How VCs Use SPVs

Assure Analytics Report

October 2022

"The private markets are increasingly favoring speed, transparency, and flexibility. VC firms are recognizing this evolution, and are changing how they raise, manage, and deploy assets. The Special Purpose Vehicle is a key part of enabling this and is quickly become a fundamental component of today's VC Legal Stack.

But we're still in the early innings of SPV adoption. We've published this report to help investors better understand how VCs work with SPVs. The research is another step forward as Assure builds the world's leading private transactions platform."

— Jeremy Neilson
CEO, Assure

For more information, please contact:
Mack Kolarich, VP Assure Analytics
mack.kolarich@assure.co

I. An Intro To SPVs for VCs

VCs strive to back the world's greatest innovators, but haven't always innovated themselves. The venture industry – from an operational and back office standpoint – has historically been quite stagnant. Yet the last decade has ushered in increasingly rapid change. Around a decade ago, VCs began to proactively design and optimize their 'VC Tech Stack.' Gradually, they also began to re-engineer their administration, legal, and fundraising strategies: some high profile firms such as Sequoia and A16Z have made recent headlines by restructuring into one giant feeder-fund to fund all underlying funds and re-orienting the firm's business model as a Registered Investment Advisor (RIA), respectively.

Many more VC firms have moved beyond a pure flagship fund strategy to use other investment vehicles such as opportunity funds and special purpose vehicles. These vehicles enable General Partners (GPs) to be more flexible – they can fund and fundraise differently, using the right investment structure for the right deal and the right roster of Limited Partners (LPs).

Due in large part to their flexibility, efficiency, and affordability, SPVs are becoming a core component of the venture capital investment toolkit. SPVs have many uses, but most commonly they help GPs to:

- Capture pro rata and maintain ownership in follow-on rounds,
- Offer co-investment opportunities to interested LPs (of keen interest to family offices),
- Invest in promising deals that are outside of a fund's thesis area or terms,
- Court prospective LPs for future funds,
- Establish an investment track record (for aspiring VCs),
- Accelerate the growth of their AUM,
- All while generating carry for the managers, if they so choose.

An SPV can be formed, funded, and deployed in weeks – and oftentimes days – letting VCs get shovels in the ground fast. And with a firm like Assure, end-to-end administrative support exists after the wire through our in-house tax experts and fund administration solutions (we prepared and delivered over 100,000 K-1s this year).

The result of this convenience is growth in SPV usage across venture capital firms. At least 20% of U.S. VCs who raised a flagship fund since the beginning of 2021 have also leveraged an SPV. Increasingly, the Assure team has seen VCs explicitly call out SPVs in their fundraising presentations as part of an investment strategy – something unheard of just a couple years ago.

For VCs who use them, SPVs typically boost a firm's overall AUM by 11%. VC SPVs tend to raise 5% to 25% of the capital raised by each flagship fund, and frequently occur towards the end of a flagship fund's lifecycle.

That said, we know many investors are still relatively new to SPVs, and experienced SPV organizers value insights on how their peers utilize these investment vehicles as well as how they compare to the market. Accordingly, this brief explores topics around management fees, carry, SPV use versus other vehicles, capital raises, manager backgrounds, LP participation, and much more.

II. Methodology

This report analyzes U.S. SPVs raised by VC firms between January 2021 and June 2022. It's based on data generated by Assure and is supplemented, when possible, with independent VC data compiled by Assure Analytics (*FKA* DifferentFunds). This VC data combines public Form D filings with news articles, press releases, and other online sources to fully cover the fundraising activity of all U.S. venture capital firms. In total, the data analyzed for this report includes over 500 SPVs raised by over 250 VC firms.

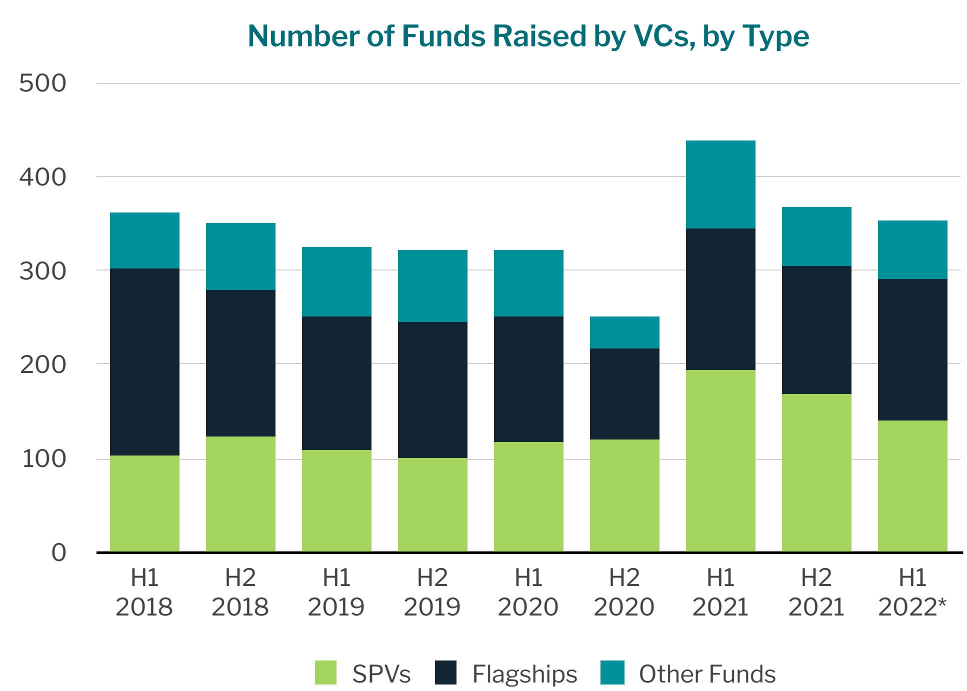
Much of the analysis compares VC data to SPV market norms. These market-wide norms are based on over 4,000 SPVs raised by more than 750 organizers between January 2021 and June 2022, and represent the findings published earlier this year in the State of the SPV report.

III. Growing Adoption of SPVs by VCs

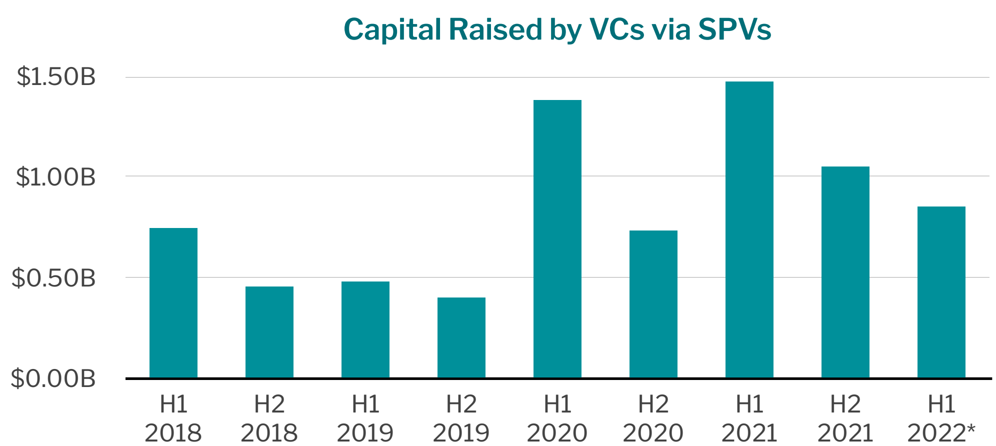
In the last several years, VCs' use of SPVs has trended upwards.

The number of SPVs raised by VCs doubled, growing from roughly 100 in the first half of 2018 to nearly 200 in the first half of 2021. Although there's been a modest decline in activity since then (corresponding with declines across the startup investing and venture ecosystems), more SPVs were formed in 1H 2022 than any half-year period before 2021.

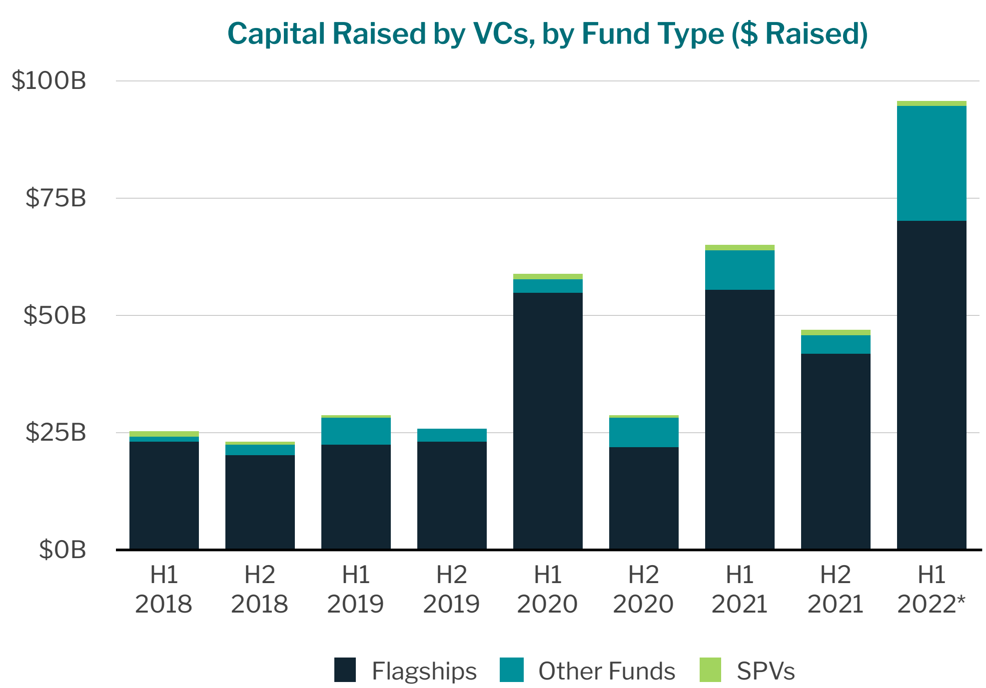
SPVs have accounted for an increasing share of all vehicles raised by VCs . Whereas SPVs made up around 30% of the fund count for VCs four years ago, today they account for over 40%.



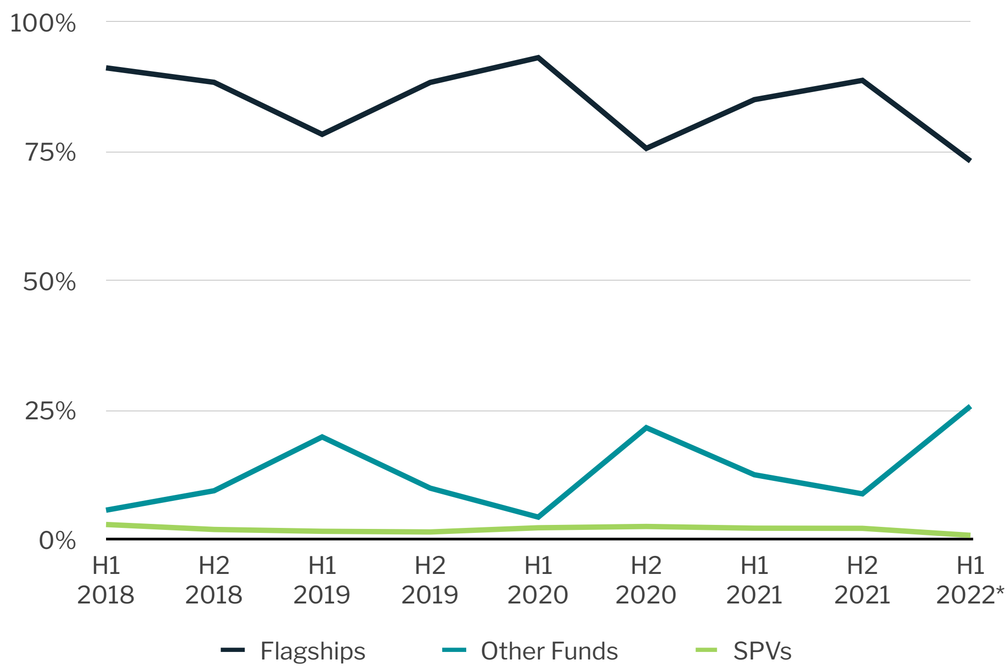
The amount of capital raised by VCs via SPVs has also grown substantially, with a particularly prominent boom in the first half of 2021. In that period SPVs collected nearly $1.5B, more than the amount raised in all of 2018. However, these numbers have since started to decline, along with a broader slowdown in private market transactions.



Although the amount of capital raised through SPVs trended upwards over the last several years, SPVs remained stable as a percent of all VC dollars. Standard flagship funds comprised 80% to 90% of VC assets, while SPVs contributed 2% to 3% in any given year. Of note, SPV's contribution to VC assets fell to less than 1% in the first half of 2022, as other fund types (primarily opportunity/growth funds) exploded in this period. Whereas in past periods this other category of funds typically accounted for 10% of AUM raised, so far in 2022 they've swelled to 23%.



Capital Raised by VCs, by Fund Type (% of Total Raised)



IV. Characteristics of VCs That Use SPVs

Fund Number

SPVs are used by VCs across the fund tenure spectrum: everyone from 1st-time funds to firms on Fund V leverage SPVs.

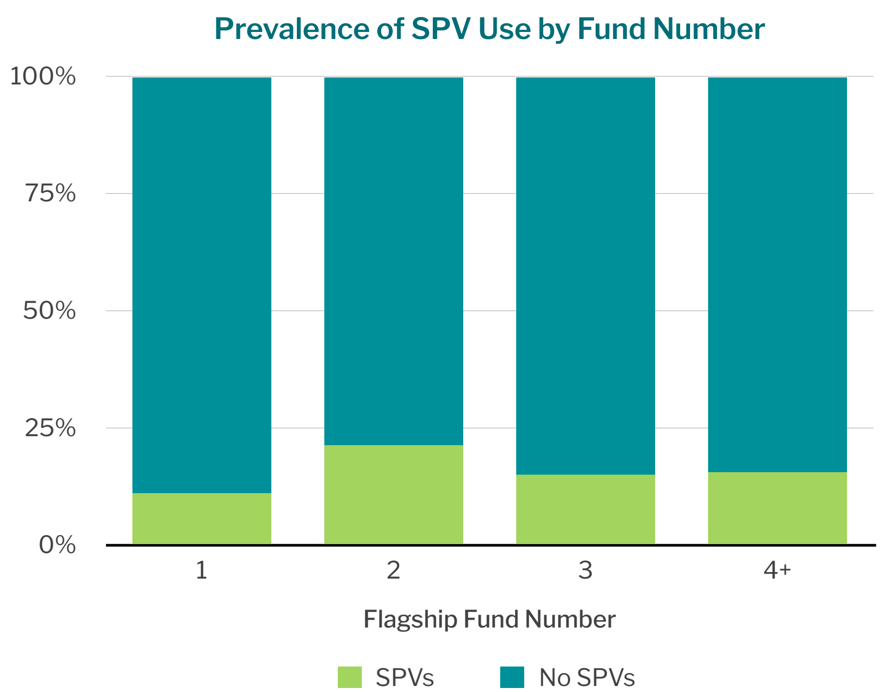
However, VCs on their second flagship fund stand out for exceptionally frequent SPV use. Whereas 15% of U.S. VCs on Fund III or later have raised an SPV, more than a fifth of those on Fund II have done so. Conversely, just 10% of VCs on Fund I have an SPV.

A few traits of SPVs and VC firms help explain these differences:

1. SPVs are frequently used by venture capital firms to fill pro rata and participate in follow-on rounds for high-performing portfolio companies: since Fund Is are newer firms, they're less likely to have identified the winners from their first flagship funds and consequently don't yet have large follow-on rounds in which to participate. Fund II's, meanwhile, will have investments from several years ago (likely through their debut funds) that have matured to later stage rounds and require extra capital infusions. Given the funds of emerging managers are typically smaller vehicles, they may not have sufficient reserves out of a flagship fund to participate in the largest and most promising rounds; particularly if one or two portfolio companies do exceptionally well and out-grow any follow-on reserves.

2. Fund III is frequently cited as the toughest flagship fund to raise: when fundraising for a third flagship vehicle, VCs on Fund II likely won't have had an exit to boost their DVPI (distributed value to paid-in capital) or multiples. Without this concrete performance, LPs can be more hesitant to re-invest in a third flagship fund. As a result, Fund IIs may use SPVs to not only participate in the later stage rounds of high-performing portfolio companies, but to fill the gap in capital they experience with prolonged fundraising periods for their third flagship vehicle. SPVs may help extend the capital runaway for Fund IIs and allow them to continue making investments until closing Fund III.

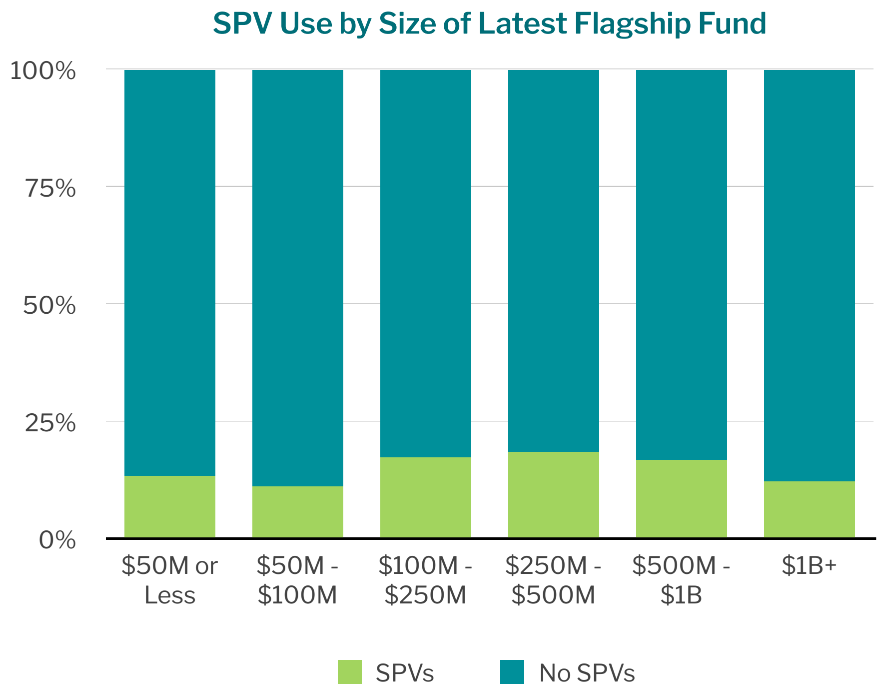
3. The last five years saw the fundraising cadence of VC firms shrink to a point where some VCs would raise new flagship funds on an almost annual basis. We are now returning to the historical norm, with firms raising a flagship fund every 2 to 3 years. As a result, this means there's greater need for bridge capital to support portfolio growth when reserves are exhausted.



Fund Size

Similarly to fund number, **VCs of all sizes use SPVs**. *Whether their latest flagship fund collected just $25M or over $1B, about 10% to 20% of firms have raised at least one SPV.*

Interestingly, VCs with smaller flagship funds are less likely to have used an SPV than those with larger flagships. This is likely a function of the same mechanisms that result in Fund Is having lower SPV use rates: smaller funds (sub-$50M in particular) are disproportionately debut funds and so are less likely to have portfolio companies entering mature, later stage rounds that require the VC to raise additional capital.

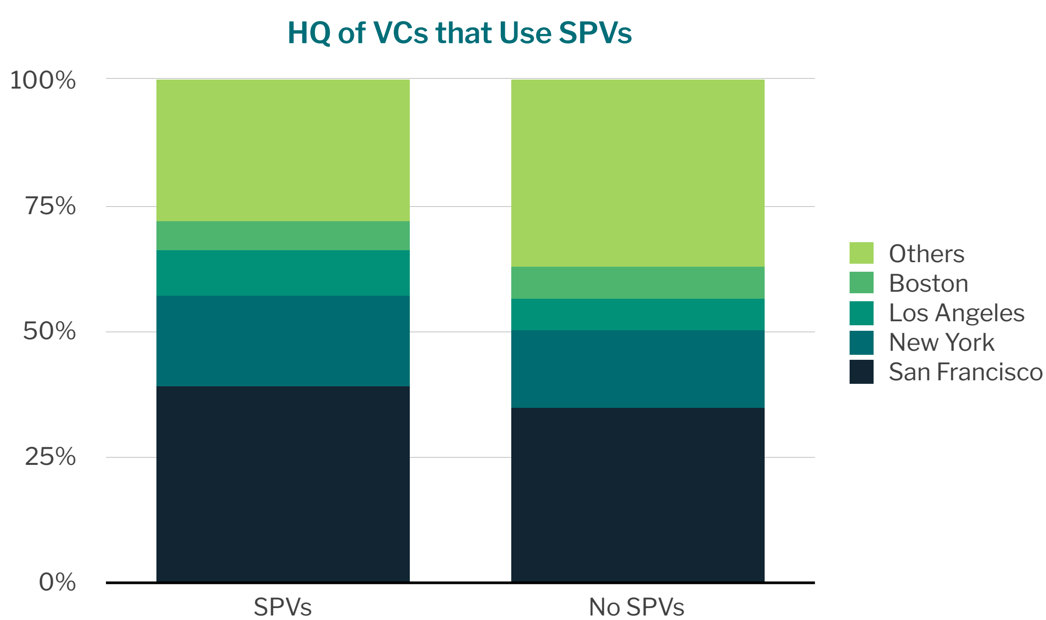


Headquarters

Venture capital firms using SPVs are more likely to be headquartered in the top metro areas for VC.

Whereas 66% of VCs with an SPV are headquartered in the San Francisco, New York, or Los Angeles metro areas, that figure is ten percentage points lower (56%) for VCs without SPVs.

Though purely speculation, this difference may result from differences in typical startup valuations in these top regions. If startups in these big VC geographies are more likely to see greater round size growth as they mature from seed to later stages, they could also be more likely to outgrow the



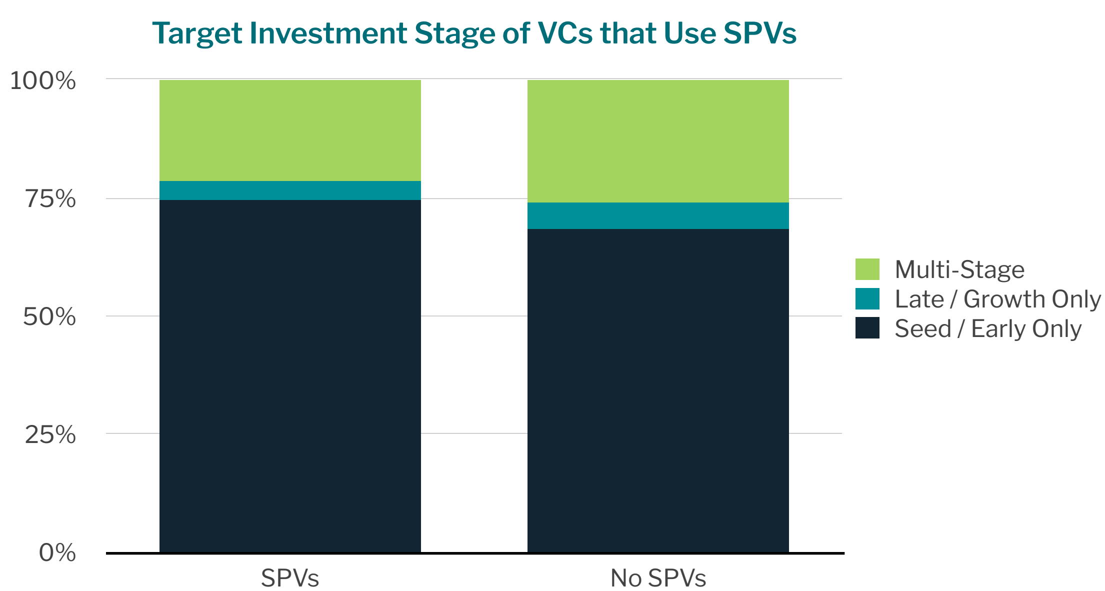
flagship funds of VCs in these regions. This could push these VCs to turn to capital supplements (in the form of SPVs) because they're investing in more competitive areas. Alternatively, VCs in the major venture metros may just be earlier in the adoption curve of SPV use as a core part of their investment strategy.

Target Stages

VCs using SPVs are more likely to target only seed or early stages for initial investments. Three-quarters of firms with at least one SPV target exclusively early stages, compared to 68% for those without SPVs.

This difference may result from multi-stage or late-stage VC firms being inherently more growth-oriented in the startups they back, since they're making initial investments closer to a liquidity event when larger, follow-on rounds are on the near-term horizon. This could push these VCs to set aside a greater portion of their flagship fund in reserves and consequently not turn to SPVs as frequently. Also, VCs making initial investments at later or growth stages tend to be larger firms with an already greater capital pool to inject into their portfolio.

VCs targeting earlier stages, in turn, might be more likely to see successful portfolio companies outgrow the seed-stage fund they originally invested through, making this class of firms more likely to supplement flagship capital with SPVs.

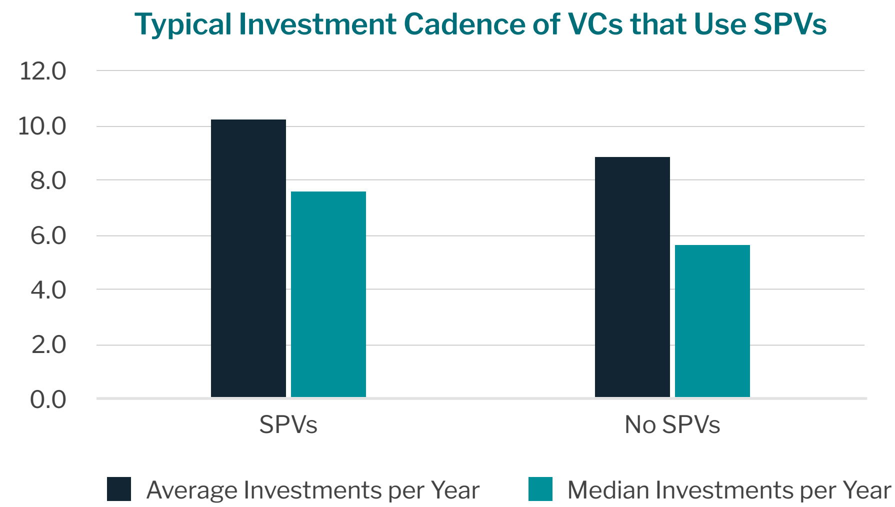


Investment Pace

Venture capital firms with SPVs tend to make more investments per year than those without SPVs.

The average VC with at least one SPV invests in 10.4 new startups per year, compared to 8.9 among VCs without SPVs. Similarly, the median VC with SPVs adds 7.6 startups to its portfolio each year, compared to 5.7 for those without SPVs.

Thus, VCs leveraging SPVs appear to invest at a quicker pace, and are perhaps more likely to take a diversification approach to venture capital (since they're creating a larger portfolio each year than those without SPVs).



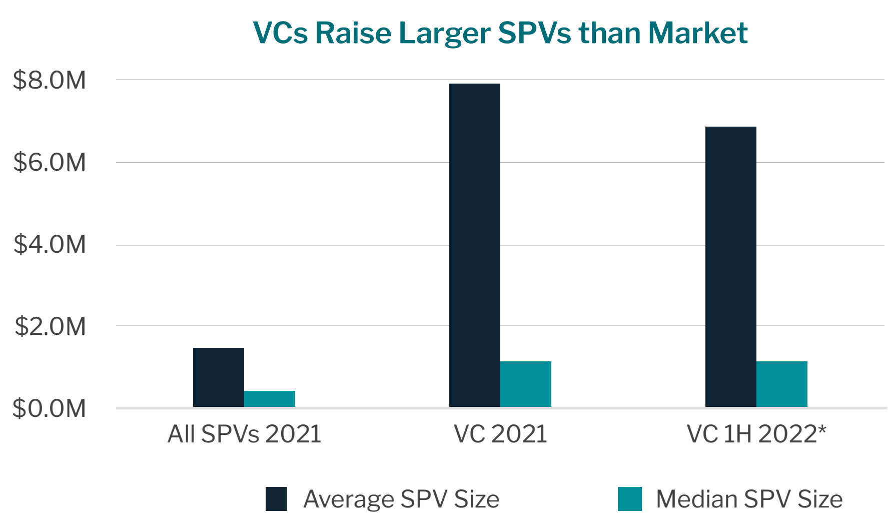
V. How VCs Use SPVs

Capital Raised & Investor Participation

In 2021, the average VC SPV collected $7.9M, with the median raising $1.1M. This represented a significant premium over SPV market norms more broadly (where SPVs had an average and median size of $1.5M and $422K, respectively). (See how select other organizers use SPVs here).

However, first half figures for 2022 pointed to a moderate decline in SPV sizes for VCs. Through June, the average VC SPV raised just $6.9M with a median of $1M.

Given that SPVs are frequently used by VCs as pro rata investment vehicles, this 10% to 12.5% drop-off in SPV size may have resulted from declining startup valuations in the first half of the year.

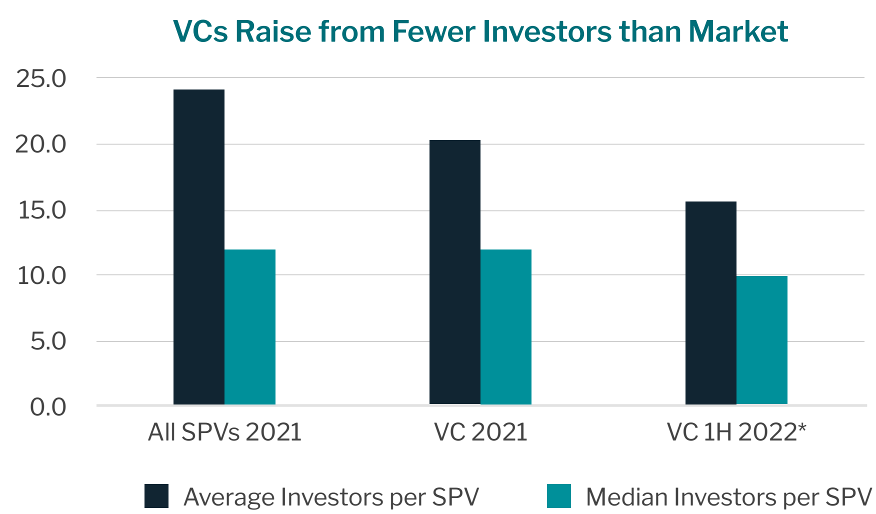


Although VCs raise larger SPVs than other organizer types, the number of investors they're pooling capital from is, if anything, smaller than market norms.

Whereas the average SPV raised from 24 investors in 2021, the average VC SPV raised from 20. (Both VC SPVs and SPVs more broadly had a median of 12 investors.)

So far in 2022, the number of participating investors contracted modestly: the average SPV had 15 investors and the median had 9.5 (representing a 20-25% drop). This modest decline correlates with overall market activity. While many investors are still participating in the private markets (in part due to the increasingly investor-friendly environment, see below), some are moderating their participation and others are staying on the sidelines. The reasons for this vary, with certain investors facing capital constraints, some waiting for valuations to settle, and others looking to rebalance to other asset classes (such as private credit).

In tandem, investor retention in VC SPVs has also declined in the first half of 2022: while the norm in 2021 was for a quarter of investors to return and back a VC's subsequent SPV, that investor retention figure fell to 15% in 1H 2022. This is the lowest median retention rate for VC SPVs on record, going back to 2015.

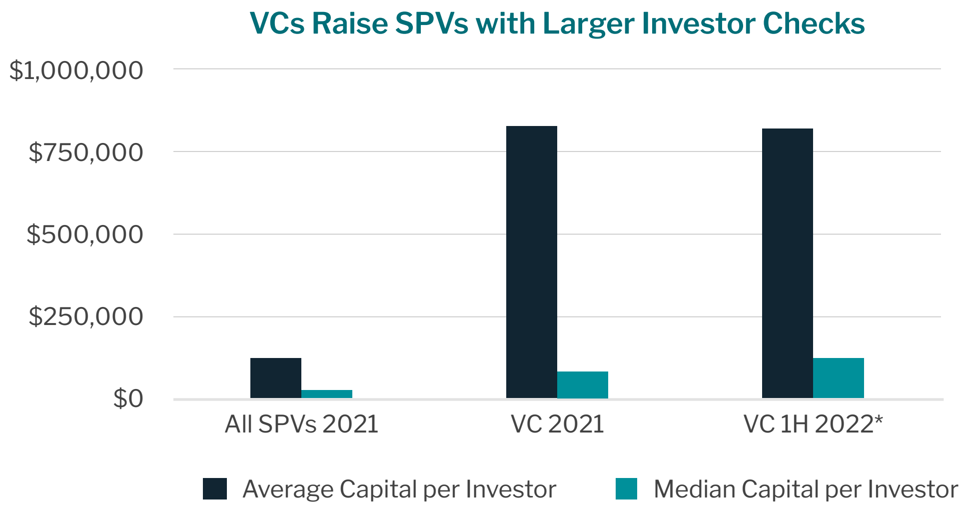


Unsurprisingly given the above, typical investor check sizes into VC SPVs are larger than what's seen in the broader SPV market.

Whereas the average SPV in 2021 raised $122K per investor, the average VC SPV raised over 6X more at $827K. Similarly, the median VC SPV raised $85K per investor, versus $26K market-wide.

This higher capital per investor may partly result from VC SPV investors more frequently being institutional LPs (e.g. endowments and family offices) with large allocation targets, rather than individual investors.

Notably for 1H 2022, the average capital per investor of VC SPVs has remained essentially flat, with a modest increase in the median.



Cadence

VCs utilize SPVs more frequently than other organizer types.

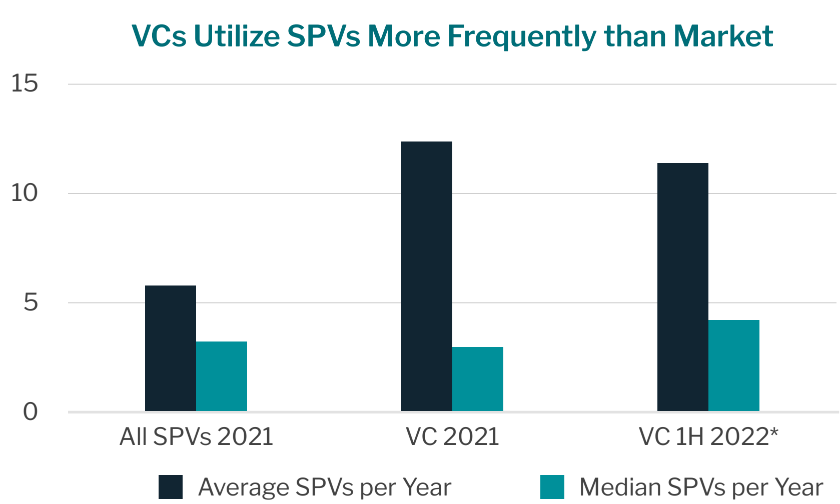
Among SPVs formed in 2021, the average was raised by an organizer with an SPV cadence of 6 vehicles per year. Among VC SPVs, however, the average was raised by an organizer with a 2X faster cadence, at 13 SPVs per year.

Interestingly, in 1H 2022 there was an increase in the median SPV cadence for VC organizers, up to about 4.5 SPVs per year from 2021's median of 3.

This could mean either:

1) VC organizers across the board are accelerating their use of SPVs, perhaps in response to current deal flow and fundraising conditions (i.e. VCs may have insufficient follow-on reserves after the inflated valuations of 2021, and are not able or ready to raise their next flagship vehicle), or

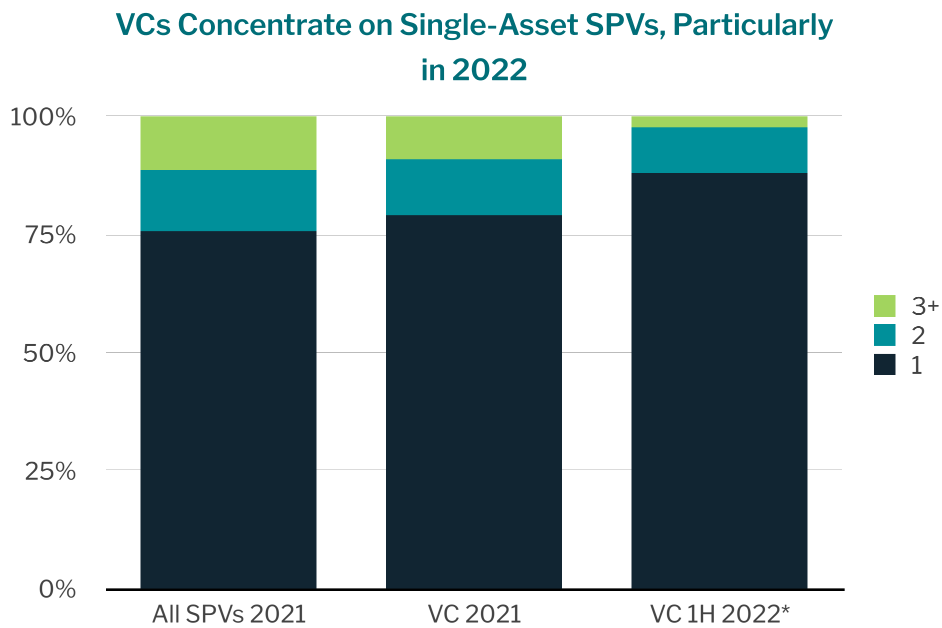
2) Those VC organizers continuing to leverage SPVs in 2022 are more often organizers who historically have done more SPVs each year, consequently pulling up the median.



Underlying Assets

Venture capital firms concentrate on single-asset SPVs, with nearly 80% of VC SPVs in 2021 investing in just one asset. This compares to an SPV market-wide ratio of 75% in 2021.

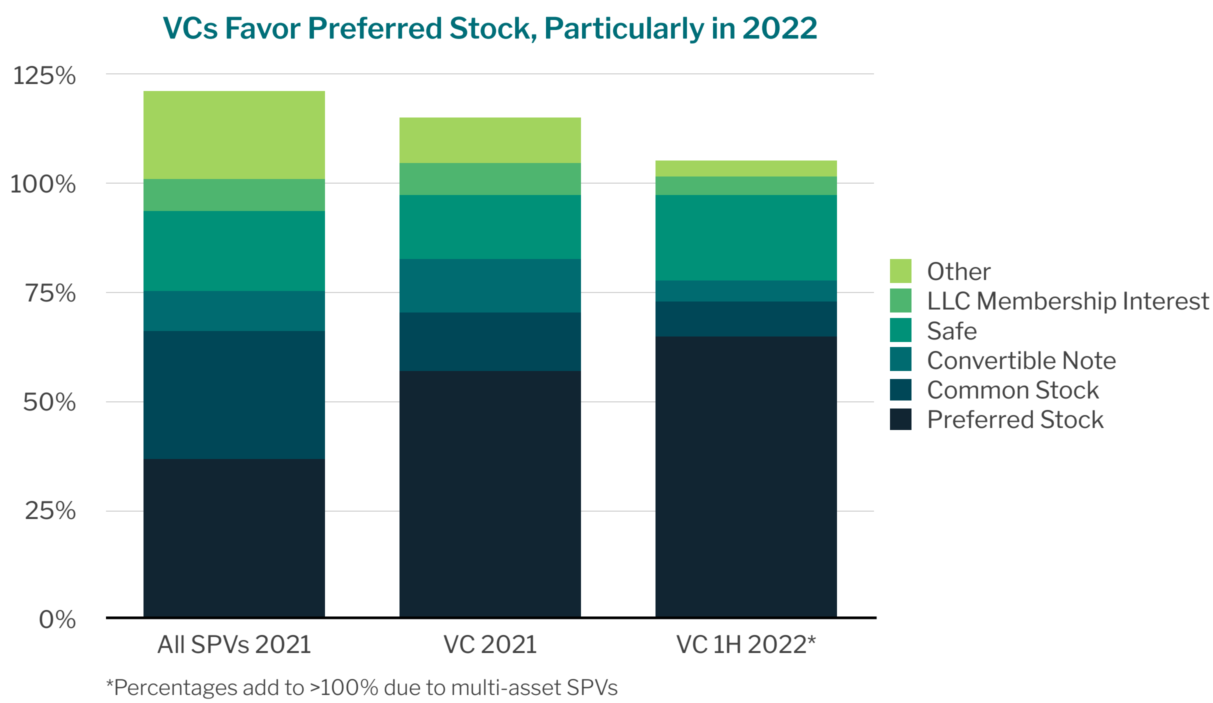
In 1H 2022 there has been further concentration in single-asset SPVs, with 88% of VC SPVs having just one purchase agreement. This might partly result from VC SPVs this year not having fully allocated their capital, with plans for a second or third asset purchase (possibly waiting for more favorable market conditions). Regardless, single-asset SPVs are the overwhelming favorite.



When VC SPVs deploy capital, they lean heavily into preferred stock, with 57% of SPVs formed in 2021 having at least one preferred stock purchase agreement. This compares to 37% for all SPVs, which are much more broadly distributed across purchase agreement types.

And in 2022, VCs have actually increased their concentration in preferred stock deals, with 65% of SPVs purchasing at least one preferred stock asset. SAFEs have also become more prevalent for VCs raising SPVs in 2022, growing from 14% of SPVs in 2021 to 20% of SPVs in 1H 2022.

A possible explanation for both the rise in preferred stock (an investor-friendly agreement type) and SAFEs (a founder-friendly agreement type) is that macro shifts have hit the late-stage venture market differently than the seed and early stages. While late-stage startups have faced more downward valuation pressure (since they're closer to exit and their public-market equivalents), seed and early stage startups have held strong. Consequently, the rise in preferred stock could be a function of investor-friendly changes in the late stage market, while the growth in SAFEs could result from continuing founder-friendly activity in the earliest stages.

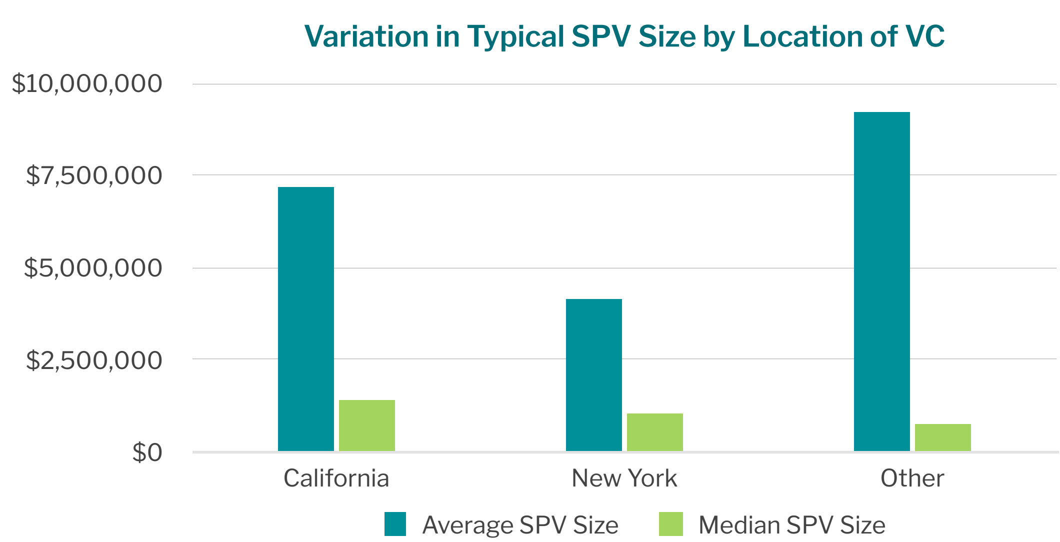


Variation by Geography

Of course, SPV use varies by the location of the venture capital firm.

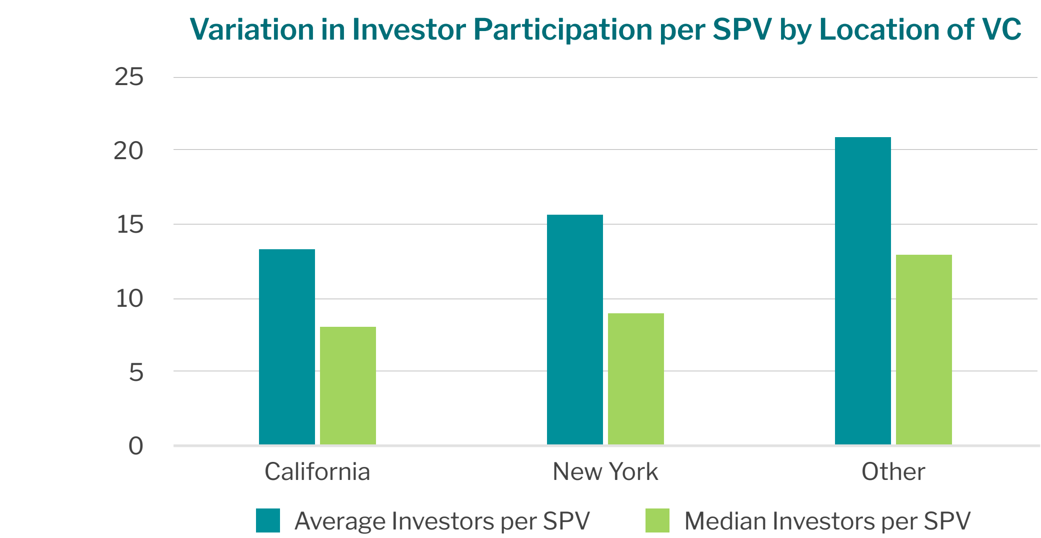
For instance, VCs in California and New York tend to raise larger SPVs than those elsewhere. The median California VC SPV collects $1.4M and the median in New York collects $1.0M, whereas in other U.S. states that figure is $784K.

The discrepancy in SPV size likely has to do with differences in the typical round size and valuation of startups in the two VC hubs of the San Francisco Bay Area and Greater New York City. Investors in these regions pay a valuation premium compared to the Midwest, Southeast, and other U.S. regions. Note that SPVs raised elsewhere have a distinctly high average capital raise, which seems to be pulled up by some particularly large international SPV outliers.



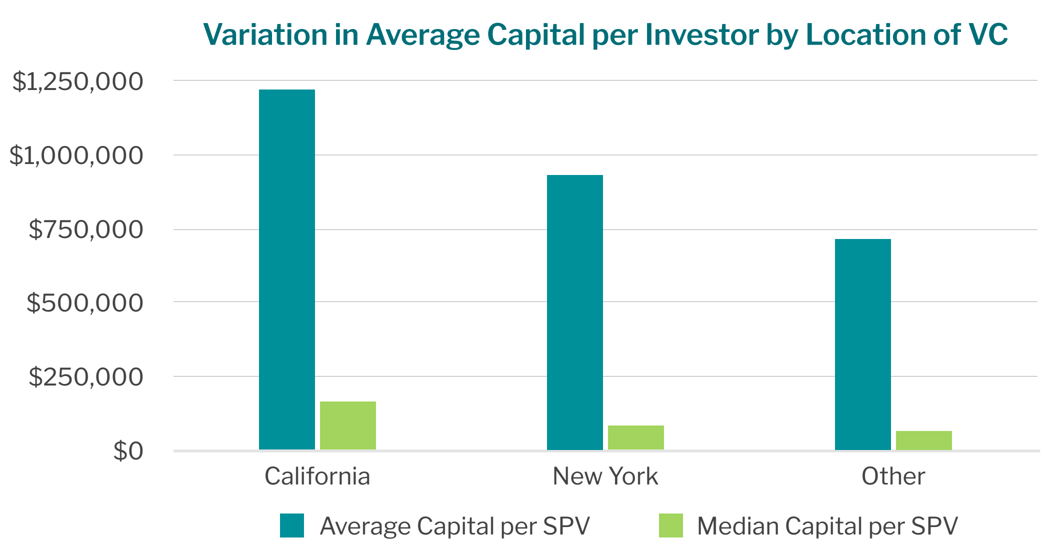
Although California and New York SPVs tend to be larger, they also tend to raise from fewer investors.

The median SPV in CA raises from 8 investors (and from 9 investors in NY), versus 13 in other geographies. As the next chart shows, this could be a function of VCs outside CA and NY raising smaller checks from each investor, meaning they need a larger investor base to participate in order to hit their target raise or maximize their allocation.



While SPVs from CA venture capital firms typically raise $163K per investor, in NY the typical SPV commitment is $88K per investor, and other U.S. states have a median capital per investor of $63K.

Of course, there is significant variation within all this. As seen by the averages, some SPVs are *much* larger in size than the medians. But at the same time, bear in mind that 50% of SPVs fall below the median, and some venture firms raise quite modest SPVs from just a handful of investors.



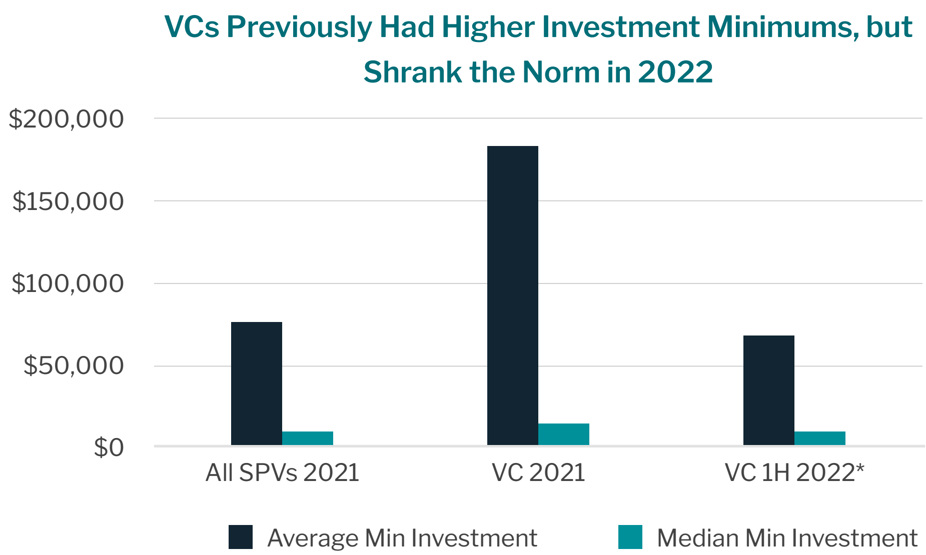
VI. Terms of VC SPVs

Investment Minimums

Compared to all SPVs, VCs tended to set higher investment minimums in 2021.

The average VC SPV investment minimum was $184K in 2021 and the median $15K, whereas the average broader SPV investment minimum was just $75K and the median $10K.

But notably, VC investment minimums have shrunk substantially so far in 2022, to an average of just $67K and a median of $10K. The 65% drop in average investment minimums is another indicator of the current economic cycle, as it suggests organizers are choosing to open investment to a wider range of investor check sizes, rather than relying on deep-pocketed investors to fill an SPV fundraise.

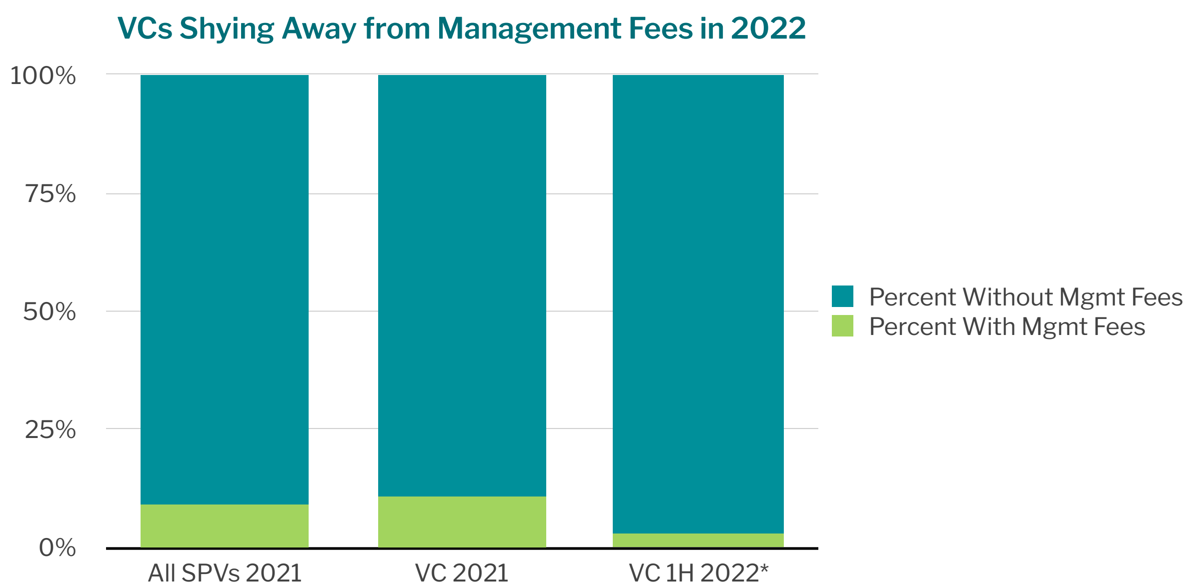


Management Fees

Similarly, although VC SPVs were more likely than other SPVs to charge management fees in 2021, in 2022 there has been a stark decline in their prevalence.

Last year, about 11% of SPVs raised by a VC firm charged their investors management fees, compared to 9% for all SPVs. But in 1H 2022, just under 3% of VC SPVs included a management fee, a 73% drop.

Once again, this is evidence that we are entering an Investor-friendly environment, and venture capital firms are relaxing terms to persuade investors to continue allocating to their deals.

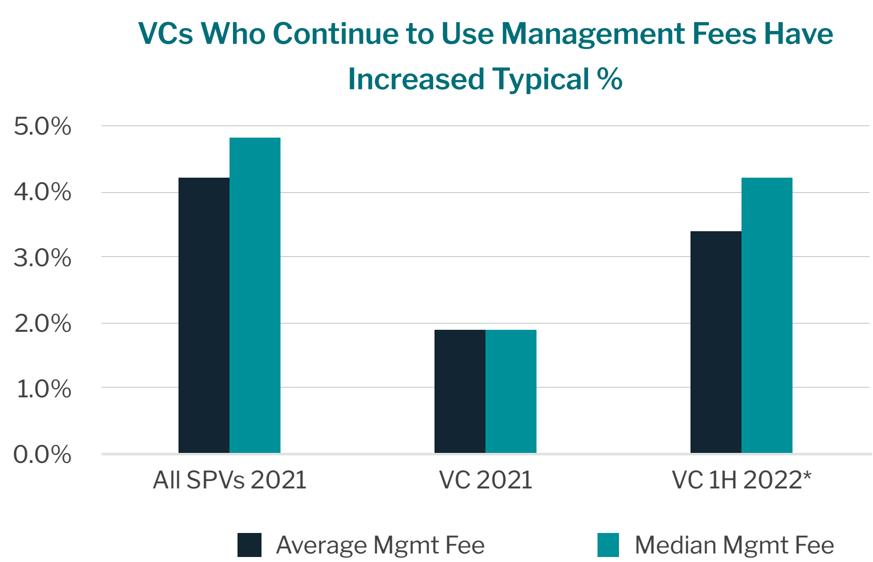


But counterintuitively, despite declining rates of management fees, the typical management fee charged by VCs has increased in 1H 2022 relative to 2021.

Whereas, among those charging a fee, the norm for VC SPVs in 2021 was a 2% fee, the average fee has risen to 3.4% and the median doubled to 4.2% in the first half of 2022.

These fees are more in-line with the broader SPV market (where the 2021 average and median were 4.2% and 4.8%, respectively), but still represent a significantly smaller fee than is typical of a flagship blind-pool VC fund (which charges 2% every year for 5-10 years).

One possible explanation for the rising management fee for VC SPVs resides in the fact that SPV management fees simply became less common for VC firms (see above). This means the pool from which the average and median fee are calculated shrank significantly. It's possible that those VCs continuing to charge a fee in 1H 2022 are just the "high fee" cohort of VCs.



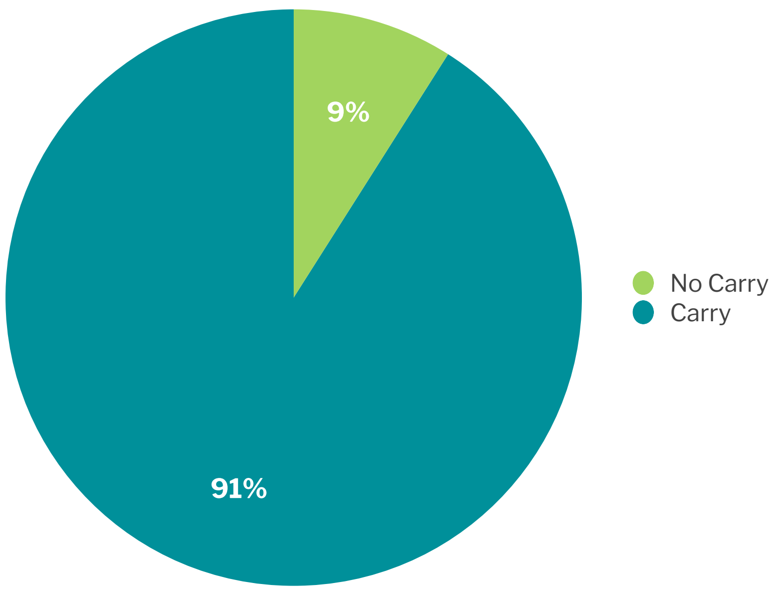
Carry

Carried interest is the key term in venture capital, as it drives the bulk of manager compensation and aligns investor and manager interests. Assure Analytics is working on an in-depth review of carry across SPVs, but wanted to touch on it for this report given its importance for venture capital partners and LPs.

As many would expect, early analysis shows that over 90% of SPVs organized by a VC firm charge carry. Of those charging carry, roughly two-thirds charge 20% (the industry norm for VC flagship funds). The other third generally charge less than 20% (between 5% and 16%).

That said, VC SPVs occasionally include carry side letters that either waive or reduce the amount of carry charged to specific investors in the SPV. Some VCs use waterfalls in their carry term (ex: if X multiple is hit, the carry percentage changes), but it's rare.

Majority of 2021 VC SPVs Charged Carry

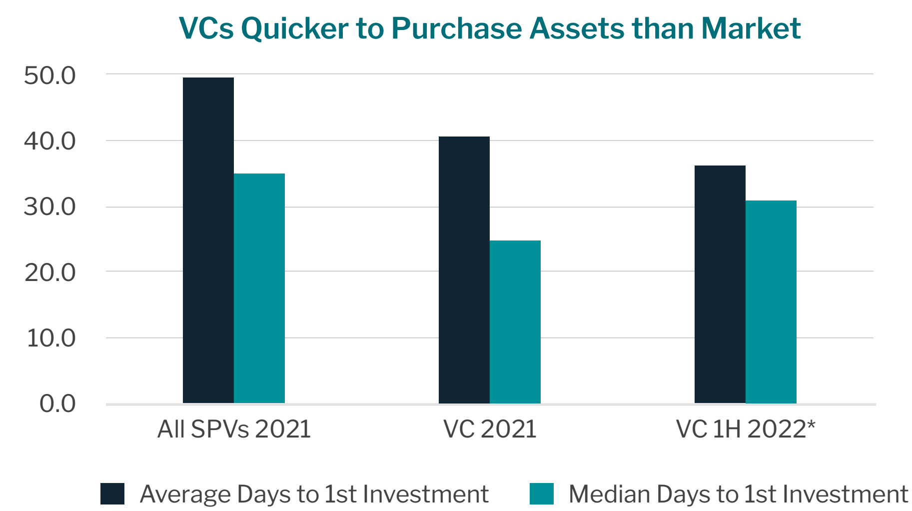


Investment Speed

VC SPVs tend to deploy their capital more quickly than SPVs raised by other organizer types.

In 2021, the median VC SPV signed its first purchase agreement just 21 days after forming, compared to 35 days across all SPVs; similarly, the average VC SPV completed its first asset purchase 41 days after forming, compared to 50 days across all SPVs.

So far in 2022, it appears more VCs are slowing down than speeding up: the median investment timeframe rose to 31 days. However, the average timeframe fell to 36 days, meaning very few VC SPVs are taking exceptionally long to deploy to their first deal.

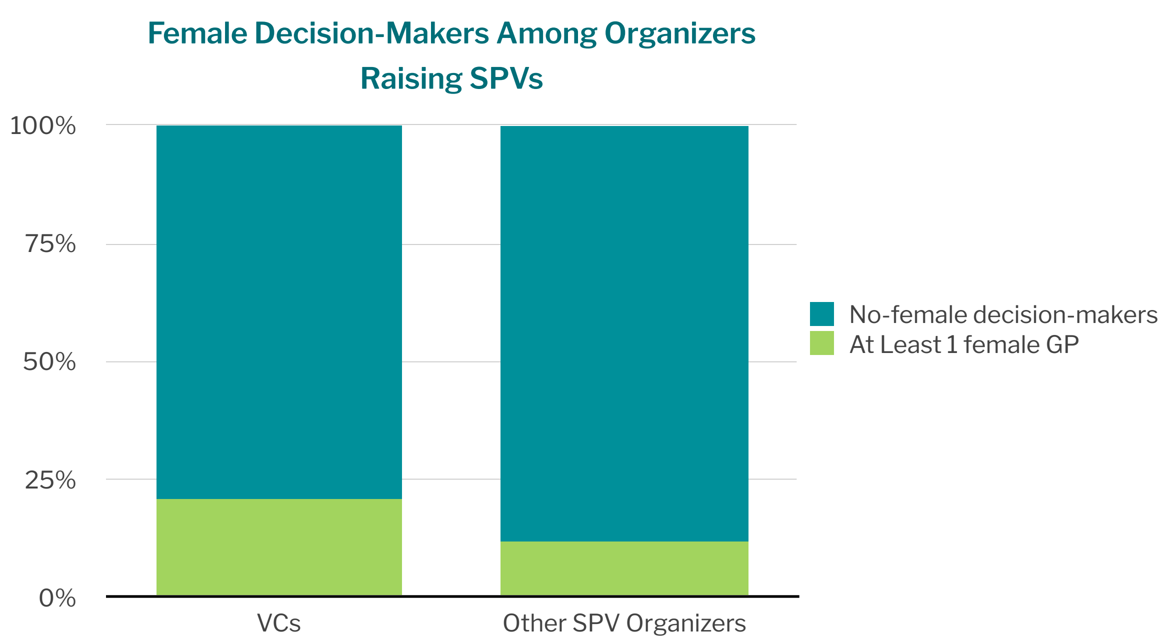


VII. Profile of VC SPV Decision-Makers

This next section offers some insight into the backgrounds and education of organizers who raised an SPV in 2021, specifically focused on comparing VC backgrounds to other organizers. Keep in mind that many organizers are actually firms with multiple partners / investment decision-makers; this analysis is based on the background and education data of all decision-makers (GPs at VC firms) for each "organizing entity."

Demographics

We estimate roughly a fifth of SPVs raised by VCs in 2021 had at least one female GP. This compares to closer to a tenth of SPVs raised by other organizer types, meaning VC SPVs were more gender diverse last year.



We also estimate that among VC SPVs raised in 2021, the average firm has a GP team where the average age is 31 years. This is on-par with other organizer types raising SPVs in 2021, but perhaps pins the typical age of GPs below industry expectations.

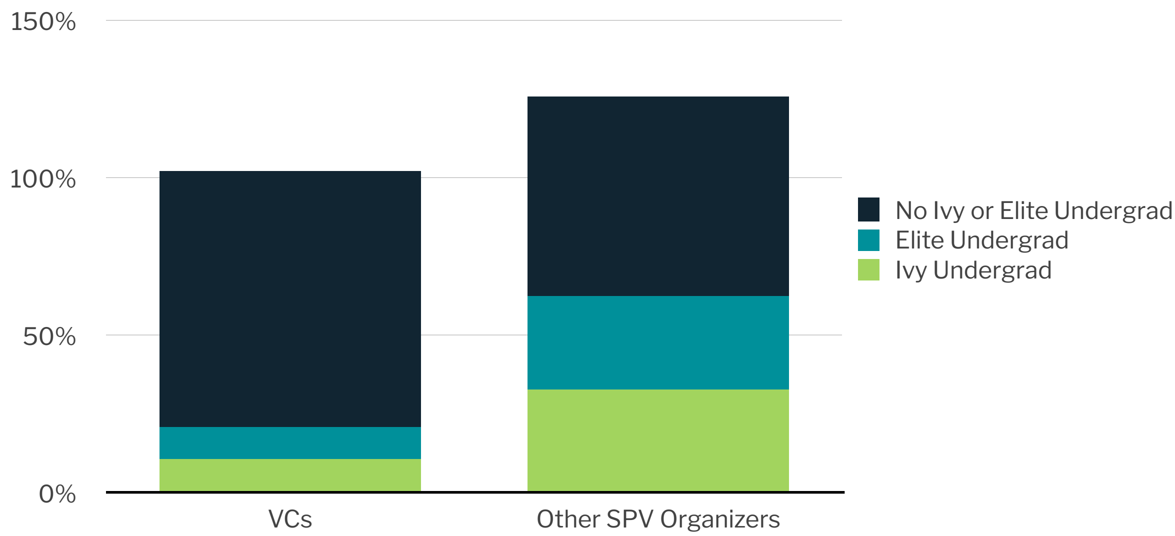
Education

We found that Ivy and Elite bachelor's degrees are far from the norm among VC organizers.

Of the nearly 500 SPVs raised by VCs in 2021, 82% were organized by a firm without any Ivy or elite school alumni. Just 11% were organized by a VC where at least one decision-maker received a bachelor's from one of the Ivy universities, and less than 10% had a decision-maker with a degree from one of the non-Ivy elite universities. (These percentages exceed 100% because each VC firm can have both an Ivy and a non-Ivy Elite alumnus.)

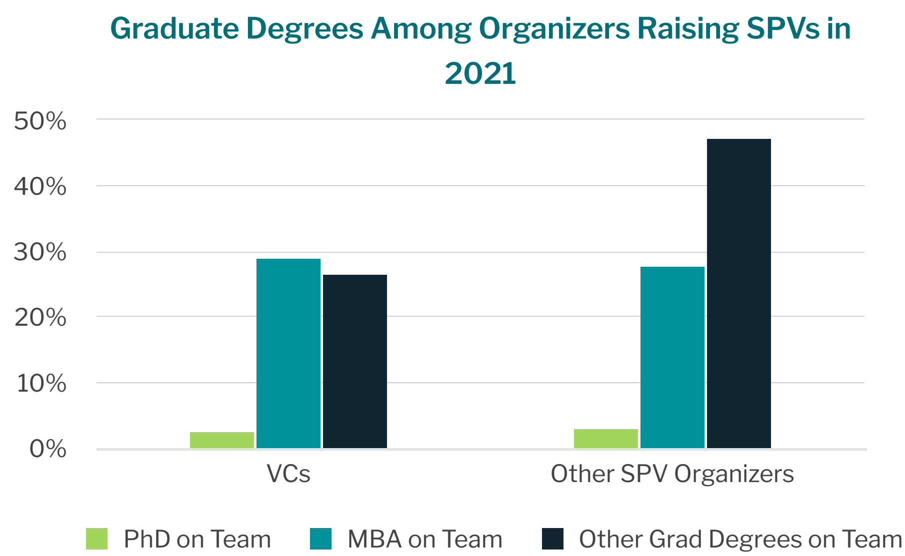
This contrasts to all other SPVs, where fewer than two-thirds were organized by a team without an Ivy or Non-Ivy Elite undergraduate degree.

Undergrad Schools Among Organizers Raising SPVs in 2021



*Percentages exceed 100% because VC firms and other Organizing entities can have multiple decision-making individuals, from multiple undergraduate programs.

As for graduate degrees, nearly 30% of VC SPVs organized in 2021 consisted of a team where at least one decision-maker held an MBA, making an MBA by-far the most common graduate degree. Just 2% of VC SPVs were organized by a team with at least one PhD. Both of these figures align with graduate degrees for SPVs raised by other organizer types.



VIII. Conclusion

Venture capital firms of all shapes, sizes, and strategies use SPVs – from sub-$25M, solo-GP, DeepTech specialist funds to $1B+ generalist funds with a dozen or more partners. SPVs are often used by VCs to take advantage of pro-rata rights and syndicate co-investment opportunities. We are starting to see fundraising decks explicitly mention the firm's intent to use SPVs (often as a way of courting the growing numbers of LPs who explicitly seek out coinvestment rights), though we are still in the early days of SPVs transforming the venture legal stack. While today just 10 to 20% of venture firms have used SPVs, this is up significantly over the last decade. SPVs make up over 40% of all vehicles raised by VCs and we expect to see continued growth. We are also seeing more emerging managers eschewing flagship funds entirely, instead opting for a 'syndicate' fund or network investment strategy.

As VC firms mature into their second and third funds, we see more of them embrace SPVs. Firms that do more deals per year are also more likely to use SPVs. VCs are leveraging this investor-friendly structure for greater alignment with current LPs and to cultivate new ones. While the vast majority of VCs charge some form of carry on their SPVs, most do not charge management fees. In terms of underlying assets, most VCs choose a single asset SPV (one startup deal per SPV). For 2022, we are also seeing a strong bifurcation in the choice of deal docs – with more VCs executing deals via either SAFEs or Preferred Stock purchase agreements.

Assure Analytics publishes a range of private markets intelligence, with additional research on VCs available on our blog. Prior reports include the State of SPVs, the State of Terms in Venture Capital, and the VC Deck Report. Please subscribe to our newsletter to stay apprised of the cutting edge in SPVs, venture capital, and other private assets.

IX. About This Report

About Assure

Assure provides a FinTech platform for private asset investing. The company specializes in Special Purpose Vehicles (SPVs) and is the largest provider in the United States having completed over 8,000 SPVs to date. The company offers end-to-end formation and administration services for clients from angel investors to venture funds to family offices to large institutional allocators, providing services from legal to accounting to compliance to tax to administration. As part of this, Assure built a state-of-the-art technology stack with white-label APIs that automate everything from banking to compliance to post close activities.

Assure Analytics is the business intelligence unit of Assure. It makes sense of millions of data points across the private markets, surfacing relevant insights and knowledge to help clients and the global financial industry make better investment decisions.

About the Authors

Leslie Jump, Chief Revenue Officer

An experienced venture capitalist, startup investor, board member, and limited partner, Leslie has dedicated over 30 years to building, advising and investing in new companies and funds across the globe. Previous experience: CEO at Different, CEO at Startup Angels, Partner at Sawari Ventures, Board of UP Global. Alumna of St. John's College, and member of its Board of Visitors and Governors.

Mack Kolarich, VP Analytics

A seasoned entrepreneur and startup community leader, Mack has spent the last decade focused on startup investing, venture capital, and research & intelligence for private assets. Previous experience: Chief Product Officer at Different, Vice President of Product at Startup Angels, CEO at SceneSquid. Alumnus of Carleton College.

Jacob Tasto, Analyst

Leveraging his prior work on economics and entrepreneurship communities, Jacob conducts research, data collection, and data analysis at Assure. Previous experience: Venture Analyst at Different, Research at Dream Big Foundation, Seed Spot. Alumnus of the University of Maryland.