

Startup Capital Raising: Legal Insights and Strategies

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Summary by



InhouseVentures

Overview

As a founder, navigating the complexities of capital raising requires not only a keen understanding of your company's growth targets but also a robust legal and strategic framework. From selecting the right investors to managing your cap table and preparing for due diligence, every decision significantly impacts your startup's future.

This video by Sian McLachlan (Practice Leader at LegalVision) offers important insights and a comprehensive legal checklist designed to equip founders with the knowledge to successfully structure and secure funding while avoiding common pitfalls that could hinder your growth.

10-Point Summary:

1. **Introduction to Capital Raising:** Sian introduces a legal checklist for founders focusing on capital raising, highlighting the importance of structuring and investor selection.
2. **Company Structure for Equity:** Founders must establish a company structure to raise equity through shares or convertible notes, ensuring legal protection and asset safety.
3. **Debt Options:** Founders can also take on debt. Forming a company structure is recommended for growing businesses over a sole trader structure.
4. **Investor Types and Expectations:** Different investors have varied expectations, ranging from family and friends to angel investors and VC funds, both locally and internationally.
5. **Capital Needs for Milestones:** Founders should calculate the capital needed to reach the next milestone, considering the duration until the next fundraising to avoid frequent capital raising.
6. **Equity vs. Debt:** The choice between equity and debt affects company ownership and financial obligations, with equity offering ownership and debt typically involving repayment terms.
7. **Convertible Instruments:** Convertible notes and SAFEs (simple agreement for future equity) offer temporary debt that can be converted into equity, with conditions on future fundraising.

8. Due Diligence Preparation: Founders must prepare for investor due diligence, ensuring all company documents (such as a shareholders agreement) and legal aspects are in order.
9. IP and Legal Compliance: Ensuring the intellectual property is appropriately assigned to the company (from employees to suppliers), and compliance with legal standards is critical for investor confidence.
10. Data Room Setup: A well-organised data room facilitates the due diligence process, providing investors with necessary company documents and information.

Common mistakes founders should avoid:

- Handling Convertibles: If you issue too many convertible instruments, this can lead to an unwieldy number of shareholders and potential legal complexities.
- Shareholder Management: Exceeding 50 shareholders may force a company to adhere to public company regulations and takeover rules, complicating future fundraising.
- Dilution Management: Founders must be mindful of equity dilution when convertibles convert, understanding the minimum dilution and its potential increase.
- Cap Table Management: Regular updates to the cap table are necessary to reflect the current equity structure, especially after convertible instruments are issued.
- Preference Shares: These shares offer investors priority in liquidation scenarios, which can disadvantage ordinary shareholders (typically founders).

As a founder, you need to plan for both growth and potential challenges, balancing optimism with realistic assessments of business risks. It's essential to build and maintain strong relationships with investors by aligning expectations and understanding investment terms. If you require legal assistance with your capital raise, get in touch with LegalVision (<https://legalvision.com.au>) and request a free legal consultation. Mention you were referred by In-house Ventures to receive your first month free when signing up as a member.