Simple Cap Table Analysis

2H 2023

When making a venture capital or growth equity investment, perhaps the most critical priority is confirming that your pro-forma ownership percentage of the target company aligns with your investment expectations – in short, that you are getting what you paid for. While cap table analysis can seem confusing at first glance, you can in most instances quickly confirm the outcome lines up with your assumptions using a simple calculation:

1. Start with the implied valuation of the company as of immediately prior to the investment (the "**Pre-Money Valuation**").

2. Add the total amount of the equity financing (your investment, together with the total amount of money expected to be raised from other investors) to the Pre-Money Valuation (this sum is the "**Post-Money Valuation**").

3. Divide the dollar amount of your investment by the Post-Money Valuation – this number (the "**Reference Percentage**") is the percentage of the total value of the Company that you should own. For example, a $1mm investment in a Company with a Post-Money Valuation of $10mm equates to a Reference Percentage of 10% ownership interest in the company.

4. Review the company's cap table and divide (i) the number of shares to be allocated to you, by (ii) the company's "fully diluted equity capitalization" (which should include the full amount of any option pool, even the unallocated portion) (this quotient is your "**Cap Table Percentage**").

5. Compare the Cap Table Percentage to the Reference Percentage. If there is any variance between these two values, it is likely that either your investment is absorbing hidden dilution, or the company has made an error in its preparation of its cap table (a not uncommon circumstance).

The simplest way to think about this analysis is that two types of value are being combined: (i) the value of the company (the pre-money valuation) and (ii) the dollar value of the investment (which is being added to the company's balance sheet). The value of the company is increased dollar for dollar by the money invested into the company (the post-money valuation), and so the existing owners of the company will own a percentage of the company equal to the pre-money value divided by the post-money value, and the new investors will own a percentage in the company equal to the new money invested divided by the post-money value.

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Example

Assumptions:

- Pre-money valuation of the target company is $40mm
- Amount raised in financing round is $10mm
- Dollar amount of your investment is $5mm (i.e., $5mm of the $10mm)
- You will receive 1,000 shares
- The Company's post-money "fully diluted equity capitalization" is 10,000 shares

Therefore, you would follow the below steps to find confirm that your understanding of your fully-diluted ownership lines up with the ownership percentage you will actually receive:

1. **Post-Money Valuation** = Pre-money valuation + amount raised in financing round
    a. **Post-Money Valuation** = $40mm + $10mm
    b. **Post-Money Valuation** = $50mm

2. **Reference Percentage** = Dollar amount of your investment / post-money valuation
    a. **Reference Percentage** = $5mm / $50mm
    b. **Reference Percentage** = 10%

3. **Cap Table Percentage** = Shares allocated to you by the company / the company's post-money "Fully Diluted Equity Capitalization"
    a. **Cap Table Percentage** = 1,000 shares / 10,000 shares
    b. **Cap Table Percentage** = 10%

4. **Cap Table Percentage** = Reference Percentage
    a. 10% = 10%

In this example, you have confirmed that the company's calculation lines up with the ownership percentage implied by your investment assumptions.

If you have any questions, please contact your primary attorney at Seward & Kissel LLP or Gary Anderson at anderson@sewkis.com or Eric Buchanan at buchanan@sewkis.com.

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