

Morgan Lewis

STARTUP & ACCELERATE

**Key Beginning Documents:
Founders' Agreements, Seed Financing,
Convertible Notes, and SAFES**

February 10, 2022

Michael Barron and Benjamin David Novak

Presenters



Benjamin David Novak

Partner, Emerging Business and Technology Practice
Angel Investor



Michael Barron

Partner, Emerging Business and Technology Practice

Morgan Lewis

Founders' Agreements

Morgan Lewis

What is a Founders' Agreement?

- Typical Provisions:
 - Governance (e.g., how to elect the Board and who the officers will be; protective provisions)
 - Transferability of Shares (e.g., ROFR in favor of the Company or other founders; tag along rights)
 - Buyouts (e.g., death, disability or termination)
 - Drag Along
 - Market Standoff



Do you need a Founders' Agreement?

Establishes roles and responsibilities

Guidance in certain circumstances (e.g., a founder wants to sell, a founder is no longer able to dedicate the same amount of time to the business)

Protects minority stockholders

Helps stabilize the Company in the event of the departure of a founder



Alternatives to Founders' Agreement

Corporations

- Bylaws
 - For a Right of First Refusal in favor of the Company and Transfer Restrictions
- Restricted Stock Purchase Agreements
 - For Vesting and Market Standoff

Limited Liability Companies

- Operating Agreement



What Happens to the Founders' Agreement upon a VC Financing?

- Founders' Agreement will likely be superseded by:
 - Investors' Rights Agreement
 - Voting Agreement
 - Right of First Refusal and Co-Sale Agreement

- Consider:
 - Amendment Provision
 - Terminates upon a VC Financing



Considerations in Structuring Seed Financings

Morgan Lewis

Considerations in Structured Seed Financings



Who are the Investors and What are their Preferences?



How Much Capital is Being Invested?



What are the Costs?



What is the Timing?



Any Specific Considerations?

Seed Financing Deal Structures

Morgan Lewis

Common Stock

Series Seed Preferred Stock



Others

Convertible Debt

SAFEs

Common Stock

Morgan Lewis

Common Stock

What is It?

- Most basic form of equity

What are the Terms?

- Generally, to elect directors, receive any dividends, share in any proceeds upon liquidation
- Generally, no special “investor-style” rights

What are the Advantages?

- Low transaction costs
- From the company’s perspective, investors have very limited economic and control rights

What are the Disadvantages?

- From the investor’s perspective, investors have very limited economic and control rights

When is it Used?

- Founder financings
- Maybe friends and family financings

Series Seed Preferred Stock

Series Seed Preferred Stock

What is It?

- A “special” form of equity

What are the Terms?

- Liquidation Preference, Dividends, Pre-emptive Rights, Board Representation, Protective Provisions, Information Rights, Access Rights, and More

What are the Advantages?

- From the investor’s perspective, a negotiated set of specific economic and control rights
- From the company’s perspective, the ability to attract smart money

What are the Disadvantages?

- Higher transaction costs
- Longer time to closing

When is it Used?

- Venture capital financings
- Sophisticated angel financings

Convertible Debt

Convertible Debt

What is It?

- A debt security that may convert into an equity security

What are the Terms?

- Principal Amount, Interest Rate, Maturity Date, Discount, Valuation Cap
- Conversion Features (Qualified Financing, Non-Qualified Financing, Change of Control, Maturity)

What are the Advantages?

- Punts the valuation conversation, if no Valuation Cap
- Low transaction costs
- Shorter time to closing

What are the Disadvantages?

- From the investor's perspective, their stockholder rights are not yet set
- From the company's perspective, the debt could mature and become due and payable

When is it Used?

- Very Often (especially in smaller raises and earlier raises)

SAFEs

Morgan Lewis

SAFEs

What is It?

- “Simple” Agreement for Future Equity

What are the Terms?

- Similar to a note with no interest or maturity

What are the Advantages?

- Theoretically low transaction costs
- Theoretically shorter time to closing

What are the Disadvantages?

- From the investor’s perspective, an irrevocable commitment of capital with a hope of fair treatment in the future

When is it Used?

- Incubator financings, very early financings, very small financings, West Coast deals

Questions?

Morgan Lewis

Save The Date

STARTUP & ACCELERATE

**Key Commercial Agreements for Early-Stage
Life Sciences Companies**

Thursday, March 10 @ 12:30pm

Biography



Michael Barron

Partner

T +1.617.951.8850

michael.barron@morganlewis.com

Michael K. Barron represents life sciences and technology companies and advises companies, entrepreneurs, and investors in the areas of formation and governance, early and later stage debt and equity financings, mergers and acquisitions, employment and executive compensation, and intellectual property matters, including trademark and technology licensing.

Michael serves on the board and as general counsel to several trade associations that focus on promoting and developing companies and professionals in the life sciences and technology industries. One of these organizations is the Massachusetts Innovation & Technology Exchange (MITX), a trade association, which is now a part of the Greater Boston Chamber of Commerce, serving more than 7,000 New England professionals involved in Internet and digital technologies industry. Michael founded MITX in 1995 to help promote the development and growth of the Internet and digital technologies industry in New England.

Biography



Benjamin David Novak

Partner

T +1.609.919.6612

benjamin.novak@morganlewis.com

Benjamin David Novak's corporate practice focuses on equity financings, debt financings, corporate governance, securities matters, and mergers and acquisitions. He represents emerging growth companies in the US and abroad in various industries including technology and life sciences, as well as, angel investors, private equity firms, and venture capital funds.

Ben is an active member of the startup and venture capital community. He serves on multiple Boards and Advisory Boards. Additionally, he routinely speaks at events, conferences, and universities on a variety of topics related to technology, entrepreneurship, and investing.

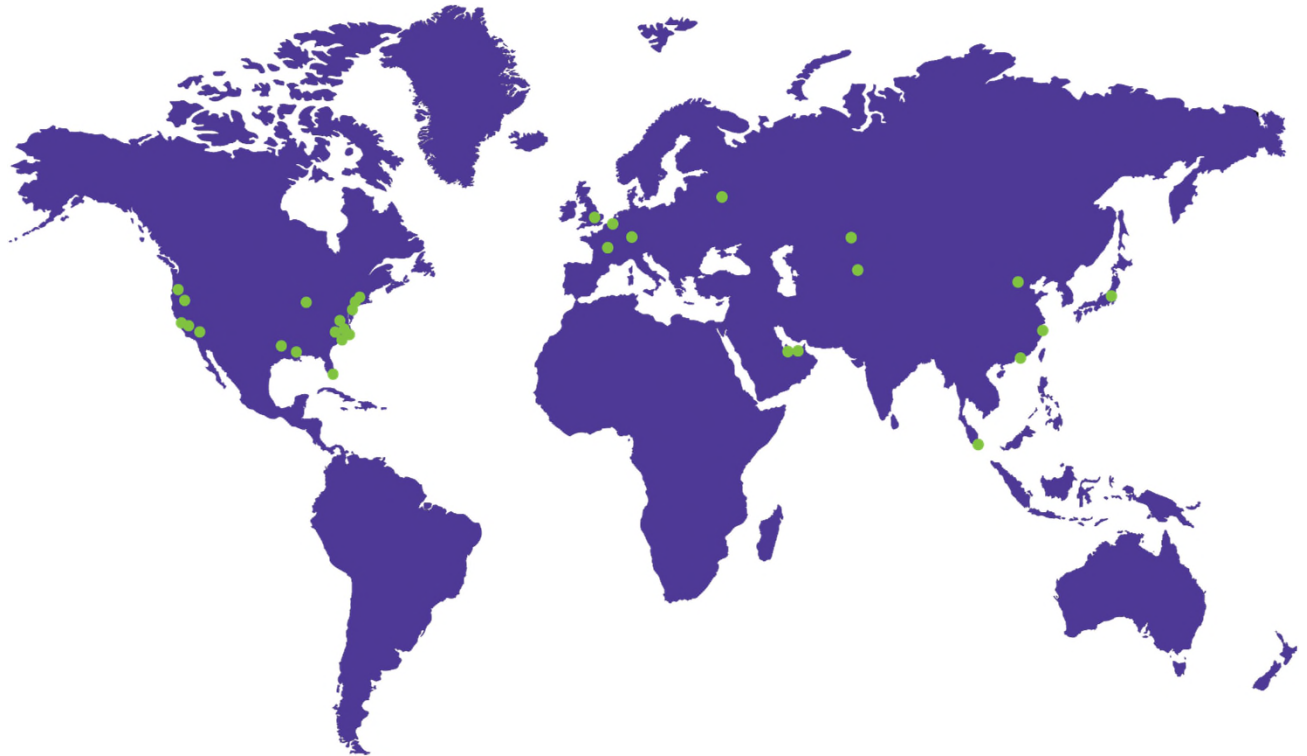
Outside of his role at Morgan Lewis, Ben is personally an active angel investor, who invests primarily in East Coast based seed stage technology companies. Prior to joining Morgan Lewis, Ben was an associate in the venture capital and technology practice of a prominent national law firm

Our Global Reach

Africa
Asia Pacific
Europe
Latin America
Middle East
North America

Our Locations

Abu Dhabi
Almaty
Beijing*
Boston
Brussels
Century City
Chicago
Dallas
Dubai
Frankfurt
Hartford
Hong Kong*
Houston
London
Los Angeles
Miami
Moscow
New York
Nur-Sultan
Orange County
Paris
Philadelphia
Pittsburgh
Princeton
San Francisco
Shanghai*
Silicon Valley
Singapore*
Tokyo
Washington, DC
Wilmington



Morgan Lewis

Our Beijing and Shanghai offices operate as representative offices of Morgan, Lewis & Bockius LLP. In Hong Kong, Morgan, Lewis & Bockius is a separate Hong Kong general partnership registered with The Law Society of Hong Kong. Morgan Lewis Stamford LLC is a Singapore law corporation affiliated with Morgan, Lewis & Bockius LLP.

THANK YOU

© 2022 Morgan, Lewis & Bockius LLP
© 2022 Morgan Lewis Stamford LLC
© 2022 Morgan, Lewis & Bockius UK LLP

Morgan, Lewis & Bockius UK LLP is a limited liability partnership registered in England and Wales under number OC378797 and is a law firm authorised and regulated by the Solicitors Regulation Authority. The SRA authorisation number is 615176.

Our Beijing and Shanghai offices operate as representative offices of Morgan, Lewis & Bockius LLP. In Hong Kong, Morgan, Lewis & Bockius is a separate Hong Kong general partnership registered with The Law Society of Hong Kong. Morgan Lewis Stamford LLC is a Singapore law corporation affiliated with Morgan, Lewis & Bockius LLP.

This material is provided for your convenience and does not constitute legal advice or create an attorney-client relationship. Prior results do not guarantee similar outcomes. Attorney Advertising.