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BERGER SINGERMAN FLORIDA'S BUSINESS LAW FIRM

- Day-to-Day: Business Deal Lawyer 18+ years
 - Business Lifecycle Counsel: Outside General Counsel
 - Corporate Finance: Startup/VC/PE/Debt Transactions
 - Exits & Partnerships: Mergers & Acquisitions and Joint Ventures
- Core Clients:
 - Emerging Companies and Middle Market Companies
 - Entrepreneurs and Investors
 - Various Industries

• Extras:

- Advisory Council Member, Alan B. Levan / NSU Broward Innovation Center (Thought Leadership/Think Tank Committee)
- Board Member Alternate, Florida Venture Forum
- Mentor, Rollins College Crummer Graduate School of Business

Presentation Outline

Background:

Business Financing Framework

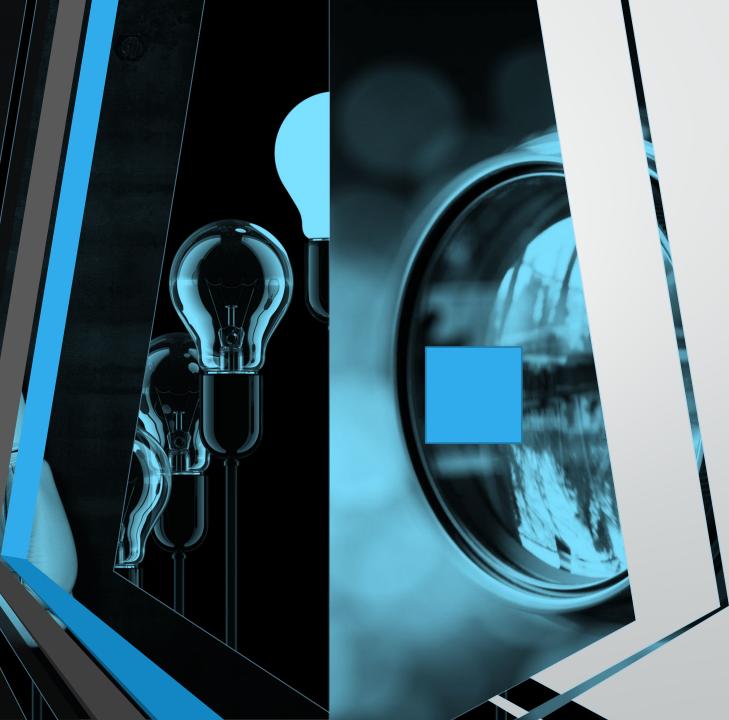
• Focus:

"Pre-Seed" Financing

Approach:

- Legal Lens
- Practitioner's Corner
- Legal Innovation Tips
- Legal Ethics:

Select Issues for Startup Counsel



Background: Business Financing Framework

- Startup Financing in the U.S.
- Startup Financing Concepts
 - Traditional Debt and Equity
 - Startup "Debt" and "Equity"
- New(er) Types and Methods of Startup Financing
 - Crowd and Coin
 - Other Methods and Modes
- Financing Stages
 - Early Stages
 - Growth Stages
 - Exit Stages

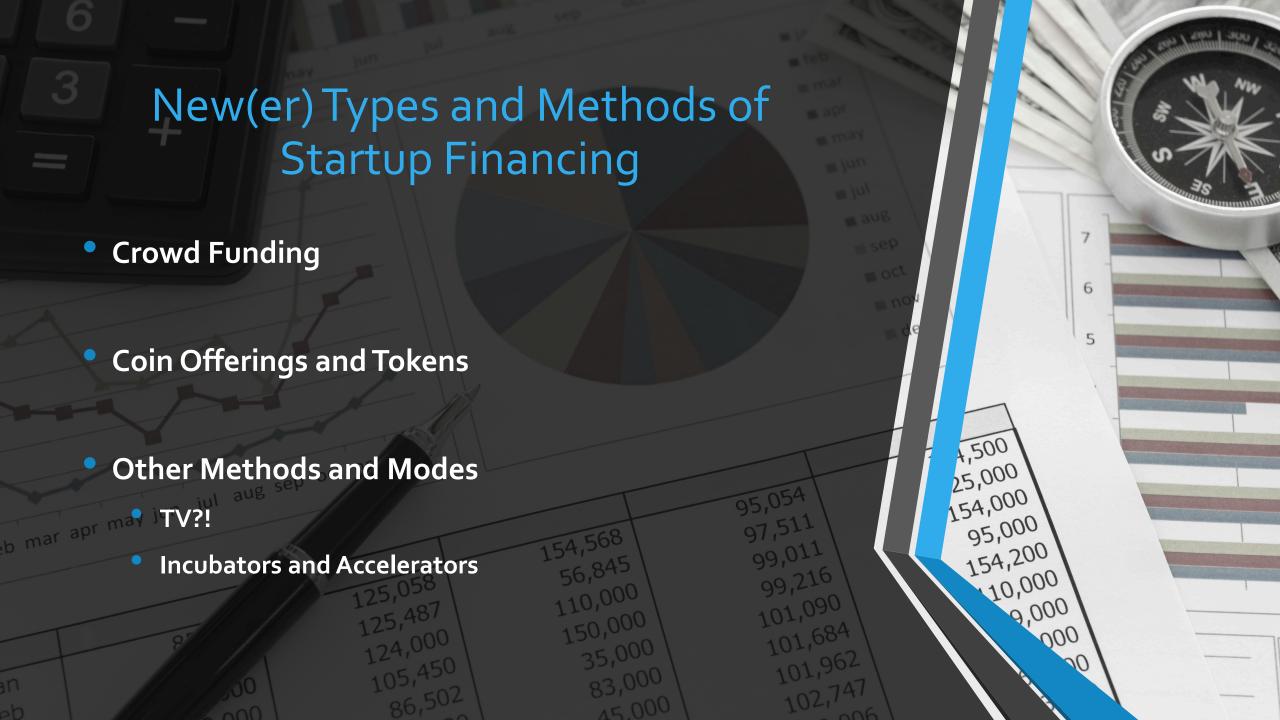
Startup Financing in the U.S.

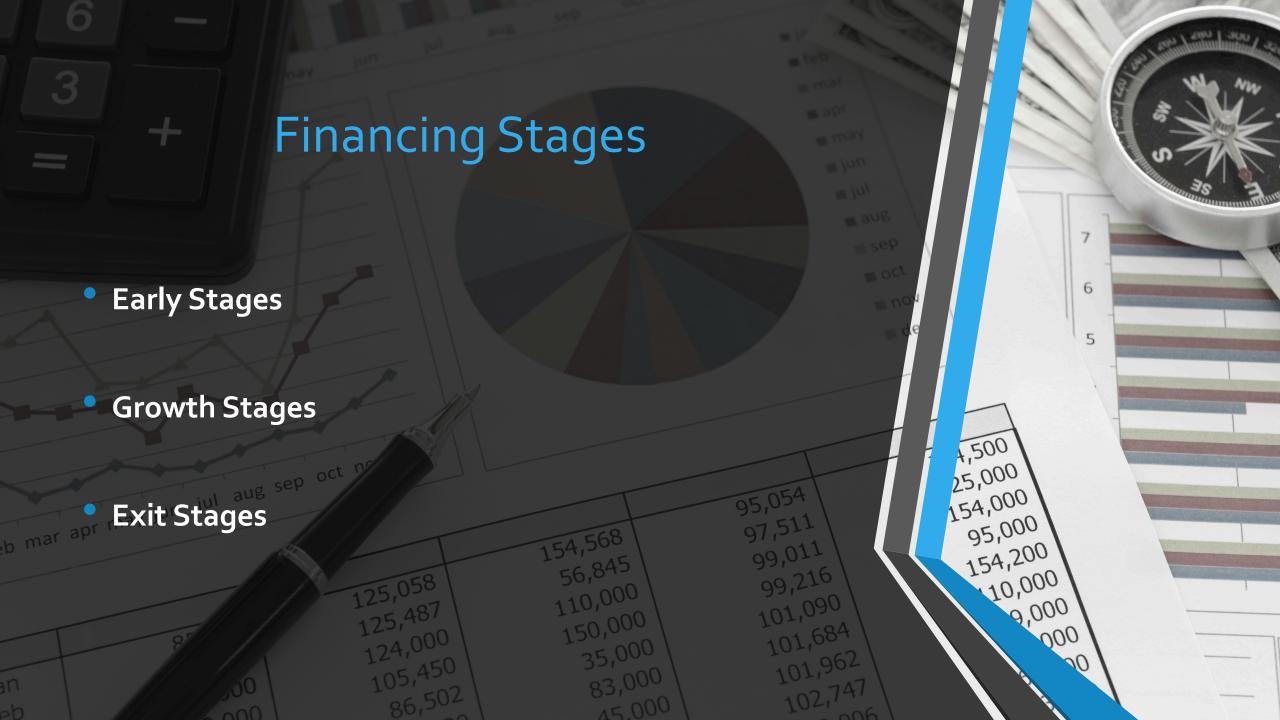




- Legal System
 - Delaware!
- Access to Capital and Talent
 - Innovative Culture
 - "Ecosystems"







Focus: "Pre-Seed" Financing

Legal Lens

- Primer on U.S. Securities Laws (Private Offerings)
- Most Common Pre-Seed Financing Instruments

Practitioner's Corner

- The "S Corp" Effect
- Service-for-Equity
- Why "Accredited Investors"?
- Form D and "Blue Sky" Filings

Legal Innovation Tips

- Cap Table Management
- Document Management and Automation
- Transaction Management



Primer on U.S. Securities Laws

Private Offerings under Section 4(a)(2) of the 1933 Act

Rule 506(b) of Regulation D

State Securities Laws

Legal Lens

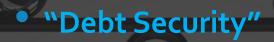
Most Common Pre-Seed Financing Instruments

Convertible Promissory Notes

SAFEs (Simple Agreements for Future Equity)

The Convertible Promissory Note ("C-Note")

 Most Popular Instrument (Most Familiar to Investors Outside of Silicone Valley)



- Principal [and interest] due at maturity
- Fixed rate of interest accrues on principal
- Principal [and interest] converts into preferred equity upon qualified financing event
- Unsecured debt
- Can Be "Stand-Alone" or "Credit Facility" (Series)
 - More common to be used in a series (i.e., a round)
- Minimal reps and warranties by startup
- Minimal ancillary documents



• Investors' View: Unpriced Equity

- Conversion events are very important
 - "Next Equity Financing" Event
 - "Corporate Transaction" Event
 - "Maturity" Event
- Conversion terms are very important
 - "Discount Rate"
 - "Valuation Cap"
- Sometimes ordered with a "Side Letter"

Can also be a "Bridge" at Later Stages

The SAFE (Simple Agreement for Future Equity)

More Popular in Recent Years

- Named and Popularized by Premier Startup Accelerator Y Combinator in 2013 (pre-money SAFE form for smaller investment amounts)
- Introduced post-money SAFE form in 2018 due to usage and larger investment amounts to treat SAFEs as their own round
- Go to ycombinator.com for forms and guides! (But remember you may not be a lawyer!)

Not a Common "Bridge" at Later Stages



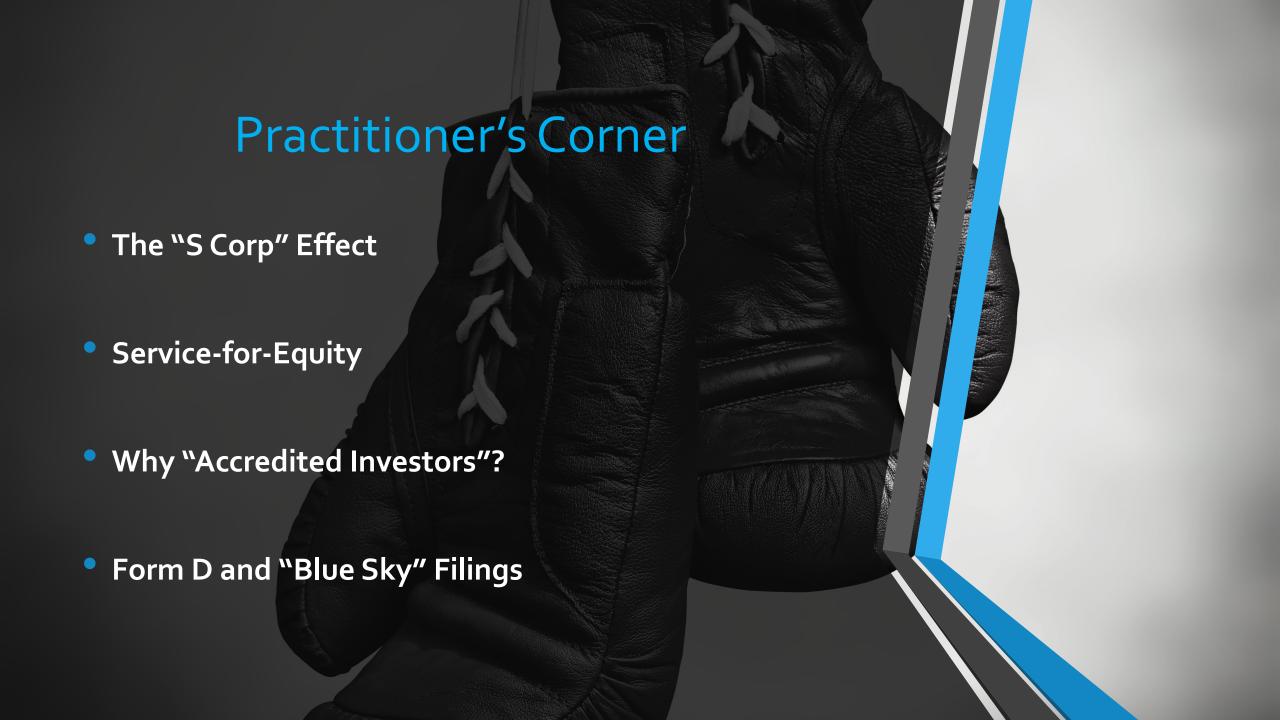


- But less common to be a series
- More flexible and simple for founders
- Similar conversion features as C-Note
 - Discount and/or Valuation Cap
 - But less complex regarding conversion events
- May have additional terms, like a "Side Letter":
 - "Most-Favored-Nation"
 - "Pro Rata" Purchase Rights
- Minimal reps and warranties by startup
- Minimal ancillary documents
- But not "Debt" a Contractual Right to Equity in the Future
 - No maturity date
 - No accrued interest



Most Common Pre-Seed Instruments – A Practical Comparison

	C-Note	SAFE
Typical Investor Perspective	Familiar	Uncertain
Complexity & Cost	More complex/higher cost	Simpler/lower cost
Founder Perspective	Minimal impact on FMV of common stock, more "stress" of debt, and increased dilution from interest conversion	No "stress" of debt, less dilution (i.e., no interest conversion), but impact on FMV of common stock less certain, and legal and tax treatment less certain
Typical for a "Round"	More common	Less common





Select Ethics Issues for Startup Counsel

- Who is the client?
- What is the scope of the representation?
- What about an attorney investing in the client?

Attorney-Client Relationship

- Model Rule 1.13 (Organization as Client)
 - (a) Lawyer represents an organization through its constituents if retained by an organization
 - (f) Lawyer must identify organization as client to shareholders, directors, etc. if reasonably should know there is a conflict between organization and shareholder, director, etc.
 - (g) Lawyer may represent both the organization and shareholders, directors, etc., subject to conflicts rules (i.e., disclosure, informed consent via signed waiver)
- Florida Rule 4-1.13 (Organization as Client)
 - Tracks Model Rule
- Comments:
 - Implications for attorney-client privilege with "joint representations"
 - Practitioner Preference represent the organization
 - Note: Model Rule 4.1 (Truthfulness in Statements to Others); Model Rule 4.2 (Communication with Person Represented by Counsel); and Model Rule 4.3 (Dealing with Unrepresented Person)
 - Formation Dilemma preempt issue by clearly stating representation changes to formed entity and signed waiver from founder(s) (Model Rule 1.9 (Duties to Former Clients))

Scope of Representation

- Model Rule 1.2 (Scope of Representation & Allocation of Authority Between Client & Lawyer)
 - (c) Lawyer may limit scope if reasonable under circumstances and client provides informed consent
- Florida Rule 4-1.2(c) (Objectives and Scope of Representation)
 - Lawyer and client may agree to limit scope if reasonable under circumstances and client provides informed consent in writing
- Comments
 - Scoping is critical for engagement letters, estimating costs and responsibility
 - Communication is key, especially with Alternative Fee Arrangements (AFAs) common with startups

Investment in a Client

- Model Rule 1.8(a) (Conflict of Interest: Current Clients: Specific Rules).
 - Lawyer shall not do business with client unless terms are "fair and reasonable" to the client and fully disclosed in writing in an understandable way to client, client is advised and has opportunity to seek independent counsel, and client provides informed consent in a signed writing
 - Other Rules
 - Model Rule 1.7 (Conflicts of Interest: Current Clients): Also need informed consent with disclosure of risk of lawyer's representation being materially limited (a)(2), and lawyer needs to follow (b) and decide if the lawyer can provide competent representation despite the conflict
 - Model Rule 1.5 (Fees): (a) Fees for representation must be reasonable
- Florida Rule 4-1.8 (Conflict of Interest; Prohibited Transactions)
 - Tracks Model Rule
- Comments
 - The Unicorn Dilemma is \$5mm in equity for \$50k worth of legal work a reasonable fee?
 - The Solution(?) Disclose and describe scenario/effect in detail (ABA Formal Opinion 00-418.QXD)

Summary

Startups Have Unique Financing Tools Available in the U.S.

Understand the Basics of Applicable Private Securities Laws

Understand Most Common Pre-Seed Instruments: C-Notes and SAFEs

Beware of Common Traps to Avoid Missteps and Unnecessary Expense

Be Aware of Innovative Legal Technology to Enhance Process

Be Mindful of Who the Client Is, What Is the Scope of Representation, and Rules on Attorney Investments in the Client

