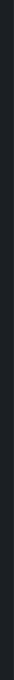


INVESTMENT
ESSENTIALS FOR
STARTUP FOUNDERS



FUNDRAISING

- **TYPES OF FUNDING**
- SECURITIES TRANSACTIONS
- READING TERM SHEETS
- SURVIVING DUE DILIGENCE
- LIVING WITH INVESTORS

EARLY-STAGE FUNDING OPTIONS



Debt Financing

Bank/Institution
Program
Rich Uncle



Equity Investment

Founder Investment
Angel Funding
Venture Capital



Strategic Investment

Joint Ventures
Corporate VC



Crowdfunding

Pre-sale Offers
Reg CF

FUNDRAISING

- FUNDING FORMS
- **SECURITIES TRANSACTIONS**
- READING TERM SHEETS
- SURVIVING DUE DILIGENCE
- LIVING WITH INVESTORS

OFFERING SECURITIES TO INVESTORS

- SECURITY –

- “... AN INVESTMENT CONTRACT FOR PURPOSES OF THE SECURITIES ACT MEANS A CONTRACT, TRANSACTION OR SCHEME WHEREBY A PERSON INVESTS HIS MONEY IN A COMMON ENTERPRISE AND IS LED TO EXPECT PROFITS SOLELY FROM THE EFFORTS OF THE PROMOTER OR A THIRD PARTY....”
- SEC v. W.J. HOWEY Co. (1946)

OFFERING SECURITIES TO INVESTORS

- COMMON EARLY STAGE SECURITIES –
 - DEBT INSTRUMENTS
 - PROMISSORY NOTES, CONVERTIBLE NOTES, SAFE NOTES
 - STOCK
 - COMMON, PREFERRED
 - OPTION CONTRACTS
 - STOCK OPTIONS, WARRANTS

OFFERING SECURITIES TO INVESTORS

- SECURITY OFFERINGS –

- ANY TIME A COMPANY, REGARDLESS OF WHETHER IT IS A LARGE, PUBLICLY TRADED COMPANY OR A SMALL, PRIVATELY-HELD COMPANY, PROPOSES TO USE AN INSTRUMENTALITY OF INTERSTATE COMMERCE IN ORDER TO ISSUE ITS SECURITIES, THE COMPANY, AS THE ISSUER OF THE SECURITIES, MUST REGISTER THE OFFERING PUBLICLY (SECTION 5 OF THE 33 ACT) **OR FIND AN EXEMPTION FOR THE TRANSACTION.**

OFFERING SECURITIES TO INVESTORS

- EXEMPT TRANSACTIONS –

THERE ARE A NUMBER OF STATUTORY PRIVATE PLACEMENT AND REGULATORY SAFE HARBOR AVENUES THAT ALLOW COMPANIES TO SELL SECURITIES WITHOUT ENGAGING IN THE LENGTHY AND EXPENSIVE PROCESS OF PUBLIC REGISTRATION, INCLUDING:

- SECTION 4(A)(2)
 - **REGULATION D (REG D)**
- INTRASTATE OFFERINGS
- CROWDFUNDING

RULE 506 TRANSACTIONS (REG D SAFE HARBOR)

RULE 506 ALLOWS ISSUERS TO RAISE AN UNLIMITED AMOUNT OF CAPITAL VIA THE SALE OF UNREGISTERED SECURITIES UNDER SECTION 4(A)(2) (FORMERLY 4(2)). THIS ALLOWS EXEMPT FUNDRAISING FOR OFFERINGS OF VARIED SIZES THAT INCLUDE THE FOLLOWING CHARACTERISTICS:

- UNLIMITED NUMBER OF “ACCREDITED” INVESTORS AND UP TO 35 NON-ACCREDITED INVESTORS
- ISSUER IS REQUIRED TO DETERMINE LEVEL OF SOPHISTICATION OF INVESTOR (MUST “REASONABLY BELIEVE” THAT EACH NON-ACCREDITED INVESTOR IS SUFFICIENTLY SOPHISTICATED/KNOWLEDGEABLE)
- NO GENERAL ADVERTISING OR SOLICITATION (IF ALLOWING NON-ACCREDITED)
- DISCLOSURE DOCUMENTS REQUIRED WITH SOMEWHAT AMBIGUOUS REQUIREMENTS FOR INCLUSION
- MUST FILE FORM D WITH THE SEC (AND COROLLARY STATE LAW FORMS IN EACH JURISDICTION IN WHICH A SECURITY IS SOLD PURSUANT TO THE OFFERING – LOEN IN CALIFORNIA)

RULE 506 TRANSACTIONS (REG D SAFE HARBOR)

ACCREDITED INVESTOR -

- A BANK, INSURANCE COMPANY, REGISTERED INVESTMENT COMPANY, BUSINESS DEVELOPMENT COMPANY, OR SMALL BUSINESS INVESTMENT COMPANY;
- AN EMPLOYEE BENEFIT PLAN, WITHIN THE MEANING OF THE EMPLOYEE RETIREMENT INCOME SECURITY ACT, IF A BANK, INSURANCE COMPANY, OR REGISTERED INVESTMENT ADVISER MAKES THE INVESTMENT DECISIONS, OR IF THE PLAN HAS TOTAL ASSETS IN EXCESS OF \$5 MILLION;
- A CHARITABLE ORGANIZATION, CORPORATION, OR PARTNERSHIP WITH ASSETS EXCEEDING \$5 MILLION;
- A DIRECTOR, EXECUTIVE OFFICER, OR GENERAL PARTNER OF THE COMPANY SELLING THE SECURITIES;
- A BUSINESS IN WHICH ALL THE EQUITY OWNERS ARE ACCREDITED INVESTORS;
- **A NATURAL PERSON WHO HAS INDIVIDUAL NET WORTH, OR JOINT NET WORTH WITH THE PERSON'S SPOUSE, THAT EXCEEDS \$1 MILLION AT THE TIME OF THE PURCHASE, OR HAS ASSETS UNDER MANAGEMENT OF \$1 MILLION OR ABOVE, EXCLUDING THE VALUE OF THE INDIVIDUAL'S PRIMARY RESIDENCE;**
- **A NATURAL PERSON WITH INCOME EXCEEDING \$200,000 IN EACH OF THE TWO MOST RECENT YEARS OR JOINT INCOME WITH A SPOUSE EXCEEDING \$300,000 FOR THOSE YEARS AND A REASONABLE EXPECTATION OF THE SAME INCOME LEVEL IN THE CURRENT YEAR; OR**
- A TRUST WITH ASSETS IN EXCESS OF \$5 MILLION, NOT FORMED TO ACQUIRE THE SECURITIES OFFERED, WHOSE PURCHASES A SOPHISTICATED PERSON MAKES."

RULE 506 TRANSACTIONS (REG D SAFE HARBOR)

DISCLOSURES -

OFFERS MADE EXCLUSIVELY TO ACCREDITED INVESTORS REQUIRE ONLY STRAIGHTFORWARD DISCLOSURES THAT INDICATE RELEVANT INFORMATION ABOUT THE COMPANY.

OFFERS MADE TO ANY NON-ACCREDITED INVESTORS MUST INCLUDE A FAIRLY ROBUST PRIVATE PLACEMENT MEMORANDUM (PPM) THAT CONTAINS EVERYTHING AN ISSUER WOULD GENERALLY NEED TO INCLUDE IN A PROSPECTUS USED FOR A REG A OR PUBLIC OFFERING, INCLUDING DESCRIPTIONS OF THE ISSUER'S:

- MARKET
- BUSINESS
- MATERIAL LEGAL PROCEEDINGS
- CAPITALIZATION
- STRUCTURE AND MANAGEMENT
- RISKS
- FINANCIAL DATA (BOTH EXISTING AND FORWARD-LOOKING)
- ANALYSIS

RULE 506 TRANSACTIONS (REG D SAFE HARBOR)

WHY YOU SHOULDN'T SELL TO NON-ACCREDITED INVESTORS —

- BURDENSOME AND EXPENSIVE DISCLOSURES
- ISSUER BEARS THE BURDEN OF PROVING INVESTOR SOPHISTICATION
- NO GENERAL SOLICITATION OF ANY KIND

FUNDRAISING

- FUNDING FORMS
- SECURITIES TRANSACTIONS
- **READING TERM SHEETS**
- SURVIVING DUE DILIGENCE
- LIVING WITH INVESTORS

NATIONAL VENTURE CAPITAL
ASSOCIATION (NVCA)
-
MODEL TERM SHEET

- OFFER TERMS
- DIVIDENDS
- LIQUIDATION PREFERENCE
- VOTING RIGHTS
- PROTECTIVE PROVISIONS
- ANTI-DILUTION PROVISIONS
- CONVERSION
- REGISTRATION RIGHTS
- INFORMATION RIGHTS
- FOLLOW-ON RIGHTS
- INVESTOR DIRECTOR
- ROFR
- DRAG-ALONG

FUNDRAISING

- FUNDING FORMS
- SECURITIES TRANSACTIONS
- READING TERM SHEETS
- **SURVIVING DUE DILIGENCE**
- LIVING WITH INVESTORS

PRIMARY DUE DILIGENCE FOCUS AREAS

- **CAP TABLE**
- **FINANCIALS**
- **INTELLECTUAL PROPERTY**
 - PRODUCT/SERVICE IP, TRADEMARKS
- **EMPLOYMENT ISSUES**
- **CONTRACTS**
 - CUSTOMER INFO, MATERIAL AGREEMENTS, LEASES, INSURANCE
- **LITIGATION**
- **COMPLIANCE**
 - TAX, FILINGS, LICENSES

FUNDRAISING

- FUNDING FORMS
- SECURITIES TRANSACTIONS
- READING TERM SHEETS
- SURVIVING DUE DILIGENCE
- **LIVING WITH INVESTORS**

NOW WHAT?

LIVING WITH INVESTORS

- OVERSIGHT
 - MANAGEMENT RIGHTS, INFORMATION RIGHTS, PROTECTIVE PROVISIONS
- DEAL PARTICIPANTS
 - FOLLOW-ON, APPROVALS
- CLAIMANTS
 - DERIVATIVE ACTIONS

RESOURCES

- LEGAL DOCS
 - ORRICK STARTUP FORMS LIBRARY (WWW.ORRICK.COM)
 - COOLEY GO (WWW.COOLEYGO.COM/DOCUMENTS)
 - NVCA (WWW.NVCA.ORG)
- REFERENCE
 - BRAD FELD – WWW.FELD.COM
 - BOOK - *VENTURE DEALS: BE SMARTER THAN YOUR LAWYER AND VENTURE CAPITALIST*
 - JOE WALLIN – WWW.STARTUPLAWBLOG.COM
 - MATT BARTUS – WWW.MATTBARTUS.COM
 - MORE FORMS – WWW.FOUNDERSWORKBENCH.COM