



May 29, 2020

Submission via Web Site

Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-1090

Re: Facilitating Capital Formation and Expanding Investment Opportunities by Improving Access to Capital in Private Markets; File Number S7-05-20

Ladies and Gentlemen:

I am a partner and General Counsel at Y Combinator (“YC”), and am writing to provide some clarity regarding the simple agreement for future equity (safe). It has come to our attention that there is concern regarding use of the safe as a financing instrument for Regulation CF. For background, Y Combinator is an early stage investment fund. Since 2005, YC has been an early investor in over 2,500 companies including Airbnb, Dropbox, Stripe, Instacart, Reddit, and Doordash, and in the process has helped create thousands of jobs. To date, the aggregate market value of Y Combinator companies is over \$200 billion.

When I started at YC, one of my goals was to help our startup companies raise money efficiently using a document that was easy for anyone to understand. This was particularly important to me because many of the companies in which we invest are founded by individuals with little legal or investment experience themselves, and the securities existing at the time (preferred stock, convertible notes) were convoluted and hard for investors and founders alike to understand. I created the safe with this goal in mind: to simplify investment in startup companies.

The SEC’s “plain English” rules partially inspired the safe. I graduated law school in 1998, the year that the SEC adopted plain English disclosure. At the large Silicon Valley law firm where I began my career, my colleagues lamented having to draft “risk factors” with the word “use” instead of “utilize,” and proxy statements with the word “will” instead of “shall.” Although I still have doubts that retail investors find registration statements or proxy statements easy to read, the SEC’s plain English rules were a significant improvement to our craft, and I learned to draft documents for public company clients using plain English rules, with simplicity and understandability as a guide. Unfortunately, private company financing documents did not, and still do not, encourage lawyers to “plain-English-ize” the terms. Laymen don’t understand and/or are loathe to read them. Startup company founders are similarly discouraged by the complexity of the concepts and the opaque way securities instruments and financing documents are drafted. The result is that private financing documents have not evolved to meet the needs of their users.

In 2013, convertible notes were used by the vast majority of Silicon Valley startup companies to raise the first (seed) round of equity financing. The typical company wasn’t selling shares of its capital stock because: (1) startups don’t sell common stock to raise money, and (2) preferred stock was – still is – sold using financing documents that are hard for non-lawyers to comprehend, and require hiring legal counsel to spend weeks negotiating terms and drafting documents. Convertible notes solved these issues by providing a relatively short document that helped companies get seed funding more quickly and with less expense. Negotiating the rights, privileges and preferences of the preferred stock into which an investor’s money would eventually convert was postponed until an equity financing happened at a later date (ideally when the company had more resources, and could hire legal counsel).



The safe was created to further simplify investing in early stage companies. The safe was informed by experience: we continually had to amend convertible notes to extend maturity dates, which often became an administrative burden for everyone involved. The inspiration was to keep the convertibility feature of the notes intact, but remove the debt features. While we were at it, we drafted this new financing instrument to be understandable and in *plain English* – no “shalls” instead of “wills,” no superfluous belts-and-suspenders provisions, no needless complexity. The goal for us has always been simplicity and transparency: we sought to make a document easy for anyone to understand.

The initial safe was released in early 2014. Since then, *1,725 YC companies have issued safes to investors*. Approximately 482 of those companies so far have converted those safes into preferred stock in connection with a subsequent preferred stock financing. Simultaneously, we published the safe on YC’s website and open-sourced it for any company, or investor, to use. The safe is now used by startups all over the world. It has been translated into multiple foreign languages, conformed to use in jurisdictions outside of the US, and has been used to raise well over \$8 billion dollars. My firm belief is that people appreciate a legal document that is drafted with the *user* in mind, not the lawyer that the user may be otherwise forced to hire.

Please bear this background in mind as you consider the appropriateness of the safe for use in crowdfunding, and consider these additional clarifications:

- The safe is *fundamentally* an instrument convertible into an equity interest, just like a convertible note, a warrant or an option.
- Do not confuse the original YC safe with the host of copy-cat instruments that have sprung up in the wake of the safe’s widespread adoption. Each of the copy-cat instruments is tweaked to serve the purpose of its creator, and YC’s original safe should be evaluated on its own, not in context of edited, hybrid, one-off or distorted facsimiles of it. These non-YC versions of the safe are a consequence of open-sourcing the safe, an action we still endorse and support notwithstanding some of the aggravating side effects. In the newest revisions to the YC safe, released in 2018, we made it easy for users of the safe to quickly understand whether they are reviewing the original YC safe or a copy-cat version by adding specific language that must be removed if either the issuer or the investor makes material modifications to the safe.¹
- Some copy-cat instruments, like the SAFT, have taken the framework and simplicity of the safe and used it for purposes for which it was never intended. The original YC safe does not convert into tokens or revenue share.
- Note that in the following excerpt from the proposed rules (page 156), the *most common event* triggering the conversion of the safe into equity, **the equity financing**, has been omitted:

A SAFE is an agreement to provide investors with a future equity stake in the issuer if certain triggering events occur. SAFEs are not an equity interest or common stock of an issuer. Rather, they are convertible into such equity only upon the occurrence of a triggering event specifically enumerated in the agreement, such as when the issuer is acquired, merges with another company, or conducts an initial public offering. [emphasis added]

Again, an equity financing is a “triggering event specifically enumerated in the agreement” and its omission from the above-quoted description is nonsensical. Based on YC’s experience, fully 99%

¹ This language states: “This Safe is one of the forms available at <http://ycombinator.com/documents> and the Company and the Investor agree that neither one has modified the form, except to fill in blanks and bracketed terms.



of all outstanding safes convert into shares of preferred stock in a private placement equity financing. It's true that the safe includes mergers and public offerings as additional triggering events, because in a minority of cases these other events may occur before an equity financing – and we wanted to provide investor protections across all of these different scenarios.

- The safe was **not** created to address any issues or problems related to company capitalization tables. In our experience and in the vast majority of cases, a separate safe is issued to each individual investor in a company. If this is a feature of a copy-cat safe variant, that is a tweak made by another party to serve its own purposes. It is not a feature of the original YC safe, nor a variant of the safe that is currently prevalent in the market.

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A safe is a security convertible into an equity interest, and we therefore support harmonizing the types of securities eligible under Regulation Crowdfunding with that of Regulation A+. However, the SEC should not exclude safes from Regulation CF offerings, and the original YC safe, which is the version of the safe most prevalent in the market, does not bear much resemblance to the copy-cat instruments that seem to be creating confusion within the context of Reg CF, and has ultimately led the SEC to issue this request for comment.

Sincerely,

A handwritten signature in black ink, appearing to read 'Carolynn', with a horizontal line extending to the right.

Carolynn Levy