BULGARIAN PRIVATE EQUITY AND VENTURE CAPITAL ASSOCIATION

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**Webinar**

# Model Convertible Loan Agreement

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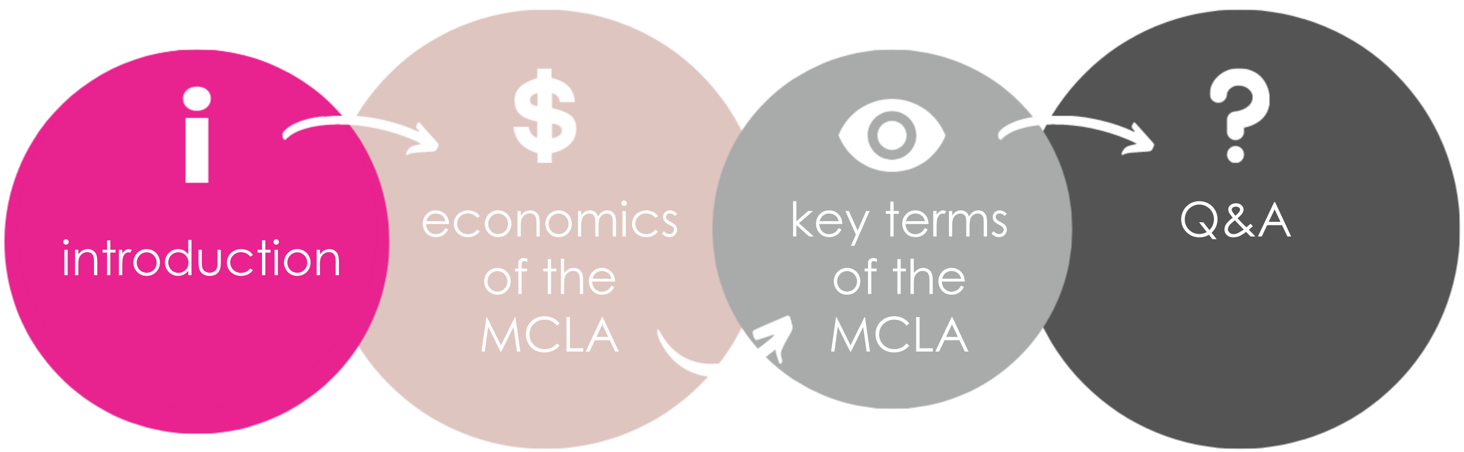

# economics of the MCLA

- Convertible loan (**CL**) – loan financing to a startup company which converts into equity at the next round of equity investment

- CL financing vs equity financing:

  - CL usually comes at an **earlier stage** of the life of the company

  - CL is for a relatively **smaller amount** than equity financing

  - CL **does not require agreement on the valuation** of the company

  - CL is a **simple document** (vs equity financing documents) and allows for faster execution and utilization of funds

# economics of the MCLA

- Company's perspective:

  - **possibility to receive financing** if the company does not qualify for bank loans or equity financing

  - CL involves interest which, however, is not paid regularly but accrues and converts into equity at the CL conversion (**PIK Interest**)

  - CL is **unsecured**

  - usually, CL **does not grant control (veto rights)** to the investor over the business of the company (except standard covenants)

# economics of the MCLA

- Investor's perspective:

  - like a call option – allows investment of a **relatively small amount of money** to lock in a favourable valuation (discounted valuation) if the company succeeds in attracting larger equity investment in the future

  - **risky instrument** – investor normally has no control over the business of the company and is (smartly) betting on its success; if the company fails (insolvency) the investor would normally lose its investment

# key terms of the MCLA

- Conversion:

  - conversion into equity at the next round of equity investment (**Qualified Financing**):

    - min amount of equity investment: e.g., 1 million

    - conversion discount – the CL principal + interest will convert into shares at a price of the lesser of:

      – 80% of the issue price per share in the equity investment OR
      – pre-Qualified Financing valuation of 1 million

  - conversion into equity on the date falling e.g., 3 years after drawdown (**Maturity Date**) – the CL principal + interest will convert into shares at a valuation of 1 million

# key terms of the MCLA

- Cash repayment:
  - at **change of control** – CL principal + interest + premium of e.g., 100% CL principal
  - at event of default (**EoD**) – CL principal + interest + default interest

# key terms of the MCLA

- Conversion mechanics:
  - valuation of outstanding CL principal + interest in BGN by 3 independent experts appointed by the Commercial Register
  - shareholders meeting to approve capital increase and amendment to the AoA
  - register the capital increase in the Commercial Register
- Key point: cooperation from Company and existing shareholders required

# key terms of the MCLA

- Events of default:
  - non-conversion
  - non-payment
  - breach of other obligations
  - misrepresentation
  - material adverse effect
  - cessation or interruption of business
- Consequences: acceleration + costs of enforcement + default interest

# key terms of the MCLA

- Representations:
  - status, power and authority
  - no insolvency
  - binding obligations
  - no EoD
  - no misleading information
  - financial statements
  - pari passu ranking
  - no conflict with obligations
  - existing agreements
  - no litigation
  - use of proceeds
  - no brokers’ or finders’ fees

# key terms of the MCLA

- Undertakings:
  - financial statements
  - operating results
  - business plan
  - information
  - most favoured lender
  - EoD notification



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# Q&A


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# Thank you!