

SAFE (SIMPLE AGREEMENT FOR FUTURE EQUITY)



INVESTOR:

Fondo Acción



SOCIAL PURPOSE ORGANIZATION:

ZhanaSolutions

EARLY AND GROWTH-STAGE SOCIAL ENTERPRISES GENERALLY SEEK TO RAISE FLEXIBLE CAPITAL to finance their growth, build their capacity, and access working capital. Bridge capital - a type of financing with lower transaction costs than a qualifying investment round, can offer these enterprises an easier and faster financing alternative that other instruments such as mezzanine finance.

A Simple Agreement for Future Equity (SAFE) is a financing instrument used in early-stage and seed funding rounds. Although similar to a convertible note, a SAFE avoids the traditional complexities of a convertible. A SAFE i) does not include an interest rate (implicit or explicit), ii) does not include a maturity date, and iii) does not include conversion triggers based on a valuation agreed to by the investor and the company.

The idea behind a SAFE is that an investor will convert their investment into equity in a future fundraising round. The pre-defined conditions set ex-ante in the agreement typically include i) a discount rate and/or ii) a valuation cap that will be used in the subsequent financing round.¹ A SAFE provides a financing option when an early-stage company doesn't have enough information or traction to establish a valuation favorable



¹ The valuation cap also protects SAFE investors from dilution during subsequent financing rounds.



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for both investor(s) and entrepreneur(s). The SAFE structure offers i) better terms for the investor through increased optionality (e.g., preferred pricing or conditions during future liquidity or liquidation events) and ii) the time and opportunity for the entrepreneur(s) to capture greater value before diluting their ownership during a qualified investment round.²

Negotiating a SAFE primarily means establishing a valuation cap and a handful of other straightforward considerations. When a triggering event occurs (e.g., a priced investment round), investors' participation rights are adjusted to reflect their preferred status and the company receives capital at a more favorable valuation, typically thanks to decreased uncertainty.



Context

Fondo Acción was created in 2000 as a non-profit, private fund dedicated to building a better relationship between local communities and the environment in Colombia. The organization's three main areas of focus are: i) child development as a key pillar of sustainable social change; ii) the environment in all forms, including protected watersheds, community land and territory, private nature reserves, and Indigenous nature reserves; and iii) cross-cutting programs related to capacity building and public policy.

In 2018, Fondo Acción launched the *Fondo de Inversiones Misionales de Impacto* (FIMI fund) to invest in Colombian early-stage and growth companies and ventures. The fund has an impact-first approach and seeks to invest in environmental and social impact enterprises with innovative business models, and teams with prior experience in the business, sector, and market in question. The fund primarily offers equity and debt financing, and investments range from USD 100,000 to USD 470,000, with terms ranging from 7 to 10 years.³



² For more information on the SAFE structure, see: <https://www.ycombinator.com/library/6m-understanding-safes-and-priced-equity-rounds>

³ For more information, visit <https://fondoaccion.org/2022/06/08/fimi-2/>



ZhanaSolutions is an environmental technology company that develops wastewater treatment solutions based on the circular economy, focusing on the integrated and efficient management of fats, oils, and grease in industrial kitchens. The company offers an innovative technology that uses a thermal grease separation process that treats wastewater from industrial kitchens and food production facilities more efficiently than conventional technologies.

Its business model consists of helping companies comply with environmental regulations and corporate standards by providing a comprehensive grease waste management service through the Zhana G-Trap, a patent-pending grease separation technology.⁴ This waste management system can recover up to 99% of grease in wastewater and offers a centralized treatment process that reduces costs and generates efficiencies. The collected grease trap waste is separated on site and is used as input for the oleochemical industry.



⁴ See: Socialab (nd). *Zhana G-Trap. Recuperador de grasas* [Zhana G-Trap: Grease Recovery Unit]. Retrieved from: <https://ar.socialab.com/challenges/PremioBidFemsa20/idea/120202>



TABLE 1 General Information - ZhanaSolutions

Year Founded	> 2019
Headquarters	> Bogotá, Colombia.
Geographic Focus	> Colombia.
Financing Sources	> Grants, private investment, impact investment.
Partners and Funders	> Innpulsa Colombia, Cleantech Hub (European Union), Oxentia (Oxford University), Colegio de Estudios Superiores de Administración, Rockstart Impact, Bancolombia, and more
Website	> https://zhanasolutions.com/



Opportunity and Deal Terms

As part of its efforts to create positive impact in Colombia, Fondo Acción provides access to impact financing via different structures, including i) calls for proposals to select and co-finance projects, ii) managing capital from various sources (philanthropic, concessional, and market rate) and allocating it to initiatives aligned with its three strategic areas of focus, and iii) occasionally serving as the direct implementer. To scout investment opportunities, Fondo Acción participates in business roundtables, shares information with other impact funds, and works with a network of partner incubators, accelerators, and other actors. This allows the FIMI team to identify ventures that align with its investment thesis, proceed with screening and due diligence, and eventually make an investment.

Within Fondo Acción, the FIMI fund serves the core purpose of developing a pipeline of impact enterprises that align with the organization’s investment thesis of i) patient capital, ii) minority deals, and



iii) social and environmental enterprises with clear exit strategies. For investments made via the FIMI fund, convertibles and SAFE structures facilitate access to bridge financing to fund the early growth of scalable impact enterprises. Companies that receive funding from Fondo Acción are also eligible for non-financial support, including knowledge and technology transfers to structure and implement impact metrics. ZhanaSolutions will benefit from Fondo Acción's support during future concessional capital fundraising efforts.

Fondo Acción was interested in investing in ZhanaSolutions primarily because of the company's solid proof of concept, the commitment of the founders, and the company's ability to scale its innovative solution throughout Colombia. ZhanaSolutions had already demonstrated an ability to establish valuable partnerships and acquire prominent, high-impact clients, which supported its growth and financial projections. Additionally, ZhanaSolutions was working in an under-addressed sector (grease waste management and the circular economy) and providing a solution with an intellectual property strategy and the potential to scale in Colombia and throughout Latin America⁵.

In December 2021, after confirming that the company had the potential to grow and scale its positive impact, the FIMI fund invested USD 120,000 in ZhanaSolutions⁶ via a SAFE (the first time it has used this instruments in its portfolio).



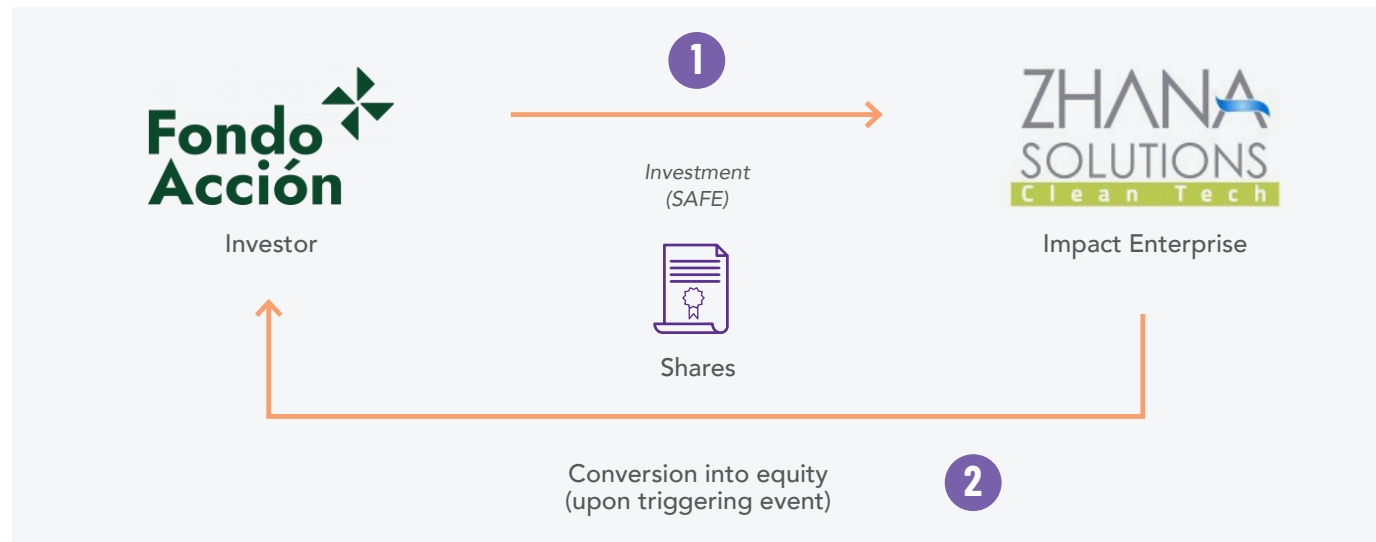
- 5 It is important to note that the potential impact of the solution provided by ZhanaSolutions is based on scaling across Latin America to replace existing urban waste management models with more sustainable solutions, with a particular focus on reducing the pressure on sewage networks and wastewater treatment systems by decreasing the amount of grease from industrial kitchen processes that enters the sewage system by 99%.
- 6 Fondo Acción. Anexo: Informe de Gestión 2021. Plan Estratégico 2021-2024 [Annex: Management Report 2021, Strategic Plan 2021-2024]. Retrieved from: <https://fondoaccion.org/wp-content/uploads/2021/04/Informe-de-Gestion-2021-RTE.pdf>





SAFE Terms and Structure

FIGURE 1 How it Works



SOURCE: Based on interviews.



ASSUMPTIONS

- Reducing grease waste from industrial kitchen processes reduces pollution in the water where this waste is disposed.
- Increasing the efficiency of grease waste treatment methods not only reduces water pollution, but also decreases the operating costs of restaurants and industrial kitchens by helping them avoid unnecessary expenses associated with pipe repair/maintenance and other complementary treatments.



- 1 Fondo Acción and ZhanaSolutions signed an investment agreement totaling USD 120,000. As part of this agreement, Fondo Acción received the right to convert its investment into shares of ZhanaSolutions at a preferred conversion price during a subsequent qualified Series A fundraising round or strategic sale.^{7 8}
- 2 When shares are issued during a future Series A round or as a result of a liquidity event, the value of the SAFE agreement will be converted into shares (i.e., the total investment amount converts into SAFE preferred stock) using the conversion price per preferred share (i.e., the discount price or SAFE price based on the pre-defined valuation cap).

TABLE 2 Terms and Conditions of SAFE

Can Replace	> Debt, convertibles
Enterprise Lifecycle	> Seed stage
Risk/Return Profile	> High risk / High return
Maturity	> Series A, strategic sale, or dissolution (whichever comes first)

Discount Rate and Valuation Cap

Fondo Acción invested USD 120,000 in ZhanaSolutions via a SAFE with a post-money valuation⁹ cap of USD 2 million and a discount rate of 20%.



- 7 Series A is generally when a company provides equity shares to investors for the first time at a pre-determined price.
- 8 A strategic or trade sale is the sale of the company (in whole or in part) to another company.
- 9 Post-money refers to the value of a company after a financing round.



Triggering Event

The triggering event for the conversion process is a Series A funding round, scheduled for the last quarter of 2023.

Conversion Price

The conversion price will be based on either (i) the SAFE price or (ii) the discount price, whichever calculation results in a greater number of shares of SAFE Preferred Stock as follows:

1. The SAFE price of USD 2 million / number of shares issued as part of the equity financing
2. A 20% discount rate is applied to the post-money share price, i.e., the Series A valuation

Pro-rata Rights or Participation Rights

During each subsequent round of funding, Fondo Acción has the right to invest additional funds capped at USD 470,000, or no more than a 25% participation.



When to Use this Instrument

- ▶ A SAFE does not accrue interest, lacks a maturity date, and no recovery option is provided in the case of non-payment. Certain investors might seek additional upside/compensation to balance the higher **conversion risk**.
- ▶ All parties should consider that a SAFE is a high-risk investment instrument, both for the investor(s) and the company. For example, if the company fails to capture value or raise a subsequent investment round, the investor(s) will not obtain the expected return and may be left without liquidity. On the other hand, if the SAFE establishes a conversion price that is too high or a valuation cap that is too low, the founder(s) face the potential of significant ownership dilution during subsequent fundraising rounds.



- ▶ **Open and transparent communication** is critical during all negotiations to establish that a SAFE is a high-risk investment and to avoid tensions during negotiations between the executive team/founders and new investors, especially during the first qualified fundraising round, as this is the first time that founders and other common shareholders will see dilution in real terms.

