# THE FOUNDER FINANCIAL INFRASTRUCTURE (FFI) STANDARD

# Book 3: Capital Structure and Equity

**Beta v0.5**

**April 2026**

https://ffistandard.org/

# BOOK 3: CAPITAL STRUCTURE AND EQUITY

Book 3 defines the standards for the equity and capital structure a company must maintain: the cap table, the modeling of convertible instruments, the administration of equity compensation plans, the documentation of capital allocation, and the mechanics of liquidation and exit distribution. These five domains together constitute the ownership layer of financial infrastructure. Every other domain in the Standard affects financial performance. This domain determines who owns the value that performance creates.

## SECTION 3.1: THE CAP TABLE STANDARD

### PURPOSE

The cap table standard governs the completeness, accuracy, and currency of the record a company maintains of all equity ownership and equity-linked obligations. A cap table that does not reflect every instrument that can become equity is not a cap table for the purposes of this Standard. It is a partial record. Partial records produce material misrepresentations of ownership whenever any unreflected instrument converts, exercises, or is disclosed in a transaction.

### DEFINITIONS

CAP TABLE: A complete record of all equity ownership and equity-linked obligations in a company, maintained on a fully diluted basis as defined in Book 0, Section 0.4. The cap table includes all issued shares by class, all granted and ungranted options within authorised pools, all warrants, all outstanding SAFEs, all outstanding convertible notes, and all other instruments that can become equity, as if all such instruments had converted or exercised at the terms in effect at the record date.

ISSUED SHARE COUNT: The number of shares that have been formally issued and are currently outstanding. Issued share count is not equivalent to fully diluted share count. A cap table that presents only the issued share count without disclosing all instruments that can become equity misrepresents the ownership structure.

FULLY DILUTED SHARE COUNT: The total number of shares that would be outstanding if all equity-linked instruments currently in existence were converted or exercised at the terms in effect at the record date. Fully diluted share count includes issued shares, all options granted but not yet exercised whether vested or unvested, all ungranted options within an authorised and reserved pool, all warrants, and all shares issuable upon conversion of outstanding SAFEs and convertible notes. Fully diluted share count is the correct denominator for calculating any ownership percentage in a company that has issued any convertible instrument or equity compensation.

SHARE CLASS: A category of shares carrying a defined set of rights, preferences, and restrictions. Common shares and preference shares are distinct share classes. Within preference shares, different series issued at different rounds typically constitute distinct classes with distinct rights. The cap table must list each share class separately and must document the rights, preferences, and restrictions applicable to each class.

PREFERENCE SHARES: Shares issued to investors that carry rights not available to common shareholders, typically including a liquidation preference, anti-dilution protection, and participation rights. The specific terms of preference shares vary by investment agreement and must be reflected precisely in the cap table and in the liquidation mechanics model governed by Section 3.5.

COMMON SHARES: Shares typically held by founders, employees, and early participants that carry voting rights and economic participation but rank below preference shares in any liquidation or distribution event.

SHARE REGISTER: The formal legal record of share ownership maintained in accordance with the applicable corporate law of the company's jurisdiction of incorporation. The share register is a legal document. The cap table governed by this Standard is a financial model. They must be consistent with each other. Discrepancies between the cap table and the share register are deficiencies in both documents.

AUTHORISED SHARE CAPITAL: The maximum number of shares a company is authorised to issue under its constitutional documents. The cap table must reflect the total authorised share capital and must show that the fully diluted share count does not exceed it.

RECORD DATE: The date as of which the cap table reflects the ownership and instrument positions of all holders. The cap table must be dated to its record date. An undated cap table does not satisfy the requirements of this Standard.

**PRINCIPLES GOVERNING THIS SECTION**

A cap table that is accurate as of a past date but not updated to reflect subsequent instrument issuances, share transfers, or option grants is not a current cap table. Currency is a compliance requirement, not a best effort. The record date must be within the update frequency stated in the compliance criteria for the applicable level.

The fully diluted share count is the only ownership denominator that is accurate in a company that has issued any convertible instrument, option grant, or warrant. All ownership percentages stated in any document governed by this Standard must be calculated on a fully diluted basis unless the document explicitly states that the figure is calculated on an issued-only basis and the reason for that presentation is documented.

The cap table and the share register must be reconciled at every update. A discrepancy between the two is a deficiency in accounting integrity under Book 1, Section 1.4, as well as a deficiency in this section.

**COMPLIANCE CRITERIA**

**Level 1**

3.1.L1.1: The company maintains a cap table dated to a record date within ninety calendar days of the date of assessment.

3.1.L1.2: The cap table lists all issued shares by class with the name of each holder, the number of shares held, and the price per share at which those shares were issued.

3.1.L1.3: The cap table lists all outstanding SAFEs and convertible notes with the principal amount, the valuation cap if applicable, the discount rate if applicable, and the date of issuance for each instrument.

3.1.L1.4: The cap table lists all option grants made under any equity compensation plan with the number of options granted, the exercise price, and the vesting schedule for each grant.

3.1.L1.5: The cap table is consistent with the company's share register; any discrepancy between the two documents is identified and the cause is documented.

**Level 2**

3.1.L2.1: The company maintains a cap table dated to a record date within thirty calendar days of the date of assessment.

3.1.L2.2: The cap table presents ownership on a fully diluted basis, including all issued shares, all granted options whether vested or unvested, all ungranted options within any authorised and reserved pool, all warrants, and all shares issuable upon conversion of all outstanding SAFEs and convertible notes at the terms in effect at the record date.

3.1.L2.3: The cap table calculates the fully diluted share count and states the fully diluted ownership percentage of each holder and each instrument class.

3.1.L2.4: The cap table is maintained in a format that can be provided to an investor or legal advisor without preparation, reformatting, or explanatory accompaniment.

3.1.L2.5: The cap table documents the rights, preferences, and restrictions applicable to each share class, including liquidation preference terms, participation rights, anti-dilution provisions, and voting rights.

3.1.L2.6: The cap table is updated within fifteen working days of any share issuance, option grant, instrument conversion, warrant exercise, or share transfer.

3.1.L2.7: The company maintains a cap table model that projects the fully diluted ownership structure following the next anticipated funding round, under the assumptions documented for that round.

**Level 3**

3.1.L3.1: The company maintains a cap table dated to a record date within seven calendar days of the date of assessment.

3.1.L3.2: The cap table model projects the fully diluted ownership structure through at minimum two anticipated future funding events, with the assumptions for each event documented including pre-money valuation, investment amount, and option pool refresh terms.

3.1.L3.3: The cap table is maintained in a version-controlled format such that any prior version can be retrieved and compared to the current version with all changes identified and dated.

3.1.L3.4: The cap table is reconciled to the share register monthly; any discrepancy is resolved within ten working days of identification.

3.1.L3.5: The cap table model integrates with the liquidation mechanics model governed by Section 3.5, such that a change in the cap table structure updates the waterfall analysis without manual recalculation.

**BENCHMARKS**

Cap table update frequency benchmarks by stage:

- Pre-Revenue: within ninety days of any instrument issuance or change

- Early Revenue: within thirty days of any instrument issuance or change
- Growth Stage: within fifteen working days of any instrument issuance or change
- Scale Stage: within seven calendar days of any instrument issuance or change

These benchmarks reflect the increasing frequency of capital events and the increasing number of stakeholders whose decisions depend on accurate cap table information as a company grows.

Token warrants and AI-Native company structures: AI-Native companies may issue token warrants, future token agreements, or equity instruments tied to usage milestones or model performance thresholds alongside conventional equity. Where such instruments exist, each must be reflected in the cap table with the terms documented precisely, including the conversion mechanism, the trigger conditions, and the dilutive effect if converted. Where conversion mechanics depend on future events or values that are not yet determinable, the cap table must document the range of possible outcomes under stated assumptions. The cap table for AI-Native companies that have issued any non-standard instrument must include a written instrument summary section that describes each non-standard instrument in plain terms sufficient for a third party to model its dilutive effect.

**COMMON DEFICIENCIES**

CD 3.1.1: The cap table reflects issued shares and granted options but does not reflect outstanding SAFEs. Three SAFEs were issued at different valuation caps in the preceding eighteen months. Their dilutive effect at the next priced round has not been modeled. The cap table presents founder ownership percentages that are materially higher than the percentages that will exist after SAFE conversion at the next round.

CD 3.1.2: The cap table reflects the fully diluted share count based on granted options but excludes the ungranted portion of the authorised option pool. The option pool was authorised at ten percent of fully diluted shares at the last financing. Forty percent of the pool has been granted. The remaining sixty percent is authorised but ungranted. Ownership percentages in the cap table are calculated over a denominator that excludes this ungranted portion. All ownership percentages are overstated relative to their true fully diluted value.

CD 3.1.3: The cap table has not been updated since the prior funding round, which closed fourteen months ago. Three option grants have been made since then. One SAFE has been issued. One employee exercised vested options. The cap table does not reflect any of these events. The cap table presented in a current data room does not represent the current ownership structure of the company.

CD 3.1.4: The cap table and the share register are inconsistent. A share transfer executed six months ago appears in the share register but not in the cap table. The cap table overstates the ownership of the transferor and does not reflect the transferee. The discrepancy has not been identified because the two documents have not been reconciled.

## SECTION 3.2: THE SAFE AND CONVERTIBLE INSTRUMENT STANDARD

**PURPOSE**

The SAFE and convertible instrument standard governs the documentation, modeling, and disclosure of instruments that will become equity at a future event. These instruments are not equity at the time of issuance. They are contractual rights to receive equity under defined conditions. The failure to model them before they convert is the most common cause of surprise dilution in early-stage companies. This

 

section requires that the conversion mechanics of every outstanding instrument are modeled before any priced funding round is initiated.

**DEFINITIONS**

SAFE: Defined in Book 0, Section 0.4. A Simple Agreement for Future Equity in which an investor provides capital in exchange for the right to receive equity in a future priced funding round, subject to terms that determine the price at which the SAFE converts.

VALUATION CAP: Defined in Book 0, Section 0.4. The maximum valuation at which a SAFE or convertible note converts to equity, regardless of the actual price per share in the triggering round. Where the priced round is conducted at a pre-money valuation above the cap, the SAFE converts as if the round were priced at the cap valuation, producing more shares for the SAFE holder than the round price alone would imply.

DISCOUNT RATE: The percentage reduction applied to the price per share in a triggering funding round to calculate the conversion price for a SAFE or convertible note that carries a discount provision. A SAFE with a twenty percent discount converts at eighty percent of the price per share paid by new investors in the triggering round. Where a SAFE carries both a valuation cap and a discount rate, the conversion price is the lower of the price implied by the cap and the price implied by the discount. The instrument converts at whichever price produces more shares for the holder.

CONVERSION PRICE: The price per share at which a SAFE or convertible note converts to equity at the triggering event. The conversion price is determined by the valuation cap, the discount rate, or both, as specified in the instrument terms. Where both apply, the conversion price is the lower of the two calculated prices.

CONVERSION EVENT: The event that triggers the conversion of a SAFE or convertible note into equity. For most SAFEs, the conversion event is a priced equity financing round that meets defined threshold conditions. The specific conditions vary by instrument and must be documented for each outstanding instrument.

PRE-MONEY VALUATION: Defined in Book 0, Section 0.4. The agreed value of the company immediately before a new investment is received. Pre-money valuation is the denominator used to calculate the conversion price under a valuation cap: conversion price equals cap valuation divided by the fully diluted share count immediately before the round.

POST-MONEY VALUATION: Defined in Book 0, Section 0.4. The value of the company immediately after a new investment, equal to pre-money valuation plus the investment amount. An investor's ownership percentage is calculated by dividing the investment amount by the post-money valuation. Pre-money and post-money valuations are not interchangeable. A round described as a five million pound valuation is ambiguous and does not satisfy the documentation requirements of this Standard without specifying which valuation is meant.

MOST FAVOURED NATION CLAUSE: A provision in a SAFE that entitles the SAFE holder to the benefit of any more favourable terms issued to a subsequent SAFE investor before a priced round. A company that issues a subsequent SAFE at more favourable terms must notify existing SAFE holders who hold MFN rights and must reflect any resulting adjustments in the cap table.

PRO-RATA RIGHT: A contractual right held by an existing investor to participate in a future funding round at their pro-rata ownership percentage, maintaining their percentage ownership after the new

 

investment. Pro-rata rights do not convert to equity automatically; they are exercised by the holder at the time of the triggering round. The existence of unexercised pro-rata rights does not affect the cap table until they are exercised.

CONVERTIBLE NOTE: A debt instrument that converts to equity at a future event, typically a priced funding round. A convertible note carries an interest rate and a maturity date. At maturity, if conversion has not occurred, the note may be repayable as debt or may convert at a predetermined price depending on the instrument terms. The interest accrued on a convertible note increases the principal amount that converts, which increases dilution relative to the original principal. The cap table must reflect the accrued interest balance on all outstanding convertible notes.

**PRINCIPALS GOVERNING THIS SECTION**

Every outstanding SAFE and convertible note must be modeled to its conversion outcome before any priced funding round is initiated. A company that enters a priced round without having modeled the post-conversion cap table has not met the requirements of this Standard.

The conversion mechanics of each instrument must be modeled at the actual pre-money valuation of the triggering round, not at an assumed or aspirational valuation. Where the pre-money valuation is below the valuation cap of one or more outstanding instruments, each such instrument converts at the round price, not at the cap price. Where the pre-money valuation is above the cap, the instrument converts at the cap price. Both scenarios must be modeled before the round is closed.

Where multiple instruments with different caps and discount rates are outstanding simultaneously, the conversion of each instrument is calculated independently. The combined dilutive effect of all instruments converting simultaneously must be reflected in the post-conversion cap table before the round terms are agreed.

**COMPLIANCE CRITERIA**

**Level 1**

3.2.L1.1: The company maintains a schedule of all outstanding SAFEs and convertible notes listing for each instrument: the investor name; the principal amount; the valuation cap if applicable; the discount rate if applicable; the issuance date; and the conversion event conditions.

3.2.L1.2: The company has calculated the number of shares each outstanding SAFE and convertible note would produce if converted at the current most recent round price or at the most recent external valuation available.

3.2.L1.3: The principal balance of each outstanding convertible note, including accrued interest to the record date, is documented and reflected in the conversion calculation.

**Level 2**

3.2.L2.1: The company maintains a conversion model for all outstanding SAFEs and convertible notes that calculates the conversion price and resulting share count for each instrument at a range of pre-money valuations spanning the company's current assessed valuation and the valuation cap of each instrument.

3.2.L2.2: The conversion model reflects whether each instrument converts at the cap price or the discount price, calculating both and applying the lower price to determine the conversion outcome.

 

3.2.L2.3: The conversion model produces a post-conversion cap table for each modeled pre-money valuation scenario, showing the fully diluted ownership of all existing holders and all converting instruments after conversion and after the new investment.

3.2.L2.4: Where any outstanding SAFE carries a Most Favoured Nation clause, the company has assessed whether any subsequent SAFE issued after that instrument triggers the MFN provision and has documented the assessment.

3.2.L2.5: The conversion model is updated within fifteen working days of any new SAFE or convertible note issuance.

3.2.L2.6: The post-conversion cap table model is presented to the board or equivalent governing body before any priced funding round term sheet is executed.

**Level 3**

3.2.L3.1: The conversion model produces post-conversion cap tables across a range of at minimum five pre-money valuation scenarios, covering the range from fifty percent below to one hundred percent above the company's current internally assessed valuation.

3.2.L3.2: The conversion model integrates with the cap table maintained under Section 3.1 and the liquidation mechanics model maintained under Section 3.5, such that a change in any instrument term updates all three models without manual recalculation.

3.2.L3.3: The company maintains version-controlled records of the conversion model such that the model as it existed at the time of any priced funding round can be retrieved and compared to the actual post-conversion cap table to verify that conversion was executed in accordance with the instrument terms.

3.2.L3.4: The company reviews the conversion implications of all outstanding instruments quarterly and documents whether any material change in the company's valuation trajectory has altered the expected dilutive effect of any outstanding instrument relative to the prior quarter's assessment.

**BENCHMARKS**

SAFE instrument terms benchmarks by stage:

Pre-Revenue SAFEs: valuation caps at pre-revenue stage are determined by negotiation and reflect the assessed potential of the company rather than a financial metric. No quantitative benchmark is applicable. The company must document the basis on which the valuation cap was agreed for each instrument.

Early Revenue SAFEs: where revenue data exists, valuation caps are increasingly referenced to revenue multiples. The applicable multiple varies by company type and market conditions. Benchmarks will be stated in v1.0 as market data for 2025 and 2026 accumulates.

Discount rates: discount rates of ten to twenty-five percent are commonly observed in SAFE instruments. A discount rate above twenty-five percent is unusual and warrants review of whether the instrument terms reflect market norms for the company's stage and geography.

Convertible note terms: interest rates on convertible notes in early-stage markets range from two to eight percent per annum in most geographies. Maturity periods of twelve to twenty-four months are common.

The company must model the interest accrual effect on conversion shares for all outstanding convertible notes.

AI-Native company instruments: AI-Native companies have in certain cases issued instruments that combine equity SAFEs with rights to future token allocations or protocol governance rights. The equity conversion mechanics of any such instrument must be modeled under the same standards as a conventional SAFE. Token or protocol rights must be documented separately and are outside the scope of the equity cap table but must be disclosed in the instrument summary section required under Section 3.1.

**COMMON DEFICIENCIES**

CD 3.2.1: The company has issued three SAFEs over twenty months at valuation caps of three million, five million, and eight million pounds respectively. A priced seed round is agreed at a pre-money valuation of six million pounds. The first two SAFEs convert at their respective caps because the round price implies a per-share value above the cap. The third SAFE converts at the round price because the round is priced below its cap. The founder modeled only the scenario in which all SAFEs convert at their caps. The actual post-conversion dilution is materially different from the modeled dilution because the third SAFE converts at a lower price per share, producing more shares than the cap-based model assumed.

CD 3.2.2: The company has issued a SAFE with a twenty percent discount and a valuation cap. The conversion model calculates the cap-based price only. The priced round is conducted at a pre-money valuation that, after dividing by the fully diluted share count, implies a per-share price that produces a discount-based conversion price lower than the cap-based price. The instrument converts at the discount price, not the cap price, because the discount produces a lower price and therefore more shares for the holder. The company's modeled post-conversion cap table is incorrect.

CD 3.2.3: The company has an outstanding convertible note with a principal of two hundred thousand pounds issued twenty-two months ago at an annual interest rate of eight percent. The conversion model uses the original principal of two hundred thousand pounds as the conversion basis. Accrued interest of thirty-five thousand two hundred pounds has not been included. The note converts on the accumulated principal and interest balance of two hundred and thirty-five thousand two hundred pounds. The cap table understates the shares issued upon conversion.

CD 3.2.4: The company has three outstanding SAFEs, two of which carry Most Favoured Nation clauses. After the first two SAFEs were issued, a third SAFE was issued at a lower valuation cap. The MFN holders have not been notified. Their rights entitle them to adopt the lower cap. The cap table model does not reflect the potential exercise of MFN rights. If exercised, the dilution from the first two SAFEs is materially higher than the cap table reflects.

## SECTION 3.3: THE EQUITY COMPENSATION STANDARD

**PURPOSE**

The equity compensation standard governs the design, documentation, administration, and modeling of employee and advisor equity plans. Equity compensation is both a cash flow management tool and an ownership management tool. Its effect on the fully diluted cap table is permanent. Every grant made from an equity plan is a transfer of economic interest from existing holders to the recipient. The requirements of this section ensure that those transfers are documented, modeled, and disclosed with the same precision required of any other equity instrument.

**DEFINITIONS**

EQUITY COMPENSATION PLAN: A formally adopted plan under which a company grants options, restricted shares, restricted share units, or other equity-linked instruments to employees, advisors, and other service providers. The plan must be adopted by the board or equivalent governing body and must document the total number of shares authorised for issuance under the plan.

OPTION POOL: The shares reserved for issuance under an equity compensation plan that have not yet been granted. The option pool comprises both granted options and the ungranted reserve. The ungranted reserve must be included in the fully diluted share count and must be reflected in the cap table as an authorised but unissued block.

GRANT: The formal award of options or shares to a recipient under an equity compensation plan. A grant is not effective until documented in a written grant agreement executed by both the company and the recipient. An undocumented grant does not satisfy the requirements of this Standard.

VESTING SCHEDULE: The timeline over which a recipient's rights to exercise options or receive shares become effective. The vesting schedule must be documented in the grant agreement and must specify the vesting commencement date, the cliff period if any, and the vesting frequency after the cliff.

CLIFF: The minimum service period a recipient must complete before any portion of their grant vests. A one-year cliff means that no options vest until the recipient has completed twelve months of continuous service, at which point typically twenty-five percent of the total grant vests.

EXERCISE PRICE: The price per share at which an option holder may purchase shares upon exercise. The exercise price must be documented in the grant agreement. The exercise price is typically set at the fair market value of the shares on the grant date. An exercise price below fair market value on the grant date may create tax liabilities for the recipient in certain jurisdictions.

FAIR MARKET VALUE: The value per share on the grant date as determined by a formal valuation or, where a formal valuation is not available, by a documented management assessment of share value. The basis for any fair market value determination must be documented and retained.

GOOD LEAVER AND BAD LEAVER PROVISIONS: Contractual terms that determine what happens to unvested and vested options when a recipient leaves the company. Good leaver provisions typically allow departing recipients who leave under defined circumstances to retain or exercise some or all of their vested options. Bad leaver provisions typically result in forfeiture of unvested options and may affect vested options depending on the terms. These provisions must be documented in the equity plan and in each grant agreement.

FULLY LOADED COST OF EQUITY COMPENSATION: The economic cost to existing shareholders of each equity grant, calculated as the fully diluted ownership percentage transferred to the recipient multiplied by the current assessed enterprise value of the company. This cost is not recorded in the income statement in most jurisdictions under applicable accounting standards but must be reflected in the cap table and in the ownership dilution analysis.

OPTION POOL REFRESH: An increase in the number of shares authorised for issuance under an equity compensation plan, typically negotiated as a condition of a new funding round. An option pool refresh before a priced round increases the fully diluted share count before the new investment is made, which reduces the pre-money value per share and increases dilution for existing holders proportionally. The

 

refresh is taken from the pre-money value and is therefore borne by existing holders, not by the new investor.

**PRINCIPLES GOVERNING THIS SECTION**

The option pool refresh is a pre-money event. When a funding round requires an option pool refresh as a condition of investment, the refresh increases the fully diluted share count before the round price is set. The new investor's ownership percentage is calculated on the post-money valuation and the post-refresh fully diluted count. The dilutive effect of the refresh is therefore borne by the founders and existing common shareholders, not by the new investor. A company that models the option pool refresh as a post-money event in its cap table model misstates the dilutive effect on existing holders.

Every equity grant must be documented before it is included in the cap table. An oral promise of equity does not create a cap table entry. An unsigned grant agreement does not create a cap table entry. The cap table reflects only formally documented, executed grants.

**COMPLIANCE CRITERIA**

**Level 1**

3.3.L1.1: The company maintains a written equity compensation plan or equivalent document adopted by the board or governing body, stating the total shares authorised for issuance under the plan.

3.3.L1.2: The company maintains a schedule of all grants made under the equity compensation plan, listing for each grant: the recipient name; the number of options or shares granted; the exercise price; the grant date; and the vesting schedule.

3.3.L1.3: All grants in the schedule are supported by an executed grant agreement between the company and the recipient.

3.3.L1.4: The cap table reflects the total authorised option pool, distinguishing the granted portion from the ungranted reserve.

**Level 2**

3.3.L2.1: The company maintains a vesting schedule model for all outstanding grants that tracks, for each grant: the number of options vested to date; the number of options unvested; the next vesting date; and the number of options that will vest at each future vesting date through the end of the vesting schedule.

3.3.L2.2: The fair market value of shares on each grant date is documented with the basis for the determination stated.

3.3.L2.3: The good leaver and bad leaver provisions applicable to each grant are documented in the grant agreement and are summarised in the equity plan schedule.

3.3.L2.4: The company models the dilutive effect of any planned option pool refresh required by an anticipated funding round before that round is initiated, showing the pre-refresh and post-refresh fully diluted share count and the resulting change in ownership percentage for each existing holder.

3.3.L2.5: The company maintains a record of all options that have been exercised, forfeited, or lapsed, with the date and reason for each event.

3.3.L2.6: The ungranted option pool reserve is reviewed annually; where the reserve is insufficient to cover planned grants for the following twelve months, the company initiates the process to authorise an additional reserve before the existing reserve is exhausted.

**Level 3**

3.3.L3.1: The vesting schedule model projects, for each quarter in the following twelve months, the cumulative number of vested options outstanding and the potential dilutive effect if all vested options were exercised.

3.3.L3.2: The company models the economic cost of each grant cohort by calculating the fully diluted ownership percentage transferred at grant date multiplied by the company's current internally assessed enterprise value, and maintains this record for all grants made in the preceding twenty-four months.

3.3.L3.3: The equity compensation plan is reviewed by a qualified legal advisor at minimum every two years to assess whether the plan terms remain compliant with applicable tax and employment law in the jurisdictions where recipients are located.

3.3.L3.4: The company maintains a forward modeling scenario showing the fully diluted ownership structure after all planned grants over the next twelve months, after all vesting events over the next twelve months, and after the next anticipated option pool refresh.

**BENCHMARKS**

Option pool size benchmarks by stage:

Pre-Revenue to Early Revenue: total authorised option pool of ten to fifteen percent of fully diluted shares is typical. Pools below ten percent are commonly insufficient to cover grants required through the next funding round. Pools above twenty percent before any institutional investment dilute founder ownership without necessarily reflecting the grants required.

Growth Stage: total authorised option pool of fifteen to twenty percent of fully diluted shares on a post-round basis is commonly required by institutional investors as a condition of investment, reflecting the need to grant options to senior hires required to scale the business.

Scale Stage: the option pool is managed as a rolling reserve, with annual refreshes authorised as required to maintain sufficient ungranted shares for the following twelve months of planned grants.

Vesting schedule norms:

Four-year vesting with a one-year cliff is the most common vesting structure observed in venture-backed companies globally. Three-year vesting schedules are observed more frequently in European markets. Two-year vesting schedules are considered short and may be questioned by investors who prefer incentive alignment over longer periods.

Monthly vesting after the cliff is the standard frequency in most markets. Quarterly vesting is acceptable for advisor grants.

Exercise price benchmarks:

 

For markets where enterprise value is estimated at each grant date, the exercise price is set at the fair market value per common share on the grant date. For markets where an EMI valuation or equivalent is required by tax law, the exercise price must comply with applicable tax authority requirements.

AI-Native company equity structures: AI-Native companies have in certain cases structured advisor grants tied to research contributions or model performance milestones. Where vesting is conditional on a performance metric rather than time-based service, the grant must document the metric, the measurement methodology, and the dispute resolution process if the metric outcome is contested. Time-based and performance-based vesting conditions must not be combined in a single grant without documenting how each condition interacts with the other. Performance-conditioned grants present valuation and tax complexity that requires qualified legal and tax advice before grant.

**COMMON DEFICIENCIES**

CD 3.3.1: The company has made verbal equity commitments to two advisors and an early employee. None of the commitments are documented in executed grant agreements. None appear in the cap table. The company's founders believe the commitments exist and that the individuals expect to receive equity. The commitments are not reflected in the fully diluted share count. When the company initiates a funding round and the investors conduct cap table due diligence, the undocumented commitments surface. The resulting negotiation delays the round and produces an ownership structure that was not modeled in the pre-round cap table.

CD 3.3.2: The option pool was established at ten percent of fully diluted shares. Forty percent of the pool has been granted. At the current growth pace, the remaining ungranted reserve is insufficient to cover the planned grants for senior hires over the next twelve months. The company does not identify this insufficiency until it attempts to make a grant and discovers that the authorised reserve is exhausted. An emergency pool refresh is required outside of a funding round, which requires board approval and shareholder consent that was not anticipated.

CD 3.3.3: The company is in negotiation for a Series A funding round. The lead investor requires an option pool of twenty percent of post-money fully diluted shares as a condition of investment. The company's current pool is twelve percent of pre-money fully diluted shares. The company's founder models the pool refresh as a post-money event, concluding that the refresh does not affect their pre-money ownership. The pool refresh is a pre-money event that increases the fully diluted share count before the round price is determined. The founder's post-round ownership percentage is materially lower than the pre-money model implied because the refresh was taken from the pre-money value.

CD 3.3.4: An early employee was granted options eighteen months ago with a four-year vesting schedule and a one-year cliff. The employee leaves the company after fifteen months of service. The company's grant agreement does not specify the good leaver and bad leaver provisions clearly. A dispute arises about whether the employee is entitled to exercise the options vested after the cliff. The absence of clear provisions requires legal advice to resolve. The cap table cannot be updated until the dispute is resolved.

## SECTION 3.4: THE CAPITAL ALLOCATION STANDARD

**PURPOSE**

The capital allocation standard governs the documentation of how capital raised is deployed. Every funding round commits the company to an implied use of the capital raised. The standard requires that the use of proceeds is documented before the capital is raised and that the actual deployment of capital is

 

tracked against the documented plan. The failure to document capital allocation is a governance deficiency. The failure to track actual deployment against the plan is a financial management deficiency.

**DEFINITIONS**

USE OF PROCEEDS: A document or section of a financial model that states how the capital raised in a specific funding round will be deployed across functional categories over the intended deployment period.

DEPLOYMENT PERIOD: The period over which capital raised in a funding round is expected to be deployed, from the date of receipt to the date on which the company expects to have reached the milestone that justifies the subsequent funding round.

MILESTONE: A specific, measurable achievement that the company intends to reach by the end of the deployment period, which justifies the next funding round at an expected valuation. The milestone must be specific enough to be assessed objectively. Vague milestones such as "achieve product market fit" do not satisfy the requirements of this Standard.

CAPITAL EFFICIENCY: The amount of capital consumed to generate each unit of defined progress toward the milestone. Capital efficiency is measured as total capital deployed divided by the progress metric appropriate to the company's stage and type. For Recurring Revenue companies, capital efficiency is commonly measured as total capital deployed per unit of monthly recurring revenue added.

BURN MULTIPLE: Defined in Book 2, Section 2.5. Calculated as net cash consumed divided by net new annualised recurring revenue generated in the same period.

RUNWAY TO MILESTONE: The projected number of months of cash runway remaining after the defined milestone is reached at the current net burn rate. A company that reaches its milestone with less than three months of cash runway has insufficient time to prepare and close a subsequent funding round in most market conditions and does not have adequate capital efficiency in its deployment plan.

**PRINCIPLES GOVERNING THIS SECTION**

The use of proceeds must be prepared before a funding round closes. A use of proceeds document prepared after capital is received does not demonstrate that the deployment was planned; it demonstrates that it was reconstructed. The Standard requires that the plan precedes the deployment.

Capital allocation must be tracked against the plan at minimum quarterly. A company that has received capital but cannot demonstrate that the deployment is tracking against the plan has not met the requirements of this section.

**COMPLIANCE CRITERIA**

**Level 1**

3.4.L1.1: The company has documented the intended use of proceeds for each funding round completed, specifying the functional categories to which capital will be allocated, before or within thirty calendar days of the closing of the round.

3.4.L1.2: The company has identified the milestone it intends to reach by deploying the capital from each completed round, with the milestone stated in specific and measurable terms.

3.4.L1.3: The company tracks actual capital deployment against the documented plan at minimum quarterly.

**Level 2**

3.4.L2.1: The use of proceeds document specifies the planned capital allocation by functional category, including at minimum: product and engineering; sales and marketing; general and administrative; and cash reserve at end of deployment period.

3.4.L2.2: The use of proceeds document states the planned deployment period and the projected runway to milestone in months.

3.4.L2.3: The company maintains a capital deployment tracking model that compares actual spend by functional category to the planned allocation for each quarter of the deployment period, with variance commentary for any category where actual spend differs from plan by more than fifteen percent.

3.4.L2.4: The company reviews the use of proceeds plan at minimum semi-annually and documents whether the plan remains appropriate given actual progress toward the milestone.

3.4.L2.5: Where the company determines that a material reallocation of capital between functional categories is required, the reallocation is documented, the revised plan is presented to the board or equivalent governing body, and the rationale for the reallocation is recorded.

**Level 3**

3.4.L3.1: The capital deployment tracking model integrates with the three-statement model such that actual spend against plan is reflected in the cash flow statement and the cash runway calculation without manual recalculation.

3.4.L3.2: The company maintains a capital efficiency model that calculates, for each quarter, the capital deployed per unit of progress toward the milestone and tracks this ratio over the deployment period.

3.4.L3.3: The company models the runway to milestone under a scenario in which deployment proceeds as planned, a scenario in which deployment is twenty percent above plan in one or more categories, and a scenario in which the milestone timeline extends by six months, with the cash runway implications of each scenario documented.

3.4.L3.4: The board or equivalent governing body reviews the capital deployment tracking report and the capital efficiency model at minimum quarterly.

**BENCHMARKS**

Runway to milestone benchmarks:

At the point of a priced funding round, the deployment plan should produce a runway that reaches the defined milestone with at minimum six months of remaining cash runway at current burn, to allow time for the next fundraising process. The commonly observed benchmark for institutional investors is that a company should reach its next milestone with between six and nine months of runway remaining.

A deployment plan that reaches the milestone with less than three months of remaining runway creates material execution risk: any delay in milestone achievement or any slowdown in the subsequent fundraising process produces an existential cash constraint.

Use of proceeds allocation benchmarks by stage:

These benchmarks are directional indicators based on commonly observed allocations in venture-backed companies. They will be refined in v1.0.

- Pre-Revenue to Early Revenue rounds: forty to sixty percent of proceeds commonly allocated to product and engineering; fifteen to twenty-five percent to sales and marketing; fifteen to twenty-five percent to general and administrative and reserve.

- Growth Stage rounds: thirty to fifty percent commonly allocated to sales and marketing to accelerate customer acquisition; twenty to thirty percent to product and engineering; fifteen to twenty-five percent to general and administrative and reserve.

**COMMON DEFICIENCIES**

CD 3.4.1: The company raised a seed round twelve months ago. The use of proceeds was not formally documented before the round closed. Twelve months after the round, the company cannot demonstrate a clear connection between the capital deployed and the plan presented to investors, because no contemporaneous plan exists. The milestone was not defined in specific terms at the time of the raise and cannot be objectively assessed.

CD 3.4.2: The use of proceeds document allocates eighty percent of capital to product and engineering and twenty percent to general and administrative costs. Actual deployment over the first two quarters differs materially from the plan: forty percent has been allocated to sales and marketing, reducing the product and engineering allocation. The reallocation has not been documented or presented to the board. Investors who review the deployment tracking have no record of an approved reallocation.

CD 3.4.3: The company's deployment plan assumes the milestone will be reached in eighteen months. At the current burn rate, the plan reaches the milestone with two months of runway remaining. The company has not modeled the impact of a three-month delay in milestone achievement on the subsequent fundraising timeline. A three-month delay produces a cash constraint that requires a bridge round. The bridge round was not anticipated in the capital structure planning.

## SECTION 3.5: THE LIQUIDATION AND EXIT MECHANICS STANDARD

**PURPOSE**

The liquidation and exit mechanics standard governs the modeling and documentation of how proceeds are distributed to all holders of equity and equity-linked instruments in a liquidity event. A liquidity event includes an acquisition, a merger, a secondary transaction involving a material portion of the company's shares, a dissolution, or any other event that results in the distribution of value to equity holders. The purpose of this modeling is to allow every founder, employee, and investor to understand what they will receive under a range of exit scenarios before any such event occurs, not at the moment of execution.

**DEFINITIONS**

 

LIQUIDITY EVENT: An acquisition of the company, a merger in which the company is not the surviving entity, a dissolution, or any other transaction that results in the distribution of value to equity and equity-linked instrument holders.

LIQUIDATION PREFERENCE: The right of a preference shareholder to receive a defined amount from the proceeds of a liquidity event before any distribution is made to common shareholders. The liquidation preference is typically expressed as a multiple of the original investment amount. A one times liquidation preference entitles the holder to receive the original investment amount before common shareholders receive any proceeds.

LIQUIDATION PREFERENCE MULTIPLE: The multiple of the original investment that a preference shareholder is entitled to receive before common shareholders participate in proceeds. A two times liquidation preference multiple entitles the holder to receive twice the original investment before common shareholders participate.

PARTICIPATING PREFERENCE: A preference share structure in which the holder receives their liquidation preference amount and then participates alongside common shareholders in the remaining proceeds on an as-converted basis. Participating preference produces higher returns for preference holders than non-participating preference at the same exit valuation.

NON-PARTICIPATING PREFERENCE: A preference share structure in which the holder either receives their liquidation preference or converts to common shares and participates in the full proceeds, but not both. Non-participating preference holders compare the liquidation preference amount to the as-converted common proceeds and take the higher of the two.

PREFERENCE STACK: The total amount of liquidation preference that must be distributed to preference shareholders before any proceeds are available to common shareholders. The preference stack is calculated as the sum of liquidation preference multiples multiplied by original investment amounts across all preference share series. As more funding rounds occur at increasing investment amounts, the preference stack grows. At a modest exit valuation, the preference stack may consume all available proceeds.

WATERFALL ANALYSIS: A model that calculates the distribution of proceeds from a liquidity event to all holders of equity and equity-linked instruments, in the order of priority established by the company's share structure and investment agreements. The waterfall distributes proceeds sequentially: first to preference shareholders in accordance with their liquidation preferences, then to common shareholders and, if applicable, to participating preference shareholders in the remainder.

PARTICIPATION CAP: A limit on the total amount that a participating preference shareholder may receive from a liquidity event, typically expressed as a multiple of the original investment. Where a participation cap applies, the participating preference holder compares their capped participating proceeds to their as-converted common proceeds and takes the higher of the two.

ANTI-DILUTION PROTECTION: A provision in preference share terms that adjusts the conversion ratio of preference shares downward if the company subsequently raises capital at a lower price per share than the price paid by the preference shareholder. Anti-dilution protection transfers dilution from the protected investor to founders and common shareholders when a down round occurs. The two primary forms are broad-based weighted average anti-dilution and full ratchet anti-dilution.

BROAD-BASED WEIGHTED AVERAGE ANTI-DILUTION: An anti-dilution mechanism that adjusts the conversion price of preference shares based on a weighted average of the old price and the new lower

 

price, weighted by the number of shares outstanding at each price. This mechanism produces a moderate conversion ratio adjustment that is shared between the protected investor and existing holders.

FULL RATCHET ANTI-DILUTION: An anti-dilution mechanism that adjusts the conversion price of preference shares to the price per share in the new round, regardless of the size of the new round. Full ratchet anti-dilution produces the maximum possible adjustment in the investor's favour and can result in severe dilution for founders and common shareholders in a down round.

DRAG-ALONG RIGHT: A contractual right held by a defined majority of shareholders to compel all other shareholders to approve a liquidity event on the same terms. Drag-along rights are typically held by preference shareholders above a defined threshold and are designed to prevent a minority of common shareholders from blocking an acquisition that the majority has approved.

**PRINCIPLES GOVERNING THIS SECTION**

The waterfall analysis must be modeled for all current holders of equity and equity-linked instruments before any funding round closes, not after. Every new funding round that creates or extends a preference stack changes the distribution of proceeds in a liquidity event. The founders and existing common shareholders must understand the implications of the new stack before agreeing to the round terms.

Anti-dilution provisions must be modeled at the time of agreement, not at the time they may trigger. A preference shareholder who holds broad-based weighted average anti-dilution protection in a round that is priced above the next round will have their conversion ratio adjusted in the next round. The dilutive effect of that adjustment on common holders must be modeled when the protection is agreed, even though it may not trigger for years.

The waterfall analysis must cover a range of exit valuations, not a single assumed exit. Common shareholders often receive no proceeds in a modest exit because the preference stack absorbs all available proceeds. Founders must understand the exit valuation at which their common shares first generate positive proceeds, commonly referred to as the preference stack breakeven.

**COMPLIANCE CRITERIA**

**Level 1**

3.5.L1.1: The company has documented the liquidation preference terms, participation rights, and anti-dilution provisions for each series of preference shares outstanding.

3.5.L1.2: The company has calculated the total preference stack as of the record date, expressed as the total amount that must be distributed to preference shareholders before any proceeds are available to common shareholders.

3.5.L1.3: The company has identified the exit valuation at which common shareholders first receive positive proceeds from a liquidity event at the current preference stack.

**Level 2**

3.5.L2.1: The company maintains a waterfall analysis model that calculates the distribution of proceeds to all holders of equity and equity-linked instruments across a range of exit valuations spanning from the total preference stack amount to three times the company's current internally assessed enterprise value.

 

3.5.L2.2: The waterfall model reflects the correct order of distribution priority for each share class, including any participation rights and participation caps for each series of preference shares.

3.5.L2.3: The waterfall model reflects the conversion mechanics of all outstanding SAFEs and convertible notes, showing the post-conversion shares that would be distributed proceeds in each exit scenario.

3.5.L2.4: The waterfall model shows separately, for each exit valuation modeled, the total proceeds received by each of the following groups: each series of preference shareholders; all common shareholders in aggregate; all option holders in aggregate.

3.5.L2.5: The waterfall model is updated within fifteen working days of any change to the preference share structure, option pool, or outstanding convertible instruments.

3.5.L2.6: The waterfall model is presented to the board or equivalent governing body before any funding round term sheet is executed and before any acquisition discussion progresses to a term sheet stage.

**Level 3**

3.5.L3.1: The waterfall model covers a range of at minimum ten exit valuation scenarios, including the preference stack breakeven, the valuation at which each series of preference shares converts to as-converted common participation, and the valuation at which founder and employee common holdings produce returns comparable to the investor returns at each preference series conversion point.

3.5.L3.2: The waterfall model integrates with the cap table maintained under Section 3.1 such that a change in any instrument position updates the waterfall without manual recalculation.

3.5.L3.3: The waterfall model reflects the anti-dilution adjustment mechanism for each preference series, showing the conversion ratio adjustment that would result from a down round at a range of down-round prices and the resulting impact on founder and common shareholder proceeds.

3.5.L3.4: The company maintains a return model for each preference series that calculates the internal rate of return and multiple on invested capital for that series at each exit valuation modeled in the waterfall, allowing the company to assess whether exit terms would provide acceptable returns to each investor class.

**BENCHMARKS**

Preference stack benchmarks:

The preference stack grows with each funding round. At Growth Stage after a seed and Series A, the preference stack commonly represents a significant portion of the company's current assessed value. A preference stack exceeding one times the company's current internally assessed enterprise value means that at the current valuation, all exit proceeds would be absorbed by the preference stack and common shareholders would receive nothing.

Founders must model the preference stack as a percentage of the company's assessed value at each funding round and understand how the stack affects the exit valuation required to produce meaningful returns for common holders.

Liquidation preference multiple benchmarks:

 

One times non-participating preference is the most common structure in well-functioning early-stage markets. It is the structure most commonly recommended by investor associations and legal bodies in the UK and US markets.

Participating preference structures are less common in US markets but occur in European and Asian markets. Full ratchet anti-dilution is considered an aggressive term and is uncommon in competitive funding markets but may appear in down rounds or bridge rounds where the investor holds a stronger negotiating position.

Anti-dilution benchmarks:

Broad-based weighted average anti-dilution is the standard provision in most institutional investment documents in UK and US markets. Full ratchet anti-dilution is considered an aggressive term and is uncommon in competitive funding markets.

**COMMON DEFICIENCIES**

CD 3.5.1: The company has raised three funding rounds over four years. Each round included a one times participating preference with a three times participation cap. The preference stack now totals six million pounds across all three series. The company is in acquisition discussions at a headline valuation of nine million pounds. The founder models the waterfall on the basis that founders and employees will share in three million pounds of proceeds after the preference stack is cleared. The participating preference terms entitle each series to their preference amount and then to participate in the remaining proceeds alongside common shareholders up to the cap. The actual distribution to common shareholders after preference and participation is materially less than three million pounds. The founder has not modeled the participation mechanics.

CD 3.5.2: The company raised a Series A round at a price per share of two pounds. The Series A preference terms include broad-based weighted average anti-dilution protection. The company subsequently raises a bridge round at a price per share of one pound. The anti-dilution mechanism adjusts the conversion ratio of the Series A preference shares. The founders did not model the anti-dilution adjustment at the time of the Series A agreement. At the bridge round, the adjustment is calculated for the first time and produces a conversion ratio change that increases the number of common shares into which the Series A preference converts, diluting founder and employee ownership materially.

CD 3.5.3: The company is acquired at a valuation below the combined preference stack of its two investor series. All proceeds are distributed to preference shareholders under the liquidation preference. No proceeds reach common shareholders or option holders. Founders and employees receive nothing from the acquisition. The founders did not model this outcome before agreeing to the preference terms in each round because no waterfall analysis was maintained.

CD 3.5.4: The waterfall model was prepared at the time of the last funding round and has not been updated. Since that round, three SAFEs have been issued and a new option pool was authorised and partially granted. The waterfall model does not reflect the SAFEs or the new option grants. The preference stack and the common distribution calculations in the model are both incorrect. The board approved the last acquisition term sheet based on an outdated waterfall analysis.

**STAGE AND LEVEL APPLICABILITY**

 

The compliance level expectations for each section of Book 3 are established in the Financial Infrastructure Maturity Model in Book 0, Section 0.8. The operative mappings for this Book are as follows.

Section 3.1: Cap Table Standard
Pre-Incorporation: no requirement
Pre-Revenue: Level 1
Early Revenue: Level 2 from the date of issuance of the first convertible instrument
Growth Stage: Level 2
Scale Stage: Level 3

Section 3.2: SAFE and Convertible Instrument Standard
Pre-Incorporation: no requirement
Pre-Revenue: Level 1 from the date of issuance of the first SAFE or convertible note
Early Revenue: Level 2
Growth Stage: Level 2
Scale Stage: Level 3

Section 3.3: Equity Compensation Standard
Pre-Incorporation: no requirement
Pre-Revenue: Level 1 from the date of the first equity grant
Early Revenue: Level 1
Growth Stage: Level 2
Scale Stage: Level 2

Section 3.4: Capital Allocation Standard
Pre-Incorporation: no requirement
Pre-Revenue: Level 1 following the first funding round
Early Revenue: Level 1
Growth Stage: Level 2
Scale Stage: Level 2

Section 3.5: Liquidation and Exit Mechanics Standard
Pre-Incorporation: no requirement
Pre-Revenue: Level 1 from the date of issuance of the first preference share
Early Revenue: Level 1
Growth Stage: Level 2
Scale Stage: Level 3

Stage definitions are as established in Book 0, Section 0.5. The note from Book 0, Section 0.8 regarding capital structure requirements applying from the date of first instrument issuance governs the Early Revenue column for Sections 3.1 and 3.2.

Feedback on Book 3 may be submitted to standard@ffistandard.org with reference to the specific section and criterion number. Feedback received before the close of the beta review period will be considered in the preparation of v1.0.