially all of the investor's holding period, the issuer used at least 80% (by value) of its assets in the active conduct of one or more "qualified trades or businesses."

— The stock was acquired by the investor at its original issuance in exchange for cash or property (other than stock) or as compensation for services. Certain redemptions during the four-year period beginning two years before the issuance of what would otherwise qualify as QSB stock may cause such stock not to qualify.

STATE TAX CONSEQUENCES GENERALLY

Even when income is exempt from federal income tax, it may still be subject to state taxes, depending on the state(s) in which the investor is subject to taxation. Many state income tax laws conform to the Code, including the federal definition of gross income, while others do not.

To plan effectively and avoid costly surprises, investors should be aware of states that do not conform to the Code or have state-specific provisions regarding QSB stock. Irregularities in state tax laws that investors should watch out for include:

— *States that do not conform to the Code.* Some states, including Mississippi, New Jersey and Pennsylvania, impose a personal income tax that does not conform to the Code, including Section 1202. In these states, gains on the sale or exchange of QSB stock generally will be subject to tax in the state, like other capital gains. Although Arkansas tax law does not conform to the Code generally, it does specifically conform to Section 1202 of the Code.

— *States that conform to the Code in part but specifically modify the Section 1202 benefit.* Although a state may conform its tax law to the Code generally, the state may have specific provisions that modify the treatment of QSB stock. States with such provisions include Alabama and California, which generally do not allow any exclusion for gain from the sale or exchange of QSB stock, and Hawaii and Wisconsin, both of which only provide a 50% exclusion for gain from the sale or exchange of QSB stock (even where the sale qualifies for the 100% federal tax exclusion). In Wisconsin, the exclusion is further limited to gains on stock acquired after 2013.

— *States that conform to the Code as of a specific fixed date.* Many states conform their tax laws to the Code as of a fixed date. Because this fixed date may not be current, the tax laws in some states previously did not match the current federal treatment of QSB stock. As a result of the recent Massachusetts law change described below, all states (except for those described in the preceding bullet) that conform their tax laws to the Code as of a fixed date now fully recognize the 100% federal exclusion for the sale or exchange of QSB stock. ■

A CLOSER LOOK AT THREE KEY STATES

California, Massachusetts and New York collectively account for a majority of all venture capital financing activity in the United States, making the state tax treatment of QSB stock particularly important to VC investors located in these states. The state tax treatment of QSB stock in California, Massachusetts and New York is generally as follows:

— *California.* Because California generally does not allow any exclusion for gains from the sale or exchange of QSB stock, such gains are subject to California state tax even when exempt from federal income tax under Section 1202. California personal income tax rates currently range up to 13.3%, depending on income level.

— *Massachusetts.* As a result of a recent change in Massachusetts tax law, noncorporate taxpayers in Massachusetts can generally take into account the full available federal tax exclusion for sales of QSB stock on or after January 1, 2022. For sales prior to that date, the exclusion under Section 1202 is generally limited to 50%. However, Massachusetts also has a special rule providing a reduced rate of tax for sales of stock in certain small business corporations domiciled in Massachusetts, which may be available, both before and after January 1, 2022, for sales that do not qualify for the full federal exclusion.

— *New York.* New York tax law conforms to the federal treatment of QSB stock. Taxpayers subject to New York State or New York City personal income tax can generally take into account, in computing those taxes, the full exclusion that is allowed to them for federal income tax purposes.

Trends in VC-Backed Company M&A Deal Terms

We reviewed all merger transactions between 2018 and 2022 involving VC-backed targets (as reported in PitchBook after 2019, in Dow Jones VentureSource or PitchBook for 2019, and in Dow Jones VentureSource prior to 2019) in which the merger documentation was publicly available and the deal value was $25 million or more. Based on this review, we have compiled the following deal data:[1]

Characteristics of Deals Reviewed	**2018**	**2019**	**2020**	**2021**	**2022**
Sample Size	37	20	25	45	22
Cash	84%	60%	60%	24%	41%
Stock	3%	0%	8%	18%	5%
Cash and Stock	13%	40%	32%	58%	54%
Deals With Earnout	**2018**	**2019**	**2020**	**2021**	**2022**
With Earnout	32%	40%	28%	42%	41%
Without Earnout	68%	60%	72%	58%	59%
Deals With Indemnification	**2018**	**2019**	**2020**	**2021**	**2022**
With Indemnification					
By Target's Shareholders	84%	80%	88%	76%[3]	86%
By Buyer	39%	45%	32%	29%	68%
Deals With Representation and Warranty Insurance	**2018**	**2019**	**2020**	**2021**	**2022**
With Representation and Warranty Insurance	41%	25%	68%	47%	50%
Survival of Representations and Warranties[4]	**2018**	**2019**	**2020**	**2021**	**2022**
Shortest	12 Mos.	12 Mos.	12 Mos.	12 Mos.	12 Mos.
Longest	24 Mos.	24 Mos.	18 Mos.	24 Mos.	24 Mos.
Most Frequent	18 Mos.	18 Mos.	12 Mos.	12 Mos.	12 Mos.
Caps on Indemnification Obligations	**2018**	**2019**	**2020**	**2021**	**2022**
With Cap	100%	100%	100%	100%	100%
Limited to Escrow	79%	86%	81%	90%[6]	78%
Limited to Purchase Price	0%	0%	0%	0%	0%
Exceptions to Limits[5]	100%	100%	95%	100%	89%
Without Cap	0%	0%	0%	0%	0%
Escrows	**2018**	**2019**	**2020**	**2021**	**2022**
With Escrow	90%[7]	94%	90%	91%	89%
% of Deal Value					
Lowest[8]	3%	10%	8%	5%	7%
Highest	15%	13%	15%	18%	15%
Most Frequent	10%	12%	15%	10%	8%
Length of Time[9]					
Shortest	12 Mos.	12 Mos.	12 Mos.	12 Mos.	12 Mos.
Longest	36 Mos.	36 Mos.	24 Mos.	36 Mos.	30 Mos.
Most Frequent	18 Mos.	12 Mos.	12 Mos.	12 Mos.	12 Mos.
Exclusive Remedy	72%	64%	68%	53%	73%
Exceptions to Escrow Limit Where Escrow Was Exclusive Remedy[5]	100%	100%	92%	100%	91%
Baskets for Indemnification	**2018**	**2019**	**2020**	**2021**	**2022**
Deductible	47%	56%	52%[10]	71%[11]	53%
Threshold	53%	44%	29%[10]	26%[11]	32%
MAE Closing Condition	**2018**	**2019**	**2020**	**2021**	**2022**
Condition in Favor of Buyer	100%	100%	100%	97%	100%
Condition in Favor of Target	12%	35%	24%	37%	29%
Exceptions to MAE	**2018**	**2019**	**2020**	**2021**	**2022**
With Exception[12]	97%[13]	100%	100%	95%[13]	100%

[1] For certain transactions, certain deal terms have been redacted from the publicly available documentation and are not reflected in the data compiled below.

[2] Excludes two transactions that do not provide for indemnification but permit setoff against contingent consideration.

[3] Measured for representations and warranties generally; specified representations and warranties may survive longer.

[4] Generally, exceptions were for fraud, willful misrepresentation and certain "fundamental" representations commonly including capitalization, authority and validity. In a limited number of transactions, exceptions also included intellectual property representations.

[5] Includes two transactions where the limit was below the escrow amount.

[6] One transaction not including an escrow at closing did require funding of escrow with proceeds of earnout payments.

[7] Excludes transactions which also specifically referred to representation and warranty insurance as recourse for the buyer.

[8] Length of time does not include transactions where such time period cannot be ascertained from publicly available documentation.

[9] A "hybrid" approach with both a deductible and a threshold was used in another 10% of these transactions in 2020 and 11% of these transactions in 2022.

[10] A 50/50 cost sharing approach was used in another 3% of these transactions in 2021.

[11] Generally, exceptions were for general economic and industry conditions.

[12] The only transaction(s) not including such exceptions provided for a closing on the same day the definitive agreement was signed.

Trends in Convertible Note and SAFE Terms

Based on hundreds of convertible note and SAFE (simple agreements for future equity) financing transactions we handled from 2018 to 2022 for companies and investors, we have compiled the following deal data:

		2018	2019	2020	2021	2022
Deals With Purchase Agreement		**2018**	**2019**	**2020**	**2021**	**2022**
If included, a purchase agreement typically contains representations and warranties from the company (and possibly the founders).	% of deals	40%	63%	36%	50%	38%
Term*		**2018**	**2019**	**2020**	**2021**	**2022**
The term of the convertible note before it matures.	Median	12 mos.	17 mos.	24 mos.	12 mos.	12 mos.
	Range	3–24 mos.	12–36 mos.	5–48 mos.	4–36 mos.	10-60 mos.
Interest Rate*		**2018**	**2019**	**2020**	**2021**	**2022**
The rate at which interest accrues during the term of the convertible note.	Median	5%	6%	5%	5%	6%
	Range	2%–8%	3%–15%	0.2%–8.5%	0.2%–8%	1.3%–8%
Deals With Security Interest*		**2018**	**2019**	**2020**	**2021**	**2022**
Convertible note investors sometimes require the company to provide a security interest in company assets.	% secured	15%	18%	11%	0%	0%
	% unsecured	85%	82%	89%	100%	100%
Deals With Conversion Discount		**2018**	**2019**	**2020**	**2021**	**2022**
Convertible note and SAFE investors often require that conversion in connection with an equity financing be at a discount from the price paid by new investors in the financing. A conversion discount is often coupled with a cap on the valuation at which conversion occurs.	% of deals	77%	70%	89%	85%	63%
	Range of discounts	10%–25%	10%–25%	15%–40%	10%–35%	10%–30%
	% with ≤ 20% discount	91%	95%	92%	94%	87%
	% with > 20% discount	9%	5%	8%	6%	13%
	% with valuation cap	57%	42%	40%	35%	47%
Deals With Conversion Upon Maturity*		**2018**	**2019**	**2020**	**2021**	**2022**
If a convertible note is outstanding at the time of maturity and is not otherwise paid upon maturity, it often converts into shares of the company's common stock or preferred stock. This conversion is most often at the election of the investor but may be mandatory.	% of deals	40%	55%	53%	59%	46%
	% with optional conversion	75%	92%	90%	80%	50%
	% with mandatory conversion	25%	8%	10%	20%	50%
	% that convert into:					
	common stock	38%	33%	11%	10%	33%
	preferred stock	62%	67%	89%	90%	67%
Deals With Conversion Upon Company Sale		**2018**	**2019**	**2020**	**2021**	**2022**
If a convertible note or SAFE is outstanding at the time of a sale of the company, it often converts into shares of the company's common stock or preferred stock. This conversion is most often at the election of the investor but may be mandatory.	% of deals†	57%	56%	32%	50%	21%
	% with optional conversion	88%	73%	78%	90%	80%
	% with mandatory conversion	12%	27%	22%	10%	20%
	% that convert into:					
	common stock	82%	67%	50%	80%	60%
	preferred stock	18%	33%	50%	20%	40%
Deals With Repayment Premium Upon Company Sale		**2018**	**2019**	**2020**	**2021**	**2022**
Convertible note and SAFE investors may require that they receive a multiple of the outstanding investment amount in connection with a sale of the company.	% of deals†	57%	37%	43%	50%	29%
	Median premium	2x	2x	2x	2x	1.5x
	Range of premiums	1.2x–2x	1.5x–3x	1.5x–3x	1.25x–2.5x	1.25x–2.0x
Deals With Warrant Coverage		**2018**	**2019**	**2020**	**2021**	**2022**
Investors sometimes receive a warrant in addition to their note or SAFE. The amount of company stock covered by the warrant is usually proportional to the investment amount, referred to as the warrant coverage.	% of deals	10%	15%	0%	5%	0%
	Coverage range	25%–65%	10%–35%	N/A	25% (one deal)	NA
	% that cover common	33%	50%	N/A	100%	NA
	% that cover preferred	67%	25%	N/A	0%	NA
	% that cover common or preferred (depending on the circumstances)	0%	25%	N/A	0%	NA

* Excludes SAFEs, which by their nature do not have maturity dates, interest rates or security interests.

† Excluding SAFEs, 45%, 50%, 42%, 53% and 38% of convertible note transactions included conversion upon company sale and 70%, 45%, 63%, 53% and 54% of convertible note transactions included a repayment premium upon company sale for each of the years 2018 through 2022, respectively.

Trends in Venture Capital Financing Terms

Based on hundreds of venture capital financing transactions we handled from 2018 to 2022 for companies and investors, we have compiled the following deal data:

Deals With Multiple Liquidation Preferences		2018	2018 Range	2019	2019 Range	2020	2020 Range	2021	2021 Range	2022	2022 Range
A "multiple liquidation preference" entitles holders of preferred stock to receive more than 1x their money back before sale or liquidation proceeds are distributed to holders of common stock.	First round	3%	1.5x	2%	1.5x (one deal)	0%	N/A	0%	N/A	0%	N/A
	Post-first round	3%	1.5x–2.5x	4%	1.5x–2x	3%	1.5x–2.25x	0%	N/A	2%	2x – 3x

Deals With Participating Preferred Stock		2018	2018 Range	2019	2019 Range	2020	2020 Range	2021	2021 Range	2022	2022 Range
"Participating preferred" stock entitles holders to receive a stated liquidation preference plus a pro-rata share (on an as-converted basis) of any remaining proceeds available for distribution to holders of common stock.	First round										
	Total	13%		14%		9%		9%		4%	
	Capped	0%	N/A	38%	1x–3x	80%	2x–3x	20%	3x (one deal)	0%	N/A
	Post–first round										
	Total	31%		11%		10%		6%		10%	
	Capped	41%	2x–5x	17%	1.6x–3.5x	22%	1.25x–2x	29%	2x–2.5x	30%	1.5x-3.5x

Deals With an Accruing Dividend		2018	2019	2020	2021	2022
"Accruing dividends" are generally payable upon liquidation or redemption of the preferred stock, effectively increasing the liquidation preference of the preferred stock.	First round	7%	10%	9%	5%	2%
	Post–first round	24%	15%	8%	11%	10%

Anti-Dilution Provisions		2018	2019	2020	2021	2022
A "full ratchet" anti-dilution formula provides that the conversion price of the preferred stock will be reduced to the price paid in the dilutive issuance, regardless of how many shares are involved in the dilutive issuance. In contrast, a "weighted average" anti-dilution formula takes into account the dilutive impact based upon the number of shares and the price involved in the dilutive issuance and the number of shares outstanding before and after the dilutive issuance.	First round					
	Full ratchet	0%	0%	2%	0%	2%
	Weighted average	100%	100%	98%	100%	98%
	Post–first round					
	Full ratchet	1%	2%	0%	0%	3%
	Weighted average	99%	98%	100%	100%	97%

Deals With Pay-to-Play Provisions		2018	2019	2020	2021	2022
"Pay-to-play" provisions provide an incentive to investors to invest in future rounds of financing. Investors that do not purchase their full pro-rata share in a future round lose certain rights (e.g., their shares of preferred stock may be converted into common stock at the then applicable conversion rate or a more punitive rate, and they may lose director designation, registration or other rights).	Total	7%	8%	3%	3%	2%
	% of total that convert into common stock	100%	92%	100%	83%	100%
	% of total that convert into another series of preferred stock	0%	8%	0%	17%	0%

Explanatory Note : "First round" refers to a company's first priced preferred stock financing regardless of round designation.

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Data Sources: WilmerHale compiled all data in this report from PitchBook, except as otherwise indicated.

Special note on data: Due to delayed reporting of some transactions, the venture capital financing and M&A data discussed in this report is likely to be adjusted over time as additional deals are reported. Based on historical experience, the number of reported venture capital financing and M&A transactions is likely to increase by approximately 5–10% in the first year following the initial release of data and by smaller amounts in succeeding years, and other venture capital financing and M&A data is likely to be adjusted to reflect the inclusion of additional deals.

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