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Singapore

VENTURE CAPITAL

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This country-specific Q&A provides an overview of venture capital laws and regulations applicable in Singapore.

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SINGAPORE
VENTURE CAPITAL

1. Are there specific legal requirements or preferences regarding the choice of entity and/or equity structure for early-stage businesses that are seeking venture capital funding in the jurisdiction?

THERE ARE A NUMBER OF DIFFERENT CORPORATE STRUCTURES THAT MAY BE USED FOR SETTING UP EARLY-STAGE BUSINESSES IN SINGAPORE, SUCH AS SOLE PROPRIETORSHIP, LIMITED PARTNERSHIP, LIMITED LIABILITY PARTNERSHIP OR PRIVATE COMPANY LIMITED BY SHARES. HOWEVER MOST, IF NOT ALL, EARLY-STAGE BUSINESSES THAT SEEK VENTURE CAPITAL FUNDING IN SINGAPORE ARE SET UP AS PRIVATE COMPANIES LIMITED BY SHARES. THERE ARE REASONS FOR THIS, THE KEY ONES OF WHICH ARE SET OUT BELOW:

1. **Limited liability**: Shareholders of a private limited company enjoy limited liability, which means an obligation of the company is solely the obligation of the company and the liabilities of the company are to be met out of the property of that company. The liability of a shareholder to contribute is limited to the amount, if any, unpaid on its shares and so its personal or other assets are protected from the company's liabilities;
2. **Separate legal entity**: A private limited company is a separate legal entity, which can sue or be sued in its own name. Separation is often attractive to investors as it provides a clear structure for ownership and investment; and
3. **Ease of share issuance and flexibility of equity structure**: The process for issuing shares in a Singapore private company is simple and straightforward, requiring mainly the requisite shareholder approvals and filings to be made with the Accounting and Corporate Regulatory Authority (**ACRA**) of Singapore, being Singapore's national regulator of business entities. The ability to issue different classes of shares with varying rights (such as liquidation preferences and anti-dilution mechanisms) also allow investors additional ways to protect their investments. A key point to note is that private limited companies may have at most 50 shareholders (excluding employees of the company or of its subsidiary). Accordingly, if the number of persons taking up shares in the company will cause the company to exceed this limit, the company would be required to convert from a private limited company to a public limited company (which would be subject to more regulations than a private limited company).

2. What are the principal legal documents for a venture capital equity investment in the jurisdiction and are any of them publicly filed or otherwise available to the public?

The principal legal documents for a venture capital equity investment in Singapore are:

1. **Non-disclosure agreement**: to regulate the provision of information from the target company to the investor;
2. **Non-binding term sheet**: setting out the principal key terms for the relevant fundraising round;
3. **Share subscription agreement**: between the company and the relevant investors relating to the issuance and subscription of new shares in the company;
4. **Shareholders' agreement**: between the company and all shareholders of the fundraising company relating to the governance of the company;
5. **Constitution**: of the company, amended and restated to incorporate the relevant terms of the equity instruments of the company being issued, and typically incorporating some or all of the terms of the shareholders' agreement; and
6. **Employee incentive arrangements**: often

in the form of an employee share option plan which gives the right for certain employees to obtain shares or other instruments upon exercise of options.

The constitution of the company is filed with ACRA and publicly available. The other transaction documents would not typically be publicly filed.

3. Is there a venture capital industry body in the jurisdiction and, if so, does it provide template investment documents? If so, how common is it to deviate from such templates and does this evolve as companies move from seed to larger rounds?

The Singapore Venture & Private Capital Association (**SVCA**) was formed in 1992 to promote the development and interests of the private capital industry in Singapore.

In 2022, the Singapore Academy of Law and the SVCA released an updated and expanded set of model legal documents called the Venture Capital Investment Model Agreements (**VIMA 2.0**) intended for use for early-stage financing rounds. The updated VIMA 2.0 incorporate feedback from the industry on the original VIMA templates which were released to the market in 2018, and aim to balance the interests of investors, founders and company, and reflect market trends with a view to narrowing the scope of issues to be negotiated.

The VIMA 2.0 comprise a set of Pre-Series A and Series A templates. The Series A documents include:

1. **Lexicon**: to explain the relevant concepts, terms and provisions to founders and investors;
2. **Non-disclosure agreement**;
3. **Term Sheet**: setting out the key terms for the investment and the material rights and obligations of the investors, founders and the company;
4. **Subscription Agreement**: for the subscription of Series A shares in the company;
5. **Shareholders' Agreement**: relating to the governance of the company and the rights and obligations of the shareholders;
6. **Convertible Note**: to document an investment into a company way of a debt which will convert into shares on certain triggering events, most commonly the next equity round.
7. **Environmental, Social and Governance Letter Agreement**.

Additionally, the Pre-Series A documents include:

1. **CARE – Convertible Agreement Regarding Equity**: which allows an investor to invest cash in a company in exchange for shares or cash on certain triggering events. The CARE follows contains similar terms to the SAFE note (or a simple agreement for future equity) which is used in other jurisdictions; and
2. **Founders' Agreement**: to be entered into between the founders and the company to regulate key early stage governance matters and the founders equity.

The VIMA 2.0 are available for download on the SAL and SVCA websites.

There are an increasing number of early-stage deals which are based off the VIMA 2.0 model documents, however, as companies move to larger rounds, deal terms tend to become more negotiated and tailored to the specific business and transaction.

4. Are there any regulatory frameworks in respect of companies offering shares for sale that need to be considered, for example any restrictions on selling and/or promoting the sale of shares to the general public?

Under the Securities and Futures Act 2001, a company that seeks to raise funds by offering shares would need to issue a prospectus unless an exemption applies. A prospectus is a detailed legal document, typically running into hundreds of pages, setting out the matters that an investor would reasonably need to know before making the investment along with various other matters mandated by law. The preparation of such a document normally involves financial, accounting and legal advisors and this method of seeking finance is generally not relevant for early-stage businesses – it is both costly and time consuming, and would generally not be relevant to investors taking investments in early stage businesses such as venture capital investors.

Early-stage businesses that seek to raise funds will generally rely on the following exemptions for raising funds (whether equity or debt) without a prospectus:

1. **small offer**: a small offer, where the total amount raised is less than SGD5 million in any period of 12 months;1
2. **private placement**: an offer made to no

more than 50 persons in any period of 12 months, provided the offer is not accompanied by an advertisement and no selling or promotional expenses are paid or incurred in connection with the offer other than those incurred for administrative or professional services, or by way of commission or fee for services rendered by;2 or
3. **accredited or institutional investors**: an offer made to accredited investors3 or institutional investors4 which at a high-level:
    1. an institutional investor is a financial institution such as a bank or investment firm; and
    2. an accredited investor is an individual with net personal assets of SGD2 million in value or financial assets exceeding SGD1 million in value or whose income in the last 12 months is not less than SGD300,000. A corporation can also be an accredited investor if it has net assets of more than SGD10 million in value.

5. Are there any general merger control, anti-trust/competition and/or foreign direct investment regimes applicable to venture capital investments in the jurisdiction?

There are no foreign investment controls specifically relating to venture capital investments in Singapore companies by foreign investors, except for companies that own residential landed property.

However, the acquisition of shares in companies in certain regulated industry sectors may require approval from the relevant regulator regardless of the jurisdiction of the investor, applying to both foreign and domestic purchasers, if the acquisition were to cause the investor to hold a percentage of shares in the company exceeding certain specified percentage thresholds. The relevant percentage threshold will depend on specific industry sector concerned, but percentage thresholds that are commonly stipulated are 5%, 12%, 20% and 50%.

A non-exhaustive list of these regulated industries include:

1. the banking and finance industry (requiring approval from the Monetary Authority of Singapore);
2. the utilities and gas industry (requiring approval from the Energy Market Authority);
3. the broadcasting and newspaper industry (requiring approval from the Minister for Communications and Information); and
4. the telecommunications industry (requiring approval from the Infocomm Media Development Authority.

In broad terms, Singapore has a voluntary merger control regime which means that filings are warranted in Singapore only where a transaction could lead to a restriction in competition in Singapore. Given the nature of typical venture capital investments for minority stakes into early-stage businesses, it is unlikely that the competition clearance in Singapore would be required for such transactions.

6. What are the prevailing tax incentives or structures offered to venture capital investors in the jurisdiction, if any?

The response to this question will be provided separately.

7. What is the process, and internal approvals needed, for a company issuing shares to investors in the jurisdiction and are there any related taxes or notary (or other fees) payable?

Subject to any other reserved matter approvals contractually required under the shareholders agreement or constitution of the company, for a company to issue shares, the company will require shareholders approval (passed by way of an ordinary resolution) approving the allotment and issuance of the shares. The company will have to have to file the prescribed return of allotment with ACRA and the allotment and issuance of the shares is only effective when the electronic register of members has been updated by ACRA.

If the company is issuing preference shares, the terms of the preference shares has to be included in the constitution of the company prior to the allotment of any such preference shares. The amendment of the constitution of the company will, subject to any other reserved matter approval, require shareholders approval (passed by way of a special resolution i.e. 75% + 1). Thereafter, the company will have to file the notice of resolution and a copy of the constitution as adopted or altered with ACRA within 14 days of the passing of such resolution.

No stamp duty fees are payable in respect of an issuance of share. Nominal fees are payable to ACRA when making the relevant lodgements.

8. How prevalent is participation from investors that are not venture capital funds, including angel investors, family offices, high net worth individuals, and corporate venture capital?

Singapore's investment landscape is dynamic and diverse, encompassing a range of participants beyond traditional venture capital funds. Singapore has established itself as a major hub for startups and innovation in Asia, attracting a variety of investors, and therefore the following types of investors are also seen in the market alongside traditional venture capital funds:

1. **Angel Investors**: very early stage businesses in Singapore are often backed by angel investors. With the number of startups and multinationals now based in Singapore, these investors might be entrepreneurs themselves or retired executives who not only bring in funds but also valuable experience and networks. Singapore has developed a number of angel networks, with prominent ones including the Singapore Angel Investment Network and BANSEA (Business Angel Network Southeast Asia), indicating a well-structured community of angel investors.
2. **Family Offices**: there has been a noticeable increase in the number of family offices setting up operations in Singapore in recent years, partly due to favourable regulatory conditions and the view of Singapore as financially stable hub. More than half of Asia's family offices are based in Singapore as of 2023. Historically these firms have focussed more on investment into private capital funds, including venture funds (as well as other classes), but there has been a trend in the last two years of increasing direct participating in funding rounds.
3. **Corporate Venture Capital (CVC)**: many multinational corporations have established their CVC arms in Singapore to tap into the innovative startup ecosystem. Singapore's strategic location, pro-business environment, legal frameworks, and government support for innovation have made it an attractive destination for corporate investors. The government has also launched several initiatives, such as the Startup SG Equity scheme, to encourage investments in startups through co-investment with the private sector. The Singapore Economic Development Board (**EDB**) has also launched a support scheme called the Corporate Venture Launchpad 2.0 which can provide financial incentives for corporates establishing their venture operations in Singapore.

9. What is the typical investment period for a venture capital fund in the jurisdiction?

The investment period for a venture capital fund, which is the span during which the fund actively makes new investments, usually ranges from three to six years. This is followed by an additional period during which the fund manages and eventually exits these investments, aiming to return capital to the limited partners (**LPs**). The entire lifespan of a fund, including the investment period and the subsequent management and exit phase, is often around 10 years, although this can sometimes be extended to 12 or even 14 years through specific arrangements with the LPs.

10. What are the key investment terms which a venture investor looks for in the jurisdiction including representations and warranties, class of share, board representation (and observers), voting and other control rights, redemption rights, anti-dilution protection and information rights?

Investors will typically negotiate for a specific class of shares that carry certain rights and privileges not afforded to ordinary shareholders. Typically, these shares would be a new class of preference shares, which would be convertible into ordinary shares, have some or all of the following rights:

1. **Voting**: investors would expect voting rights, and such preference shares would sit alongside the ordinary shares and vote equally. Enhanced or weighted-voting rights are possible, but rarely seen unless the relevant company is in distress.
2. **Liquidation Preference**: liquidation preferences are common in venture investment transactions, which ensure that preferred shareholders are paid out before ordinary shareholders in the event of a sale or liquidation of the company. The liquidation preference can be a multiple of the relevant investment amount, but commonly is equal to the investment amount. Preference shares

can also be structured as either ‘participating’ or ‘non-participating’, with participating shares not only having a preference on liquidation but also allowing the holder to participate in further dividends or proceeds along with the ordinary shareholders.

3. **Anti-dilution**: anti-dilution provisions protect investors from dilution of their ownership percentage in the event that the company issues additional shares at a lower price than what the investors originally paid. There are different types of anti-dilution provisions, with the most common in the Singapore market being the ‘broad based weighted average’.
4. **Redemption Rights**: these allow investors to require the company to repurchase their shares after a certain period or upon the occurrence of specific events. Redemption rights are a form of liquidity protection for investors but can be a financial burden for the company, and are not commonly included in early-stage transactions in Singapore.

To issue the relevant preference shares, the investors, the company and often the founders will usually enter into a subscription agreement. The subscription agreement contains the obligations and mechanics related to the issuance of the relevant preference shares and, importantly from an investors perspective, typically a series of representations and warranties related to the company. These are statements of fact made by the company, and also often by the founders, to the investors at the time of investment covering a wide range of topics, including the company’s structure, financial status, intellectual property, compliance with laws, and more. The purpose of these representations and warranties is to provide the investor with a clear picture of the company’s situation and to establish a baseline of facts upon which the investor is willing to proceed with the investment.

Investors expect a number of contractual provisions and protections to apply to their investment going forward, and these would usually be contained in a shareholders’ agreement. The shareholders’ agreement will typically include terms relating to, amongst others, the management and governance of the company, the transferability of the investors’ shares (including in connection with an exit), and provisions with regard to the founders (such as restrictive covenants). The key terms investors would typically to negotiate include:

1. **Board Representation and Observers**: investors may require the right to appoint one or more members to the company’s board of directors. This gives them a direct role in company oversight and major decision-making. Company’s are usually prepared to give an investor a director seat if their investment is of sufficient size. Additionally, investors might negotiate for the right to appoint board observers who do not have a vote on the board but can attend meetings.
2. **Control Rights**: investors will often require that certain operational, governance and structural actions of the company, such as raising additional capital, changing the company’s constitution, or selling the company, require the approval of some or all of the preferred shareholders. This can give investors significant control over the company’s strategic direction. These ‘reserved matters’ are usually heavily negotiated – it is common to have a list of items that require approval of some or all of the directors of the company appointed by the investors, and separately a list of items that need approval of some or all of the preferred shareholders. These are in addition to any consent requirements under the Companies Act of Singapore.
3. **Information Rights**: investors typically negotiate for the right to receive regular financial and operational information from the company. This can include annual budgets, quarterly and annual financial statements, and other reports that provide insight into the company’s performance and prospects. The nature of the information provided to shareholders is often subject to negotiation, with material shareholders having the right to access or receive more information.
4. **Transfer regime**: investors, founders and the company will often negotiate a set of restrictions on the transfer of shares of the company. Common restrictions on transfers include having ‘right of first refusal’ or ‘right of first offer’ processes, which investors will often resist applying to their own shares but will want to ensure founders are subject to those provisions. Drag-along and tag-along rights are also common, with the specific nature of those subject to negotiation. Investors would also typically expect founders to be subject to lock-up periods given their importance to the business. Depending on the nature of the investors, and the company, it is also common to see restrictions on transferring to a specified group of potential shareholders, such as competitors of the major shareholders or competitors of the investee company itself.

11. How common are arrangement/ monitoring fees for investors in the jurisdiction?

Arrangement fees are one-time fees paid by an investee company to the venture capital investor, usually leading the fundraising round, for arranging the investment. These are reasonably common in the market, and are usually agreed to by the investee company for covering the costs associated with due diligence, legal documentation and administrative expenses incurred during the investment transaction. Typically these are a fixed fee, but sometimes are structured as a percentage of the total investment amount.

It would be unusual for a venture capital investor to charge an investee company ongoing monitoring fees.

12. Are founders and senior management typically subject to restrictive covenants following ceasing to be an employee and/or shareholder and, if so, what is their general scope and duration?

It is customary for venture capital investors to require that founders and senior management are subject to restrictive covenants for as long they remain shareholders and for a certain period of time afterwards.

However, restrictive covenants such as non-competition and non-solicitation restrictions are prima facie void, unless it can be shown that there is a legitimate proprietary interest to be protected and the clause is reasonable with respect to the interest of the parties concerned and to the interests of the public.

On legitimate interests, the courts have found that if the employee is involved in developing a specific product offering, the employer may have a legitimate interest in imposing restrictive covenants on the employee as the employee holds trade secrets. However, where the protection of confidential information or trade secrets is already covered by other means, for example confidentiality clauses in the shareholders' agreement or employment agreement, the employer will have to demonstrate that the restraint of trade clause in question covers a legitimate proprietary interest over and above the protection of confidential information or trade secrets.

The courts in Singapore have considered the following factors in determining whether a restrictive covenant is "reasonable", including:

1. the length of the period attached to the restrictive covenants – this should not be an arbitrary number, but should be a reasonable time period that would be required to protect the relevant interests (several factors have to be taken into account in the assessment of the reasonableness of the length of period of restraint, such as the seniority and role of the employee in the business, the employee's responsibilities and access to confidential information / trade connections, the type of industry and what the industry considers reasonable and embodies in its practice, etc);
2. the geographical area covered by the restrictive covenants – where the founder does not have any contact or activity in a particular geographical area, it would be considered to be unreasonable for the restrictive covenants to apply to those territories;
3. the scope of the restrictive covenant – for example, it would be unreasonable to extend the restrictive covenant to areas in which the company or the founder / employee has no involvement in; and
4. whether there is a reasonable connection to the founder or employee's position and influence – for example, it would be unreasonable for a restrictive covenant to be imposed on a founder or senior management in respect of all the company's customers, where such person does not have direct contact with the customer.

Given the variety of factors that should be considered and particularly given that the periods of restraint should be considered in respect of each individual case, there is no blanket / standard periods of restraint for all founders and senior management. Ultimately, the party seeking to enforce the restrictive covenant (being the company or another shareholder of the company) would bear the burden of proving that it has a legitimate interest to be protected and that the clause is no wider than necessary to protect such interests, and that the restraint was reasonable in all the circumstances.

13. How are employees typically incentivised in venture capital backed companies (e.g. share options or other equity-based incentives)?

In venture capital backed companies, particularly in a competitive hub like Singapore, attracting and retaining top talent is crucial for growth and success. Growth businesses often offer equity-based incentives, including shares, share options and other types of instrument such as restricted stock units (RSUs) to incentivise employees and align the interests of those employees with those of the company and its shareholders.

1. **Share Options**: one of the most common forms of equity-based incentives is share options, which give employees the right to purchase a specific number of shares in the company at a predetermined price, known as the exercise price or strike price, after a certain period or upon meeting certain milestones. This period before the options can be exercised is known as the vesting period. If the company's share value increases over time, employees can buy shares at a lower, locked-in price with a view to selling them at a higher market price.
2. **Employee Stock Ownership Plans (ESOPs)**: another popular equity-based incentive is the Employee Stock Ownership Plan (ESOP). ESOPs are structures which provide employees with an ownership interest in the company – typically the company allocates certain of its shares to individual employees, usually at no upfront cost to the employee. Similar to share options, ESOPs often have a vesting schedule that incentivizes employees to remain with the company long-term to fully benefit from the plan and the plans will provide for clawback / buyback rights in a leaver situation.
3. **Restricted Stock Units (RSUs)**: RSUs are shares given to employees as part of their compensation, but typically come with restrictions. The most common restrictions are (i) vesting, meaning that the employee will gain full ownership of the shares only after a certain period or upon achieving specific goals, and (ii) voting, meaning that the shares are issued with economic rights but with no ability to vote alongside the voting shares. Similar in concept, but less often seen in this market, are performance shares or performance share units (PSUs) which are similar to RSUs but are tied to the achievement of certain company performance targets, such as revenue or profit margins.
4. **Phantom Shares**: Phantom shares are another form of incentive that provides the benefits of share ownership without actually requiring the company to issue shares and therefore diluting existing shareholders' equity. Instead, employees receive a cash bonus or shares equivalent to the value of a certain number of company shares, based on vesting or the company's performance.

14. What are the most commonly used vesting/good and bad leaver provisions that apply to founders/ senior management in venture capital backed companies?

Vesting and leaver provisions are commonly used to align the interests of founders and senior management with those of the investors. Vesting refers to the process by which a founder or employee earns the right to own shares, or options in respect of shares, over time. This mechanism is designed to incentivise key personnel to commit to the company for a longer period and contribute to its growth and success, whilst also ensuring there is a mechanism to redistribute equity in the case of departures.

a) Vesting provisions

Vesting of shares or other awards is typically based on time metrics, but performance / milestone-based vesting is also seen:

Time-Based Vesting: founders and senior management typically have their equity subject to time based-metrics, with the most common vesting schedule being a four-year period with a one-year cliff. This means that the founder or senior manager would not earn any equity until they have remained with the company for at least one year. After the one-year cliff, the equity would typically vest on a monthly or quarterly basis over the remaining three years.

Performance-Based Vesting: some companies will also adopt performance-based vesting schedules or milestones, which may be tied to specific events (such as the closing of an equity financing round), or hitting certain targets such as revenue goals, profitability or product development milestones. These milestones are often additional to time-based vesting and may be linked to a separate award of equity or options.

Accelerated Vesting: acceleration clauses are also sometimes included, which allow for vesting to be accelerated upon certain events, such as a change of control (e.g., the company being acquired) or the termination of the founder or senior manager without cause.

b) Leaver provisions

Good and bad leaver provisions determine what happens to a leaver's unvested and vested shares if they exit the company. The provisions are designed to protect the company and its shareholders, including investors, from the potential negative impact of a founder or key employee leaving the company.

Good Leaver: A good leaver is typically someone who leaves the company due to reasons beyond their control, such as death, permanent disability, or sometimes involuntary termination without 'cause'. Good leavers may be allowed to keep a portion or all of their vested shares, and in some cases, a portion of their unvested shares may continue to vest for a certain period after they leave.

Bad Leaver: A bad leaver is usually defined as someone who resigns from the company or who's employment is terminated for 'cause' (which is often negotiated but will generally include misconduct, violation of company policies and poor performance). Bad leaver provisions often require that the individual forfeits their unvested shares and they may be compelled to sell their vested shares back to the company at a price that could be as low as the nominal value or the price paid for the shares.

It is important for founders and senior management to understand these provisions fully, as they can have a substantial impact on their personal financial outcomes and their ongoing relationship with the company.

15. What have been the main areas of negotiation between investors, founders, and the company in the investment documentation, over the last 24 months?

Private capital raised by startups in Singapore nosedived in the latter half of 2022 and 2023 as macroeconomic factors weighed heavily on investor sentiment. As a result, investors have continued to look for more favourable terms, which founders and companies have been having to accommodate to get transactions over the line. However, a closer examination of recent trends reveals signs of stability emerging in the startup investment landscape, with some of the key areas forming the focus of negotiations being the following:

1. **Valuation**: valuation continues to be a critical negotiation point. Both investors and founders aim to strike a balance between achieving a fair valuation that reflects the company's potential and ensuring that the investment is attractive to investors without overly diluting founder ownership. Given the general write-down in the valuations of businesses that raised capital during 2021 and the first half of 2022, agreeing the valuation of a priced-round is a key hurdle given it may impact the conversion prices of interim instruments raised by companies (such as SAFE notes) and also the anti-dilution protection of existing investors, and therefore the founders residual stake.
2. **Investment structure**: a number of investors are taking a more cautious approach to deploying capital and therefore are looking to structure their investment in tranches, with conditions attached to each tranche. This can complicate the rights given to investors, as investors will often push for 'full' rights from their initial investment, whereas founders prefer rights of investors to increase along with their investment amount over time.
3. **Preference dividends**: as well as liquidation preferences and anti-dilution structures being a key area of negotiations, some investors have requested preference dividends to attach to their preference shares. These preferred dividends are payable ahead of other amounts and can be structured as 'guaranteed' payments, and are a way of further increasing the return attributable to the preference shares and therefore enhancing the position of venture capital investors over the founders.
4. **Exit Strategy**: Discussions around the company's exit strategy, including timelines and potential exit scenarios such as IPOs or acquisitions, have become more of a focus in light of the relatively limited number of public market transactions and exits for venture backed businesses in Singapore.
5. **Founder Vesting**: with exit horizons tending to be stretched out, investors have been closely looking at founder vesting provisions to ensure that founders remain committed to the company for a realistic time period. This has involved vesting periods being extended or 'reset'.

16. How prevalent is the use of convertible debt (e.g. convertible loan notes) and advance subscription agreement/ SAFEs in the jurisdiction?

Whilst there is no public data available on the use of such instruments in Singapore, convertible debt instruments such as convertible loan notes and SAFES have become increasingly prevalent in startup financing in Singapore, mirroring trends seen in other startup ecosystems around the world. These instruments offer flexibility and simplicity compared to traditional equity financing rounds, making them attractive to both investors and founders, particularly in early-stage funding rounds.

With the valuations of growth businesses being heavily negotiated in recent times, and the prospect of down rounds (and therefore anti-dilution protection being triggered) being a real prospect for some companies, founders have been open to the use of convertible instruments as they allow the business to (somewhat) defer the valuation negotiation until a later date.

17. What are the customary terms of convertible debt (e.g. convertible loan notes) and advance subscription agreement/ SAFEs in the jurisdiction and are there standard from documents?

In September 2022, the Singapore Academy of Law and Singapore Venture Capital & Private Equity Association launched the Venture Capital Investment Model Agreements (**VIMA**) 2.0, an updated and expanded set of standard form documents for use in seed rounds and early-stage financing.

The VIMA 2.0 suite contains a model form of Convertible Note, and additionally a model form of Convertible Agreement Regarding Equity (**CARE**), which is modelled on a US-style SAFE and anticipated to be used for pre-seed stage transactions.

Common terms across these convertible instruments include:

1. **Discount Rate**: convertible instruments typically include the right to convert into equity at a discount to the price paid by later investors in the next financing round, giving the relevant holder a 'return' or upside on their investment at what is perceived to be a riskier time. Parties will negotiate the discount rate, but a common range is between 10-30%.
2. **Valuation Cap**: This is the maximum valuation at which the convertible loan can convert into equity, protecting investors from dilution in the event of a high-valuation equity financing round. It is common in the Singapore market for the conversion to take place at the lower of the discount rate and the valuation cap, therefore ensuring the investor receives the most favourable terms.
3. **Interest Rate**: some instruments contain an annual interest rate, which is applied to the loan provided to the company. It is a topic of negotiation as to how that interest is treated – some instruments provide that it will form part of the principal and form part of the amount that will convert, others may have provide for the interest to be payable in cash at maturity or conversion. Parties will also negotiate whether interest will compound (meaning the interest is turned into principal on a regular basis and accrues its own interest) or be simple interest and therefore not compound.
4. **Maturity Date**: convertible instruments often include a long stop date by which the loan must be repaid or converted into equity. The nature of the instrument will determine whether there is a right to be repaid – typically SAFEs or CAREs do not include a right to receive cash repayment on the maturity date.
5. **Conversion Triggers**: these are the events that trigger the conversion of the contribution into equity, such as a subsequent funding round or a sale of the company. Often these are linked to a 'qualified financing', meaning that the loan will not convert unless a minimum amount of cash is raised by the business in a financing. This gives investors comfort that the business has raised sufficient capital to deliver on its business plans.
6. **Warranties**: the company will typically provide basic warranties around its incorporation and title to the convertible notes / instrument being issued, along with confirmation that the company has received the necessary approvals to issue the shares upon conversion of that instrument. Additionally, for more substantial investments by way of convertible instrument, investors will often push for more detailed representations and warranties with respect to the investee business, often resembling a typical suite of statements that would be given in an equity round.

18. How prevalent is the use of venture or growth debt as an alternative or supplement to equity fundraisings or other debt financing in the last 24 months?

The use of venture or growth debt as an alternative or supplement to equity fundraisings or other debt financing has been gaining traction in various startup ecosystems, including Singapore, over the last 24 months. The economic conditions of the past 24 months have played a role in the increased use of venture debt – with the uncertainty caused by events such as the COVID-19 pandemic, many companies sought out non-dilutive financing options to extend their runway and navigate through periods of market volatility.

19. What are the customary terms of venture or growth debt in the jurisdiction and are there standard from documents?

In Singapore, there is no single set of standard form documents for venture debt or growth debt transactions. Each financial institution or lender may have its own set of documents, which are then customised for each transaction. Given the bespoke nature of these financing arrangements, the terms of these arrangements can be complex and will be the subject of negotiation between the borrower and the lender. The terms of such financing arrangements can vary widely depending on the lender, the industry, and the specific financial situation of the borrower, but will commonly include some or all of the following:

1. **Interest Rates and fees**: venture debt typically comes with higher interest rates than traditional bank loans due to the higher risk associated with lending to early stage businesses that may not have positive cash flows or significant assets to use as collateral. Interest rates can vary but are often in the range of 10-15% per annum. In addition to interest, lenders may charge an upfront fee and an end-of-term payment or exit fee, which can be a percentage of the loan or a fixed amount.
2. **Warrants**: lenders may also require warrants as part of the deal. Warrants are options to purchase equity in the company at a predetermined price and help compensate the lender for the higher risk. The percentage of warrants typically ranges from 5-20% of the loan amount, but this can vary widely.
3. **Loan term**: the term of venture debt is usually shorter than traditional loans, often ranging from 3 to 5 years. The amortization schedule, which is how the loan is paid back over time, may include an initial period where only interest is paid, followed by a period of principal plus interest payments.
4. **Covenants and security**: venture debt agreements will typically include financial covenants, such as minimum cash balances or financial ratios that the borrower must maintain. However, these covenants are generally less restrictive than those associated with traditional bank financing. The loan may be secured against the assets of the company, although this is less common in venture debt than in traditional lending.
5. **Subordination**: venture debt is often subordinated to other debt, meaning that in the event of a default, other creditors get paid before the venture debt lenders. This is typically outlined in an intercreditor agreement.

20. What are the current market trends for venture capital in the jurisdiction (including the exits of venture backed companies) and do you see this changing in the next year?

Consistent with a number of global markets, the venture capital landscape in Singapore continues to undergo changes, and challenges, as we head into 2024, influenced by broader economic trends and shifting investor priorities.

The venture capital market in Singapore experienced a sharp decline in investment in 2023, dropping to its lowest level in four years, with a 44% year-over-year decrease in equity funding value from 2022. This downturn is attributed to economic headwinds (inflation and high interest rates shifting the attractiveness of fixed income alternatives, as just one example), high valuations, and low liquidity, which are likely to continue affecting the market in 2024. A sense of caution remains from the investors perspective, prompting a preference for established models and essential sectors. A return to the bullish run of previous years, however, seems unlikely, with investors prioritising profitability rather than the ‘grow at all costs’ model of previous years. However, with US inflation now steady and interest rates coming down, and that trend expected to continue, there is optimism starting to move through the market.

One notable trend, as with other parts of the world, is the increasing attention towards AI startups. Energy transition and sustainability are also key sectors of focus for investors, with a number of clean energy businesses raising capital in the early months of 2024.

Exits remain a key area of focus, and challenge, for Singapore headquartered businesses. IPO exits have been limited, with companies primarily looking to Hong Kong and New York to provide liquidity rather than more local markets, albeit the markets continue to develop and may provide opportunities for smaller and mid cap businesses. There is optimism that some businesses may find exits as a part of a wave of consolidation expected to move through the region. Sectors such as e-commerce, fintech, and logistics are already seeing these transactions, where there is a demand for enhanced convenience and value, prompting platforms to merge for broader market access and improved services. Further, with the general decrease in valuations across the region, but those valuations now more stable, venture backed businesses may find themselves as attractive M&A targets for private equity and large corporate buyers.

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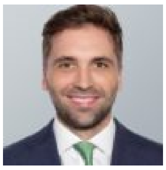

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