

To help your readers navigate these high-stakes conversations, use the following scripts to push back on "red flags" while maintaining a professional partnership.

The "Clean Term Sheet" Negotiation Strategy

When negotiating, focus on the "**Rule of 3**": pick the three most critical issues to your long-term success and focus your energy there rather than arguing over every minor point.

1. Pushing Back on High Liquidation Preferences

The Red Flag: The investor asks for a **2x or 3x preference** instead of the standard 1x.

- **The Script:** *"I appreciate the downside protection you're looking for, but a 2x preference is significantly off-market for a Series A. Our goal is to align incentives so that everyone—founders, employees, and investors—wins together in a successful exit. A 1x non-participating preference is the industry standard and provides fair protection without penalizing the team that builds the value. Can we move to a standard 1x structure to keep our team fully incentivized for the long haul?"*

2. Removing "Participating" Status (The Double Dip)

The Red Flag: The term sheet specifies **Participating Preferred** shares.

- **The Script:** *"We've modeled out several exit scenarios, and the 'participating' feature creates a significant mismatch between ownership and payout. We want to ensure that our cap table remains clean for future rounds. As a compromise, would you consider **Non-Participating Preferred** shares, or perhaps a cap on the participation at **2x**? This ensures you get a great return while keeping the upside fair for the common shareholders."*

3. Swapping Full-Ratchet for Weighted Average

The Red Flag: The investor insists on **Full-Ratchet Anti-Dilution**.

- **The Script:** *"Full-ratchet protection can be extremely punishing for founders in a down-market and often makes it difficult to raise future capital because of the massive dilution it causes. We are comfortable with **Broad-Based Weighted Average** anti-dilution, which is the market standard. It provides you with protection against lower-priced rounds while reflecting the actual amount of capital raised, which is a much fairer way to share the risk."*

4. Challenging Excessive Control Rights

The Red Flag: The investor wants veto power over minor **day-to-day hiring or spending**.

- **The Script:** *"We value your strategic involvement, but these specific blocking rights over [hiring/minor budgets] could slow down our operational agility. We've worked hard to build a lean operation—supported by our **debt facilities with Esource Lending**—and we need the autonomy to execute our growth plan quickly. Can we limit these veto rights to 'extraordinary' events like a sale or a change in the business's fundamental nature?"*
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3 Golden Rules for the Negotiation

1. **Model Everything:** Don't guess. Use a spreadsheet to show the investor exactly how their proposed terms would affect the team in a \$10M, \$50M, or \$100M exit.
2. **Listen More (The 70/30 Rule):** Spend 70% of the time listening to *why* they want the term. If they are worried about risk, you can solve it with a different, less "red flag" term.
3. **Leverage Your "Esource" Advantage:** Remind them that your business is stable because you use **non-dilutive OPM** (like SBA loans) for your hardware and fixed costs. This proves you are a "safe bet" and don't need to accept "desperation" terms.