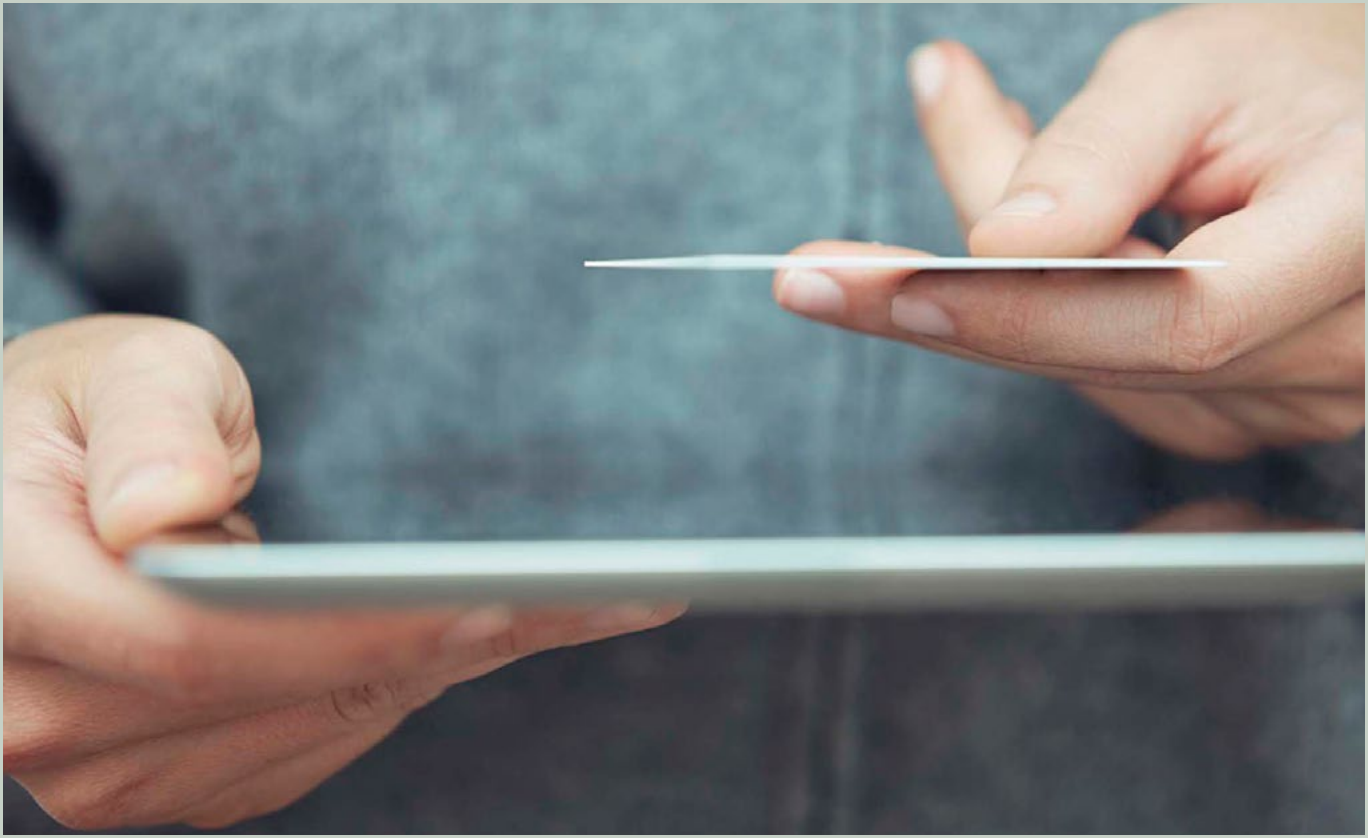
Vol. 1

Start-up guide | Investments

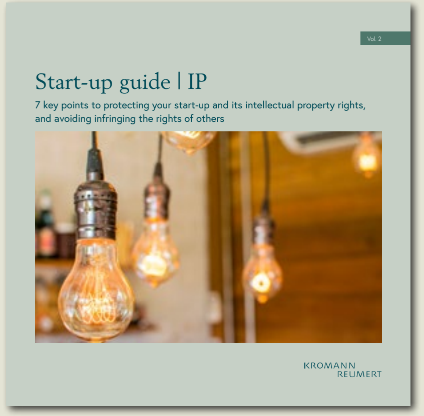
7 key points from a legal perspective for getting ready for investments

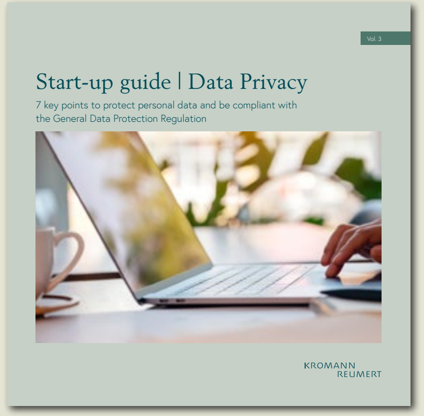


KROMANN REUMERT

Read our other start-up guides

If you're also interested in protecting your start-up's rights and avoiding pitfalls in relation to the rights of others, be sure to request a copy of Vol. 2 of our start-up guide entitled "7 key points to protecting your start-up and its rights, and avoiding infringing the rights of others".





Hi there!

We know that you would probably rather spend your time working on your new idea, so we won't take up much of your time. But we really want to see you succeed with your start-up, and it is our experience that a significant factor in attracting external investments and transforming a promising start-up into a successful and valuable business is having the legal aspects in order.

It is especially important to get the legal aspects sorted out early on, if your plan is to take on external investments. Having third parties invest in your company is often much more complicated than most start-up founders expect, and agreeing to undesirable terms may potentially result in the failure of your start-up. However, many common mistakes and pitfalls may be avoided, as long as you are aware of them and handle them properly.

To help you get a quick overview of the most important legal aspects to consider on your way from start-up to funded start-up to successful business, we have drawn up 7 key points that we hope you will consider and keep in mind as you accelerate your start-up.

We love working with start-ups and would be happy to meet you for an informal discussion (free of charge, no strings attached) on your thoughts, concerns, hopes and wishes as a start-up, and to advice you on how to best prepare you and your start-up from a legal point of view. Feel free to contact any of us – you'll find our contact information in the back of this leaflet.

#1
Get organised and get compliant

Yes, that's right – even the boring stuff counts when you want to attract and get funding from investors! Having your registrations, company documents, etc. in order and readily at hand can save you a lot of time and cost when you are ready to get your investors on-board. In particular if your start-up is dependant on intellectual property rights, you should ensure that everything around the development and licensing hereof is crystal clear. Investors don't want to worry about the basics!

#2
Build and secure the strongest team

While start-ups are based on an idea, the true value of a start-up often lies in the people behind it. When maturing your business for investments, it is key to secure that the right people are on board from the start and stay there – even when they are offered better deals elsewhere. Investors considering investing in your business are also looking to see if your key salesman or key developer could potentially leave shortly after the investment. While it may be tempting to keep the entire cake for yourself, it is often worth sharing some of it with your key employees to create and maintain an even bigger cake. There are numerous ways of ensuring that your employees have the right incentive to stay on board, including warrant programs, and share allocation.

#3
Lose the deadweight

Investors don't like getting on board a business, where a significant portion of the shares are owned by parties not fully invested in driving the business forward, e.g. original founders no longer part of the business. Ensure from the beginning that your agreement with the other founders contain appropriate protection in this regard, e.g. by including a purchase right for the continuing founders in case someone wants to quit.

#4
Get incorporated…fast!

While the urban legend of entrepreneurs starting up their businesses in their parents' basement is seldom true, it is commonly the case that their development of ideas occur in a privately owned context (i.e. not through a corporation like an A/S, ApS or IVS). While this may be fine in the immediate beginning, there comes a time before long, when you should consider to incorporate both your business (in an operating company) and your ownership of the business (in a holding company) both for liability and tax purposes. Entrepreneurs often do not realise this issue until after their start-up is suddenly worth the big bucks with investors knocking on the door, and at that time it is often too late to get the optimal tax position.

#5
Get your shareholders' agreement right

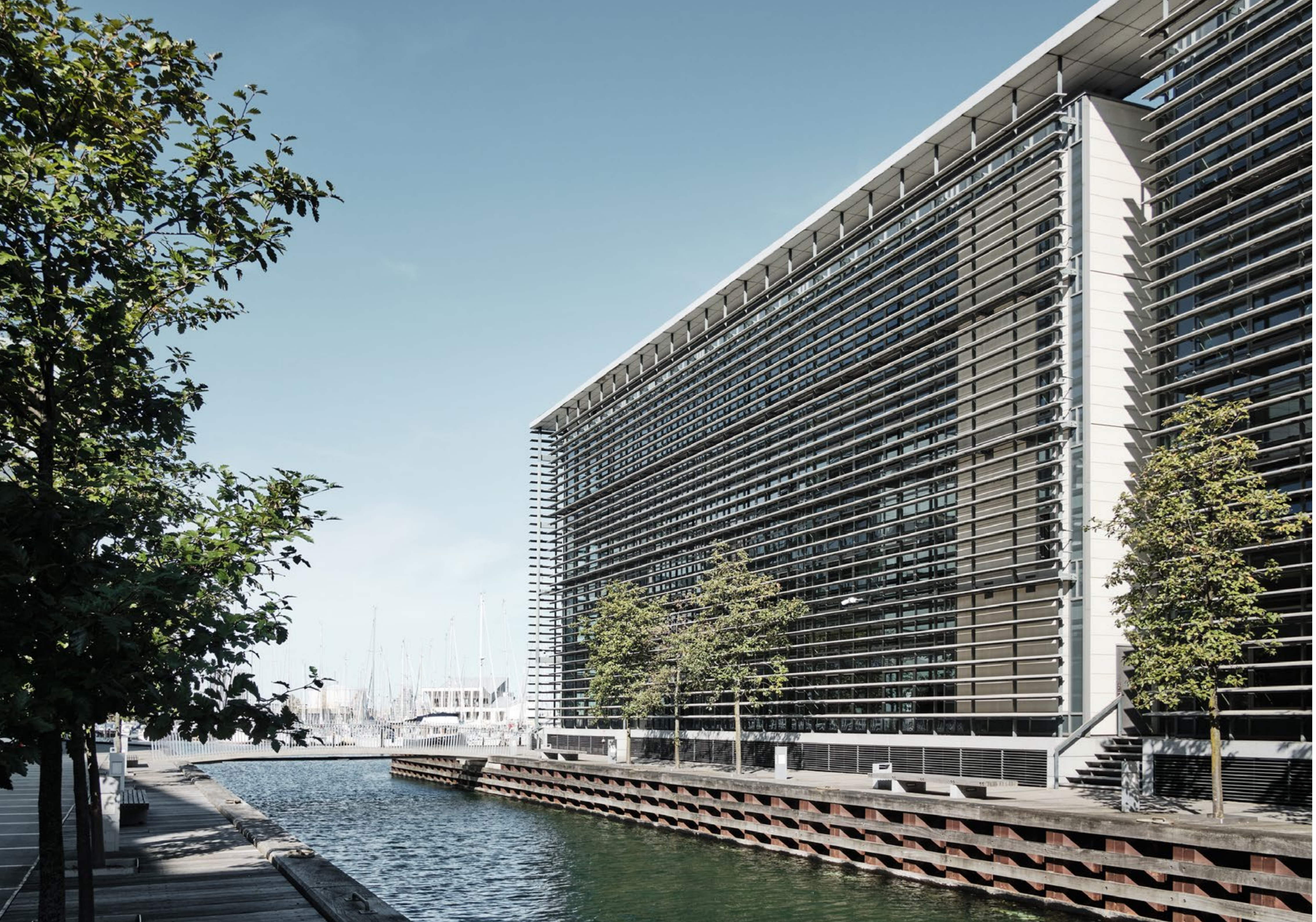
When starting up your business with one or more partners, the regulation of your relationship is key to the long-term success of your business. Do yourself the favour of getting it right the first time. Often times, shareholders' agreements do not allow for subsequent amendments unless all parties agree, which can be a significant problem and disturbance in the operation of the business if/when you realise that the terms are disadvantageous for the business or you personally. Entrepreneurs sometimes take on drafting such agreements themselves or reuse an agreement used by a friend in another context. However, this is perhaps the most important document you and your partners will ever sign, so it is very important that it is tailored to your situation and needs and that it properly takes into account not only the current situation, but also your expectations for the future. Getting it right also means including the right provisions, including, e.g. mechanisms for avoiding "dead-lock"-situations, securing preemption rights, non-compete clauses etc.

#6
Get the 'legalese'-people on board from the get-go

We often see that entrepreneurs negotiate and sign term sheets, letters of intent and other preliminary investment documents with investors on their own and only afterwards contact their lawyer. Even though such documents may not be binding, the terms are very difficult to amend after they have been agreed upon. Furthermore, the key legal terms are often not addressed in such documents resulting in unnecessarily complex subsequent negotiations. Consequently, it is a good idea to consult a lawyer before agreeing on the terms of such documents or at the very least give him/her a call for some quick thoughts. While the commercial terms may be your main focus, remember that the legal terms are crucial for your continued involvement and control over your business.

#7
Get the right investor

Investors are not all the same. Some are professional investors, some not, some want to be very actively involved in their investments, some not at all, and some might even want to utilize potential synergies with other portfolio companies. Just like getting the right people on your team, it is important that you don't get the wrong investor on board, as this can result in a bad investor relationship and in worst case, conflict. Therefore, always understand what your investor wants to do with the investment, and ensure that you have the same goals and to some extent agree on the ways of achieving them!



Contact

Do you have any questions or need help?
Feel free to write or call us for an informal talk or meeting – free of charge and with no strings attached.

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KROMANN REUMERT

At Kromann Reumert, we set the standard. Together. We provide value-adding solutions and advisory services with dedication and focus. We are driven by our four core values: quality, commercial understanding, spirited teamwork, and credibility. We are Denmark's leading law firm with offices in Copenhagen, Aarhus and London.

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