



EQUITY INVESTMENT FOR FIRST-TIME FOUNDERS

Everything you need to know before selling a share of your business
GUIDE 04

Understand equity investment before you agree to any of it.

Equity investment is one of the most powerful tools available to a growing business — but also one of the most misunderstood. For many first-time founders, the idea of selling a share of their business feels uncomfortable, even frightening. This guide replaces that discomfort with clarity: how equity works, what it means for you as a founder, how to negotiate a deal, and what the journey from first conversation to signed agreement looks like.

GUIDE 04 | Business Lincolnshire Finance Accelerator

Who this guide is for: founders considering equity investment for the first time, whether from angel investors, the Midlands Engine Investment Fund II (MEIF II), or a venture capital fund. Read Guide 01 (Business Finance Fundamentals) and Guide 03 (What Investors Look For) alongside this guide for the full picture.

YOU'LL GET

- The maths behind equity, valuation and dilution, worked through with real numbers
- What each type of equity investor offers and expects, from angels to MEIF II to VC
- A term sheet walkthrough, the full deal process, and a founder's glossary

START: Read this before your first conversation with an investor — not after you've received a term sheet.

SECTION 1 — WHAT EQUITY INVESTMENT ACTUALLY MEANS

Equity investment means selling a percentage ownership stake in your company in exchange for a cash investment. The investor becomes a part-owner — a shareholder — and shares in the future success (or failure) of the business. Unlike a loan, there are no monthly repayments. Unlike a grant, there are no conditions on what you do. But unlike both, you are no longer the sole owner of your business.

The fundamental trade-off

What you sell	What you gain
A percentage of your business — and therefore a share of all future profits and proceeds from any eventual sale. Some control: investors may want a board seat, information rights, and approval rights over major decisions. Time and energy: raising investment is a significant process that will distract you from running the business.	Cash to grow — without the obligation to repay regardless of how the business performs. Smart money: experienced investors often bring contacts, credibility, and strategic advice as well as capital. Validation: having a respected investor on board signals credibility to customers, partners, and future funders.

The key insight

Equity is not inherently better or worse than debt. It is the right tool when your growth ambitions require more capital than debt can provide, and when the potential value of the business at exit will far exceed the value of what you're selling today. A 70% share of a £5 million business is worth more than 100% of a £500,000 one.

SECTION 2 — EQUITY MECHANICS: THE MATHS YOU NEED TO KNOW

You do not need to be a mathematician to understand equity — but you do need to be comfortable with the core calculations. Investors will expect you to know these numbers fluently.

Pre-money and post-money valuation

Pre-money valuation	The agreed value of your business before the investment is made — what you and the investor negotiate.
Post-money valuation	The value of the business after the investment — pre-money valuation plus the amount invested.
Equity stake	The investor's percentage ownership: investment amount divided by post-money valuation.

Worked example: the basic equity calculation

Your business has an agreed pre-money valuation of £800,000. An investor agrees to invest £200,000.

Post-money valuation = £800,000 + £200,000 = £1,000,000

Investor equity stake = £200,000 ÷ £1,000,000 = 20% — your remaining stake = 80%

If the business is sold for £4,000,000 in five years: the investor's return = 20% × £4,000,000 = £800,000 (4× their investment). Your proceeds = 80% × £4,000,000 = £3,200,000.

Dilution — what it is and why it matters

Dilution is what happens to your ownership percentage each time new shares are issued. Every round of investment dilutes existing shareholders — including you. Dilution is not inherently bad: if the value of the business grows faster than your percentage shrinks, you end up with less of a bigger pie.

Worked example: dilution across two funding rounds

Round 1: you own 100%. You raise £150,000 at a £600,000 pre-money valuation → Investor A receives 20%. You now own 80%.

Round 2 (18 months later, business now worth £2,000,000 pre-money): you raise £400,000. Investor B receives 16.7%. Existing shares dilute proportionally → you now own 80% × (1 – 16.7%) = 66.7%; Investor A now owns 20% × (1 – 16.7%) = 16.7%.

But your 66.7% stake in a £2.4m post-money business = £1.6m in value. Your original 100% stake was worth £600,000 — you are significantly better off.

Anti-dilution provisions

Some investors ask for anti-dilution provisions — contractual protections that adjust their equity stake if the business raises money at a lower valuation in future (a "down round"). These can be complex and founder-unfriendly. Always take legal advice before agreeing to anti-dilution clauses.

Cap tables — tracking who owns what

A cap table (capitalisation table) is a record of every shareholder, how many shares they hold, and what percentage of the company that represents. Keeping an accurate cap table from day one is essential.

Shareholder	Shares held	% ownership	Value at £2m exit
Founder A	500,000	50%	£1,000,000
Founder B	300,000	30%	£600,000
Angel investor	150,000	15%	£300,000
Employee option pool	50,000	5%	£100,000
Total	1,000,000	100%	£2,000,000

Keep your cap table updated after every funding round, option grant, or share transfer. Your solicitor should also maintain a register of shareholders.

SECTION 3 — TYPES OF EQUITY INVESTOR

Not all equity investors are the same. Different investor types have different motivations, cheque sizes, involvement levels, and expectations. Choosing the right type for your stage is as important as the investment itself.

Angel investors

Who they are	High net worth individuals investing their own money — often successful entrepreneurs or senior executives.
Typical cheque size	£25,000–£250,000 per angel. Angels often co-invest in groups, pooling £250,000–£1,000,000+ per round.
Stage	Pre-revenue to early revenue. Comfortable with higher risk than institutional investors.
In Greater Lincolnshire	Lincolnshire Business Angels (LBA) is the regional network. The Accelerator can introduce you when you are ready.
Tax incentives	Most angel investments qualify for SEIS or EIS tax relief — significantly reducing the investor's effective risk.

Midlands Engine Investment Fund II (MEIF II)

What it is	A publicly backed fund covering Greater Lincolnshire and the wider Midlands, providing equity, debt, and mezzanine finance through specialist fund managers.
Typical investment	Equity: £50,000–£2,000,000+ depending on the fund manager and business stage.
Key advantage	Designed to fill market gaps. More patient capital than commercial VC. Can co-invest alongside angels.
How to access	Through the Accelerator — we have direct relationships with MEIF II fund managers and can make introductions.

Venture capital funds

Who they are	Professional investment funds managing capital on behalf of institutional investors.
Typical cheque size	£500,000–£10,000,000+. Most VCs have a minimum deal size — not relevant for very early-stage businesses.
When relevant	Usually your second or third round of investment, after establishing the business with angel or MEIF II funding.

Choosing the right investor type

Match your stage and ambition to the right investor type. Taking VC money too early can mean excessive dilution and pressure that does not suit your business. The Accelerator can help you identify the most appropriate investor type for your current stage.

SECTION 4 — EIS AND SEIS: MAKING YOUR DEAL MORE ATTRACTIVE

The Enterprise Investment Scheme (EIS) and Seed Enterprise Investment Scheme (SEIS) are UK government tax relief schemes that make equity investment in qualifying companies significantly more attractive to investors. Understanding whether your business qualifies is one of the most valuable things you can do before approaching investors.

	SEIS	EIS
Full name	Seed Enterprise Investment Scheme	Enterprise Investment Scheme
Company age	Under 3 years trading	Under 7 years from first commercial sale (10 for knowledge-intensive)
Max company size	Under £350,000 raised via SEIS	Under £12m gross assets; under 250 employees
Max investment	£150,000 total via SEIS	£12m lifetime (£5m per year)
Income tax relief	50% of investment	30% of investment
Capital gains relief	Gains exempt if shares held 3+ years	Gains exempt if shares held 3+ years
Effective investor cost	£100k investment costs effectively £50k after relief	£100k investment costs effectively £70k after relief

How to obtain EIS / SEIS advance assurance

- **1. Check basic eligibility** — UK-incorporated, trading, below the relevant size thresholds. Certain sectors are excluded (financial services, property development, energy generation, others).
- **2. Prepare your application** — submit form SEIS1 or EIS1 to HMRC with your business plan, company documents, and details of the proposed share issue. Applications can take 4–8 weeks.
- **3. Receive advance assurance** — HMRC confirms in writing whether your company appears to qualify. Share this with investors — it significantly accelerates negotiations.
- **4. Issue compliant shares** — your solicitor handles this when you close the investment. HMRC then issues EIS3 or SEIS3 certificates for investors to claim relief.

Take professional advice

EIS and SEIS rules are complex and change periodically. Always take advice from a qualified accountant or tax specialist before submitting an Advance Assurance application. Getting this wrong can invalidate the relief for your investors.

SECTION 5 — THE TERM SHEET: WHAT TO EXPECT AND NEGOTIATE

A term sheet is a non-binding document that sets out the proposed terms of an investment before full legal documentation is prepared. Get it right and the rest of the process is largely administrative; get it wrong and you may find yourself locked into terms that harm you for years.

Valuation and economics

Pre-money valuation	The agreed value before investment. Everything else flows from this — negotiate it carefully and be ready to justify it.
Share class	Investors often receive preference shares carrying different rights to founder ordinary shares. Understand what's attached before agreeing.
Liquidation preference	Investors get their money back (or a multiple) before ordinary shareholders in a sale or liquidation. A 1× non-participating preference is standard and fair; anything higher disadvantages founders.
Anti-dilution	"Broad-based weighted average" is the most founder-friendly version. Full ratchet is very founder-unfriendly — avoid it.
Option pool	Investors often require an option pool created (or expanded) before their investment, which dilutes founders before the round closes.

Control and governance

Board composition	A standard early-stage board might be 2 founders, 1 investor, 1 independent. Multiple investor seats can start to outvote founders.
Reserved matters	Decisions requiring investor approval even as a minority shareholder — issuing shares, taking on debt, key hires, selling assets. Review carefully.
Information rights	Regular financial reporting — monthly/quarterly management accounts, annual audited accounts. Reasonable and standard.
Drag / tag-along rights	If majority shareholders sell, they can drag minority shareholders along on the same terms — usually balanced by tag-along rights protecting founders too.
Pre-emption rights	Investors get first right of refusal to invest in future rounds, maintaining their percentage. Standard and reasonable.

What to negotiate hardest

- Pre-money valuation — the most important number in the deal
- Liquidation preference — ensure it is 1× non-participating at most
- Board composition — protect your ability to run the company day-to-day
- Reserved matters list — negotiate this to be as narrow as possible
- Anti-dilution terms — push for broad-based weighted average, not full ratchet
- Option pool timing — ensure it is created post-money, not pre-money

Always take independent legal advice

Never sign a term sheet — even a "non-binding" one — without independent legal advice from a solicitor experienced in venture transactions. Budget at least £2,000–£5,000 for legal fees on a first round.

SECTION 6 — THE INVESTMENT PROCESS: FIRST CONTACT TO SIGNED DEAL

Raising equity investment for the first time takes longer than almost every founder expects. Understanding the typical process helps you plan, manage your time, and avoid the mistakes that derail deals.

#	Stage	Typical time	What happens
1	Initial approach & screening	4–6 weeks	You submit an executive summary or pitch deck. Most pitches are rejected at this stage — expect a very low conversion rate.
2	First meeting / pitch	1–2 meetings	A 45–60 minute meeting presenting your business and answering questions. The investor is assessing you as much as the business.
3	Deeper diligence	2–6 weeks	The investor asks for financials, customer references, market data, team backgrounds. Can feel slow — do not panic.
4	Term sheet	1–3 weeks	A significant milestone signalling genuine intent. Negotiate carefully, then move quickly — deals can fall apart if they drag.
5	Legal documentation	4–8 weeks	Solicitors prepare the full Shareholders' Agreement and associated documents. This is where costs mount — budget for delays.
6	Completion	Completion day	Shares are issued, money is transferred, and you have your investors.

Typical timeline

From first contact to money in the bank, expect 3–6 months for an angel round and 4–9 months for an institutional round. Build fundraising time into your plan and make sure you have enough cash runway to avoid rushing.

SECTION 7 — COMMON MISTAKES FIRST-TIME FOUNDERS MAKE

Most of the mistakes that derail equity fundraising are avoidable.

Common mistake	How to avoid it
Overvaluing the business	Be realistic — an inflated valuation makes closing harder and sets you up for a painful down round.
Approaching investors before ready	Investors talk to each other. Complete the Self-Assessment and get your financials and pitch in order first.
Not understanding the term sheet	"Non-binding" does not mean "doesn't matter". Get legal advice before signing.
Taking the first offer	Resist signing immediately — even one other interested investor creates leverage.
Ignoring dilution in future rounds	Model your cap table through 2–3 rounds. Plan for dilution from the start.
Choosing investors on price alone	They'll be on your cap table for years — choose someone you can work with and trust.
Underestimating the time cost	Fundraising consumes 30–50% of a founder's time during the process.
Not checking EIS/SEIS early	Check eligibility and apply for Advance Assurance before your first investor meeting.
Mixing personal and company finances	Clean company financials are essential — sort this with your accountant first.
No shareholders' agreement between co-founders	Formalise equity splits, roles, vesting, and leaver terms before raising external investment.

SECTION 8 — AFTER THE INVESTMENT: LIFE WITH INVESTORS

Closing an investment round is a milestone — but it is also the start of a new relationship. Understanding what good investor relations look like helps you manage that relationship and build trust that makes future fundraising easier.

Investor relations	The basics
Regular reporting	Monthly or quarterly management accounts, plus a brief narrative update. Keep it concise and honest — surprises are far worse than bad news shared early.
Board meetings	Most agreements require quarterly board meetings. Come prepared with a clear agenda and an honest assessment of progress.
Milestone transparency	If you won't hit an agreed milestone, tell investors early — hiding problems destroys trust.
Future fundraising	Keep investors informed of your plans — they may want to participate and can help with warm introductions.
Exit conversations	Engage openly as the business matures — a misaligned view on exit timing causes significant tension.

When investors and founders disagree

- Share bad news early — investors are far more forgiving of problems they hear about early than surprises
- Separate operational disagreements from strategic ones — the former are usually easier to resolve
- Use your board chair or lead investor as a sounding board before conflicts escalate
- Refer to the Shareholders' Agreement — it exists to resolve disputes
- If the relationship breaks down seriously, take legal advice early — do not let it fester

Building towards the next round

- Keep your cap table up to date at all times
- Maintain clean, timely management accounts every month, without exception
- Hit your milestones, or update your plan transparently when you do not
- Build relationships with potential future investors well before you need them
- Document everything — board minutes, shareholder resolutions, option grants — rigorously

SECTION 9 — EQUITY INVESTMENT GLOSSARY

Terms you'll hear throughout the equity investment process — refer back here whenever a conversation gets technical.

Anti-dilution	Contractual protection for investors that adjusts their equity if the company raises money at a lower valuation (down round).	ARR	Annual Recurring Revenue — the annualised value of recurring subscription or contract revenue.
Board observer	A non-voting attendee at board meetings, often granted to investors without a formal board seat.	Cap table	Capitalisation table — a record of all shareholders, their share counts, and percentage ownership.
Convertible note	A short-term debt instrument that converts into equity at a future funding round, typically at a discount.	Dilution	The reduction in an existing shareholder's percentage ownership when new shares are issued.
Down round	A funding round at a lower valuation than the previous round — damaging to founder credibility.	Drag-along rights	The right of majority shareholders to require minority shareholders to sell on the same terms.
Due diligence	The investor's process of verifying claims about the business before completing an investment.	EIS	Enterprise Investment Scheme — UK government tax relief for investors in qualifying companies over 3 years old.
Equity stake	The percentage of a company owned by a shareholder.	Exit	The event through which investors realise a return — typically a trade sale, management buyout, or IPO.
Information rights	Contractual right of investors to receive financial and operational data regularly.	Lead investor	The primary investor in a round who sets the terms and often takes a board seat.
Liquidation preference	The right of investors to a specified return before ordinary shareholders in an exit or liquidation.	MBO	Management Buyout — where the management team buys out investors' stake, often a route to exit.
Option pool	A reserved percentage of shares set aside for future grants to employees and advisors.	Post-money valuation	The value of a company immediately after an investment — pre-money plus the investment amount.
Pre-emption rights	The right of existing shareholders to invest in future rounds before new investors.	Pre-money valuation	The agreed value of a company before an investment is made.
Reserved matters	Decisions that require investor approval regardless of their percentage ownership.	SEIS	Seed Enterprise Investment Scheme — UK tax relief for investors in very early-stage qualifying companies.
SHA	Shareholders' Agreement — the legally binding contract between shareholders governing how the company is run.	Tag-along rights	The right of minority shareholders to sell on the same terms as majority shareholders in any sale.
Term sheet	A non-binding document summarising proposed investment terms, agreed before full legal documentation.	Vesting	A schedule over which founders or employees earn their equity — typically 4 years with a 1-year cliff.
Warrant	A right to purchase shares at a specified price at a future date — sometimes granted alongside a loan.		

SECTION 10 — YOUR NEXT STEPS

If this guide has clarified what equity investment involves and you want to explore it further, here is a practical action plan.

Priority	Action
First	Complete the Investment Readiness Self-Assessment (GLBFA-TOOL-001) to understand where you stand across all six investment readiness dimensions.
Second	Book a fully funded Funding Diagnostic Session with the Accelerator. An adviser will review your situation, confirm whether equity is the right route, and build a prioritised action plan.
Third	Check EIS/SEIS eligibility early — ideally before approaching any investors. Take advice from a qualified accountant or tax specialist.
Fourth	Build your financial forecast using the Accelerator's free 3-year Excel template (GLBFA-XLS-001). Investors will expect this.
Fifth	Read Guide 03 (What Investors Look For) and build your pitch deck using the Accelerator's template (GLBFA-PPT-001).
Sixth	When ready, speak to the Accelerator about an introduction to Lincolnshire Business Angels or the relevant MEIF II fund manager.

Accelerator resources relevant to this guide

Reference	Resource
GLBFA-GUIDE-001	Business Finance Fundamentals — the broader context of debt, equity, and grants
GLBFA-GUIDE-003	What Investors Look For — the six dimensions investors assess
GLBFA-GUIDE-005	Working with Business Angels — the angel investment process in detail
GLBFA-TOOL-001	Investment Readiness Self-Assessment — 25-criterion RAG self-assessment
GLBFA-XLS-001	3-Year Financial Forecast Model — free Excel template
GLBFA-PPT-001	Investment Pitch Deck Template — 15-slide PowerPoint template

This guide is for information only and does not constitute financial or legal advice. Always take independent professional advice before entering into any investment agreement.

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The Business Lincolnshire Finance Accelerator gives you the knowledge, tools and expert support to understand your options and prepare to access funding at the right time, in the right way.

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