

# STARTUP GUIDEBOOK

**UConn** | RESEARCH

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### Advisement:

The information contained in this guidebook is intended to be a general guide to starting a business related to a technology-based product or service. The Founders Agreement example is not a requirement but covers many of the issues the venture participants should consider and agree on as they move forward. No part of this booklet, attachments, or related discussions constitute legal advice or written opinion of counsel. For legal advice, please consult with an attorney.

## **About the Startup Guidebook:**

This guidebook was compiled by UConn Venture Development, a unit of the UConn Office of the Vice President for Research, to assist entrepreneurs working to setup and grow a business based on new technology. Founders, especially technical innovators, are focused on the research and development of their product. However, careful consideration at these common business issues will help your company grow and thrive.

This guidebook has a checklist providing guidance on critical, difficult, and complex issues that should be discussed by founders at the beginning of a business venture. The startup checklist covers the typical necessary actions and considerations of new companies. There is a Founders Agreement example and many key entrepreneurial resource links as well. Content is adopted from various resources, with specific links to entrepreneurs in the UConn ecosystem. In addition, the content is intended to be dynamic and updated frequently.

## **About UConn Technology Commercialization Services:**

Technology Commercialization Services (“TCS”) is the University of Connecticut’s technology transfer, venture development, and incubation enterprise. Simply put, TCS is focused on the translation of academic innovations into real world applications, products, and services.

Our goals are to bring together UConn researchers and the business community, in order to significantly enhance the commercial and societal impact of UConn’s research; identify and help move inventions by UConn faculty, staff, and students towards the market through licensing or new company formation; secure patent protection for new technologies, where warranted by market forces; connect our entrepreneurs to capital and mentors, and generate support for ongoing applied/translational research projects including industry partnerships.

We encourage you to contact us for help with the following:

- evaluate and protect a UConn invention
- find proof of concept and/or startup funding at UConn, from the investment community, as well as state and private sources
- receive coaching and mentoring for your new venture
- start a company
- license a technology
- incubate your business at UConn
- access UConn programs supporting innovation and entrepreneurship

For more information, visit the TCS webpage at <https://ovpr.uconn.edu/services/tech-transfer/>

# Startup Checklist

## Very Early Startup Checklist

### \_\_\_\_\_ **Viability of Product/Service**

Be brutally honest with yourselves and determine if your business is something that can make a profit. Determine the market and how many customers would be willing to pay for this good or service.

- Customer need
  - Is this a nice improvement or a must-have? Does it drastically improve life for the customer? If not, it may be better as a license than a stand-alone company.
- Market research
  - How large is your target market? Is it large enough to attract funding, keeping in mind that markets over \$200 million typically have the best chance of success? Are there competitors that are further ahead of you?
- Customer discovery
  - Have you talked with potential customers who are NOT friends and family? Aim to talk with at least 30-50 people to get a good sense of the landscape. Listen to their needs; do not present your solution until the end of conversation.

### \_\_\_\_\_ **Pitch Deck/Business Plan**

Developing a pitch deck is an important step because it forces you to think through the details of the business, including gaps in the team and financial projections. This should be a document that evolves with the business. It should be revisited and adapted on a regular basis.

- Business plan
  - How will you make money? Would the payment be enough to cover the costs of the business and make a profit? Don't underestimate the expenses and don't overestimate how easy it will be to get sales.

See: Pitch deck template for 5, 10, 15 minute pitches

<http://bit.ly/PitchDecktemplate>

### \_\_\_\_\_ **Identify Where to Get Help**

A range of resources available at the federal, state, or local level may help you establish your business. These resources include local chambers of commerce, innovation incubators, and government entities such as the Small Business Administration.

See: [Resources](#) at end of document

# Early Startup Checklist

## Establish Business - Register with the Government

### Choose a name

Choose a company name that is appealing and memorable to your target audience. You should do research to determine that it is not already being used by another company. This can be completed using Google searches and a corporate name search tool. Keep in mind your company name may be different than your product name, which may have a different audience.

### Resources:

- At the state level, check <https://www.concord-sots.ct.gov/CONCORD/online?sn=PublicInquiry&eid=9740>
- Check the USPTO for trademarks of the name (often important for product names.) <http://www.uspto.gov/trademarks/>
- Do a website name search, and reserve your URL address if available (often this is needed for a legitimate email at the beginning)
- Once registered, avoid changing the company name and “Doing Business As”

### Establish a legal business structure

Sole Proprietorship, Partnership, LLC, C-Corp, or S-Corp

Corporations and LLCs are the most popular business entity structures for small businesses because they protect the owners’ personal assets from business debts and liabilities. LLCs are also the most flexible business structure in terms of ownership and management. The difference between C-Corporations and S-Corporations is largely a matter of tax election. LLC and S-Corporation are pass-through corporations, which means that the profits and losses pass to the owners.

### Resources:

- Choice of Entity: Tax Implications by Peter Gruen and Amy Drais at Wiggin and Dana LLP <https://www.wiggin.com/publications/choice-of-entity-us-federal-income-tax-implications/>  
This post will provide a high level overview of the tax implications of each type of entity from a variety of perspectives: taxation of the entity, taxation of its owners and employees and concerns of potential investors. The entities discussed are limited liability companies, partnerships, C corporations and S corporations.

### Obtain a Federal Employer Identification Number (FEIN)

This nine-digit number, issued for free by the Internal Revenue Service, identifies a business entity for the life of the company. This is required for incorporation, financial accounts, and all tax filings.

### Apply online

<https://www.irs.gov/businesses/small-businesses-self-employed/apply-for-an-employer-identification-number-ein-online>

\_\_\_\_\_ Register your business with the Secretary of State

Determine the state in which you want to incorporate. If you incorporate out of Connecticut, most commonly in DE, you must still register to do business in Connecticut as a foreign entity.

CT State business registration

<https://portal.ct.gov/services/business/start-your-business/business-registration-and-licensing>

\_\_\_\_\_ Register for state and local taxes

Registering for state and local taxes will allow you to obtain a tax identification number (TIN), workers' compensation, unemployment, and disability insurance.

CT State Tax Registration Application

<https://portal.ct.gov/DRS/TSC/TSC-Help-Text/Online-Registration-Application>

## \_\_\_\_\_ **Build Your Team**

\_\_\_\_\_ Assign responsibilities to founders

The earlier that roles and responsibilities among co-founders can be established, the better. It is necessary to discuss issues such as the commitment of time and resources to the business and delegate the responsibilities of maintaining financial records and establishing a marketing approach. A founders' agreement should be drafted to record the agreements, including equity, vesting schedule, and indicate what happens if someone leaves.

See also:

[Founders' Agreement at the end of this booklet.](#)

\_\_\_\_\_ Seek industry advisors & mentors

Care should be taken not to seek only colleagues or friends. The advisors and mentors should fill in gaps in expertise or have much more experience in an area that rounds out your team's own skills. Advisors can shift in experience as needs change. Formal board members may not be necessary until you take on external funds.

\_\_\_\_\_ Consultants

Consultants can fill the gaps of expertise on your team. They can be a good choice for an early stage startup, as their expertise can facilitate and expedite the process. However, consultants need to be paid so you will likely need to raise some funds first. Not only is it rare to find a consultant who will work for equity, but it is important to think critically before assigning equity in an early stage venture. Complicated capitalization tables may make your venture unattractive to investors when you are ready to seek funding.

## \_\_\_\_\_ **Continue to Advance the Product**

\_\_\_\_\_ Build MVP (minimum viable product/prototype)

- If possible, conduct a shell of a product for the purposes of testing the marketplace and getting feedback. Watch how early adopters use the MVP.
- Except for the purposes of safety, you should not delay getting feedback from the market.
- Validate the solution. Are users eagerly asking when it will be available?

- Refine and repeat or pivot, depending on the outcomes of the above.

## **Assess Financing and Obtain Startup Capital**

Startups require a lot more capital than most people expect. And it is difficult to obtain startup funds. You should refrain from engaging with angel investors or venture capitalists until you have an almost fully functioning prototype with data, and even customers if possible. You not only have to show that the service or product works, but that people have such a need they are willing to pay for it, and there is a big enough market. Until then, you should consider focusing efforts on early grants or family/friends support.

Seek startup funding

Early grants (state, federal and private), family/friends, angel investors, venture capital

Resources:

What Type of Security Should You Use to Fund Your Venture? by Evan Kipperman, Adam Silverman and Lena Bae

<https://www.wiggin.com/publications/what-type-of-security-should-you-use-to-fund-your-venture/>

Perfect your pitch deck

Keep refining your pitch deck. Now, go back and get feedback from others on how the pitch comes across. What are your main points? Do not dwell on the technology. The investors want to know how they are going to make money if they invest in you and why you are the best one to take this forward. Stick with proven pitch deck templates, if possible. Make sure you have 5, 10, and 15 minute pitch decks, as well as a 30-second elevator pitch.

Pitch deck template for 5, 10, 15 minute pitches

<http://bit.ly/PitchDecktemplate>

## **Establish Business Basics/Choose Service Providers**

Forming strong partnerships with your suppliers and service providers is important to ensure that the material and support you need for your product or service is available and affordable.

Legal

- Obtain intellectual property protection (trademarks, patents, copyrights)

If protecting intellectual property (IP) is important to your business, you must obtain the necessary legal protections. In most cases, obtaining the proper IP protections will require the assistance of an attorney. For others, such as copyright, trademark, or even provisional patent protection, you may be able to file on your own.

If UConn owns the IP related to your new venture, work with Technology Transfer experts in the Office of the Vice President for Research to obtain a license to this patent for your company. Even if the inventor is a co-founder of the company, the IP is often not owned by the inventor. Also, if the inventor is an employee of UConn, if any of the invention was made possible by research, facilities or other property of UConn, make sure the ownership is clear.

Resource:

UConn Technology Commercialization Services

<https://ovpr.uconn.edu/services/tech-transfer/>

You should also conduct a patent search (Google Patents or USPTO) to make sure there is Freedom to Operate. Even though your invention is different, if there is an existing patent that has broad claims that encompass your product, you need to be informed while pursuing your new venture.

Resource:

U.S.P.T.O. – Trademark Search

<https://www.uspto.gov/trademarks-application-process/search-trademark-database>

- Establish attorney-client relationship

It is important to find adequate legal representation early on to assist with many legal procedures. However, parties should avoid hiring a lawyer too soon before they know what they want or need from their counsel. Startups should consider a specialist, someone who is local and focused on startups, not a college friend or relative. To increase your chances of success, it is important to seek support from experienced and specialized service providers.

#### \_\_\_\_\_ Accounting

- Establish proper accounting

Keeping accurate financial records of revenues, costs, and expenses will save you time and hassle later. Invest in a software package such as Quickbooks that can make finances easier with functions such as easy invoicing, payroll, financial reports, etc.

#### \_\_\_\_\_ Banking

- Open a bank account and merchant account

It is critical to set up a business bank account to separate business and personal funds. Certain grants will audit your financial system before releasing funds.

- Get a business credit card

Establishing a strong line of credit for your business will help secure future capital from a bank or investor. Once your business has a credit card, ensure timely payment of credit bills and take advantage of incentives such as reward programs.

#### \_\_\_\_\_ Insurance

- Satisfy insurance requirements

Incorporating or forming a legal business entity does not automatically provide business

insurance. Most businesses purchase general business insurance from an insurance provider. Corporations and LLCs that hire employees will also need unemployment, disability, and workers' compensation insurance.

Resource:

CT Insurance Department

<http://www.ct.gov/cid/site/default.asp>

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#### Secure IT

- Protecting company information stored on your computers and electronic devices is important for the security of your business. Separate business and personal files, ideally on separate computers, keep up to date with software updates, use encryption software to protect customers' financial information during a transaction, and make sure you back up data often or use services that back it up automatically.

## Secondary Startup Checklist

Some of these items are important as you interact with people who could help your business. Looking for investors, networking events, and growing a social media presence can be helpful, but they can also divert your attention from the main focus: your fledgling product or service. Sometimes it is better to stay focused and in stealth mode.

### \_\_\_\_ **Establish a Brand and Presence**

\_\_\_\_ Develop logos, color schemes, images

These help potential customers envision your product or service.

\_\_\_\_ Establish a web presence

- Build/host a website

After getting a matching domain name, at the right time a website can be set up. Think about who is the target audience for your site. If your product is many years from commercialization, the website's main goal might not be to actually market the product, but instead provides legitimacy to your new venture.

- Social media profiles

In today's business world of Internet searches and social media, having various social media accounts that are both memorable and relevant to the industry creates opportunities for new customers and potential profit through marketing.

Consider top sites for your industry: [Twitter](#), [Facebook](#), [Instagram](#), [LinkedIn](#)

15 Tips to Grow a Social Media Audience for Your Startup: <http://bit.ly/2FIVJhU>

\_\_\_\_ Order business cards

Business cards are important when forming a business when you are trying to network with as many people as possible. Just as in the case of a company website, business cards also provide legitimacy to your new company.

### \_\_\_\_ **Hire Employees**

Hiring employees is not a simple matter and there are a number of requirements as an employer. Important considerations for an employer include assessing the financial circumstances of the business, identifying employee benefits or alternative means to compensate employees, and understanding employer regulations in the legal environment.

Resource:

Small Business Administration Guide, Hiring your first employee

<https://www.sba.gov/business-guide/manage-your-business/hire-manage-employees>

\_\_\_\_ Understand employer responsibilities

You will need to register for state and federal employer taxes. There are a number of laws and regulations that apply to employers, including state and federal posting laws, workers' compensation insurance, state and federal unemployment insurance, and potentially disability and health insurance, among other requirements.

\_\_\_\_ Register with the Department of Labor, State and Federal

- State of Connecticut Department of Labor

<https://wage.ctdol.state.ct.us/CTERS/index.aspx>

- Federal  
<https://www.irs.gov/businesses/small-businesses-self-employed/apply-for-an-employer-identification-number-ein-online>

\_\_\_\_\_ Get workers' compensation insurance

- CT Insurance Department  
<http://www.ct.gov/cid/site/default.asp>

## \_\_\_\_\_ **Operations**

\_\_\_\_\_ Satisfy Business licensing and permit requirements

Most state and local governments require businesses to obtain licensing before they operate. Sometimes a license is not needed until you start commercializing your product.

- For Connecticut, the Connecticut Economic Resource Center (CERC) directs businesses to the appropriate agencies to ensure they are properly registered, licensed, or permitted within the state.

Connecticut Economic Resource Center  
<https://www.cerc.com/licenses/>

\_\_\_\_\_ Draft internal documents for business

Policies, confidentiality agreements.

It is important to establish early on the documents that will govern the business and the employees.

\_\_\_\_\_ Draft external documents for business

Invoices, letters, standard contracts.

Establishing external documents for the business helps to establish legitimacy and allows you to have standard contracts for early business decisions and transactions.

## \_\_\_\_\_ **Sales & Marketing**

\_\_\_\_\_ Refine product, marketing & sales approach

Once you have adequately specified how your product solves a problem in the market, devise a clear message for your customers explaining why they will need your product or service and why they cannot find a comparable product or service elsewhere.

\_\_\_\_\_ Test your product messaging, ideally with comparative A/B type of tests

\_\_\_\_\_ Establish and work with a network

\_\_\_\_\_ Get a sales person, sales team, or individual representatives in place

It is never too early to start making connections with potential customers. An important step to this end is putting in place a salesperson or team that will provide potential customers with vital information about your product or service.

## **Founders' Agreement Format and Guide**

The following includes a sample founders' agreement and notes that provide explanations for the clauses used in the sample agreement.

# Founders' Agreement

## 1. Recitals

Agreement made [date] between [name], of [street address], [city], [state], [zip], [name], and [name], of [street address], [city], [state], [zip].

A. The parties desire to organize under the laws of the State of [state of organization] a [type of organization] to be known as [name of organization], or such other name as the parties may select, for the purposes set forth below.

B. The proportionate interests of the parties in the capital of the [type of organization] are to be as set forth below.

Now, therefore, in consideration of the mutual covenants and other valuable consideration exchanged, the parties hereby agree as follows:

## 2. Formation of [Type of Organization]

In consideration of the mutual promises hereinafter set forth, the parties hereby agree to form a [type of organization] (referred to herein as the “[type of organization]”) under the laws of the State of [state of organization].

## 3. Alternative: [Type of Organization] Agreement Attached

In consideration of the mutual promises hereinafter set forth, the parties hereby agree to form a [type of organization] (referred to herein as the “[type of organization]”) under the laws of the State of [state of organization]. The [type of organization] agreement for the [type of organization] shall be substantially in the form attached hereto as Exhibit [number].

## 4. Name of [Type of Organization]

Subject to availability, the name of the [type of organization] shall be [name of organization].

## 5. Duration

The duration of this Agreement shall be for [XX] years, provided, however, that this Agreement may be terminated prior to the end of its original term upon the occurrence of one of the following events: [description of triggering events]. Notwithstanding any term in this section, once the legal entity has been formed, the company has perpetual life.

## 6. Initial Owners

The initial owners of the [type of organization], their respective percentage interests in the capital of the [type of organization] as of [date], and the amount and type of their contributions to the [type of organization], shall be the following:

Owner	Percentage Interest	Contribution
[name of owner]	[percent]	[type of contribution]
[name of owner]	[percent]	[type of contribution]
[name of owner]	[percent]	[type of contribution]

## **7. Buy-Sell Agreement**

The parties shall enter into a buy-sell agreement in substantially the form attached hereto as Exhibit [number], which buy-sell agreement shall provide: [description of terms].

## **8. Alternative: Right of First Refusal**

It is agreed that none of the parties will sell, pledge, or otherwise encumber their interest in the [type of organization] without first offering the same to the other parties at a price to be fixed by mutual agreement and in the absence of agreement by an appraiser to be appointed by the [name]. The offer shall be in writing and shall remain open for a period of [number] days.

## **9. Matters Requiring Unanimous Consent**

Notwithstanding anything herein to the contrary, but subject to the terms of the [type of organization] agreement, the parties agree that none of the following actions may be taken without the unanimous written consent of all of the parties: [description of actions].

## **10. Employment of Attorney; Expenses of Organization**

The parties shall employ [name] as legal counsel for the purpose of drafting the [type of organization] agreement and other documents referred to herein. Counsel shall also advise the parties and the [type of organization] to be formed pursuant hereto in connection with each step in its organization. All charges for legal services, and all fees associated with organizing the [type of organization], shall be paid for by the [type of organization]. However, each of the parties hereto agrees to advance their pro rata share of such expenses as required.

## **11. Effect of Agreement**

The parties agree and acknowledge that execution and performance of this agreement shall not create a [type of organization] among the parties, and that the [type of organization] referred to herein shall not come into existence until the parties have negotiated and executed the definitive form of [type of organization] agreement, complied with all applicable legal requirements relating to valid formation and organization of a [type of organization], and have made each of the contributions to the [type of organization] referred to herein. Until the conditions specified in the previous sentence are satisfied, no party shall have any authority to make any representations or commitments on behalf of the [type of organization] to be formed, and each of the parties agrees to indemnify the other parties against any liabilities to which they may become subject as a result of the indemnifying party's breach of this section. In the event that the [type of organization] has not been formed by [date], this agreement, other than the indemnities provided for herein, shall be null and void and of no further force and effect.

## **12. Intellectual Property Rights and Competitive Activities of the Parties**

A. For valuable consideration, the receipt of which is hereby acknowledged, each of the parties does hereby transfer all of [his/her] right, title, and interest to the [type of organization] in ideas and proprietary data, if any, to certain technology, inventions, and devices, described as products that have been, or will be, developed manufactured, or sold under the Business Plan, which was prepared by the [type of organization], or otherwise, including, but not limited to, all right, title, and interest in any data or other proprietary information, or know-how related, necessary, or useful to the design, engineering, development, manufacture, or sale of said products, or to perfecting patent or trademark rights in and to said products, or improvements or modifications thereon. Each of the parties covenants with the [type of organization] that [he/she] will prepare detailed drawings, plans, and specifications of the said personal property and such other materials as are reasonably necessary for the purposes of ascertaining the potential patentability of said personal property, and [he/she] will cooperate fully with the [type of organization], including any

additional research or the preparation of any additional materials or modifications necessary in patent searches, examinations, and applications in this regard if the [type of organization] decides to apply for patents upon any of the said personal property.

B. For valuable consideration, receipt of which is hereby acknowledged, each of the parties agrees that, except as permitted or directed by the [type of organization]'s Board of Directors, [he/she] shall not divulge, furnish, or make accessible to anyone or use in any way (other than in the ordinary course of the business of the [type of organization]) any confidential or secret knowledge or information of the [type of organization] which [he/she] has acquired or become acquainted with or will acquire or become acquainted with prior to any termination of [his/her] employment by the [type of organization] (including employment by any affiliated companies prior to the date of this Agreement), with respect to the [number] parties who are employees; and, with respect to the parties who are not employees, any such information which has become known by such parties during the period of the party's involvement with the [type of organization] as a Director, Consultant, or otherwise, whether developed by [himself/herself] or by others, concerning any trade secrets, confidential, or secret designs, processes, formulae, plans, devices, or material (whether or not patented or patentable) directly or indirectly useful in any aspect of the business of the [type of organization], any confidential customer or supplier lists of the [type of organization], any confidential or secret development or research work of the [type of organization], or any other confidential or secret aspects of the business of the [type of organization]. Each party acknowledges that the above described knowledge or information constitutes a unique and valuable asset of the [type of organization] acquired at great time and expense by the [type of organization] and its predecessors, and that any disclosure or other use of such knowledge or information other than for the sole benefit of the [type of organization] would be wrongful and would cause irreparable harm to the [type of organization]. Each party agrees to refrain from any acts or omissions that would reduce the value of such knowledge or information to the [type of organization]. The foregoing obligations of confidentiality, however, shall not apply to any knowledge or information which is now published or which subsequently becomes generally publicly known, other than as a direct or indirect result of the breach of this agreement by any party.

C. For valuable consideration receipt of which is hereby acknowledged:

a. Each party agrees that, during the period of [his/her] affiliation with the [type of organization] in any manner or capacity (e.g., as an advisor, principal, agent, partner, officer, director, shareholder, employee, member of any association, or otherwise) (or any affiliated companies) for the [number] parties who are employees; or during the period of [his/her] involvement with the [type of organization] with respect to the parties who are not employees; and for a period of [number of years] year(s) thereafter, [he/she] shall not, directly or indirectly, engage in competition with the [type of organization] anywhere within the United States in any manner or capacity (e.g., as an advisor, principal, agent, partner, officer, director, shareholder, employee, member of any association, or otherwise) in any phase of the business which the [type of organization] is conducting during the term of [his/her] employment, including but not limited to the design, development, manufacture, distribution, marketing, leasing, or selling of any [description of product] and of accessories, devices, or components related to the products or services being sold by the [type of organization], provided, however, that ownership by a party, of a passive investment, of less than [amount]% of the outstanding shares of authorized stock of any corporation listed on a national securities exchange or publicly traded in the over-the-counter market shall not constitute a breach of this Section.

b. Each party agrees that, during the period of [his/her] affiliation with the [Type of Organization] in any manner or capacity (e.g., as an advisor, principal, agent, partner, officer, director, shareholder, employee, member of any association, or otherwise) (or any affiliated companies) for the [number] parties who are employees; or during the period of [his/her] involvement with the [Type of Organization] with respect to the parties who are not employees; and for a period of [number of years] year(s) thereafter [he/she] will not, directly or indirectly, assist or encourage any other person in carrying out, directly or

indirectly, any activity that would be prohibited by the above provisions of this Section if such activity were carried out by such party, either directly or indirectly, and in particular each party agrees that [he/she] will not, directly or indirectly, induce any employee of the [Type of Organization] to carry out, directly or indirectly, any such activity.

### 13. Representations of Parties

A. Each party is not obligated under any contract (including licenses, covenants, or commitments of any nature) or other agreement, or subject to any judgment, decree or order of any Court or administrative agency which would conflict with [his/her] obligation to use [his/her] best efforts to promote the interests of the [Type of Organization] or which would conflict with the [Type of Organization]'s business as conducted or as proposed to be conducted. Neither the execution nor delivery of this Agreement, nor the carrying on of the [Type of Organization]'s business as an officer, director or employee by a party, nor the conduct of the [Type of Organization]'s business as conducted or as proposed to be conducted, will conflict with or result in a breach of the terms, conditions, or provisions of or constitute a default under any contract, covenant, or instrument under which a party is now obligated. Founder has previously delivered to special counsel for the founders copies of all agreements between [him/her] and [his/her] previous employers and other persons that are relevant.

B. Each party does not own, directly or indirectly, of record or beneficially, more than [amount]% of the outstanding voting securities (which shall include any security or option convertible into or exercisable for voting securities) of any corporation other than the [type of organization], nor is a party a general partner or limited partner in a [type of organization] in which [he/she] has a direct or indirect interest in more than [amount]% of the profits of such [type of organization].

a. Without having undertaken to determine independently the accuracy or completeness of either the representations and warranties of the [type of organization] contained herein or any of the information contained in the Business Plan, a party has no reason to believe that the representations and warranties of the [type of organization] contained in Section [number/letter] of this Agreement are not true and correct, and is familiar with the contents of the Business Plan and has no knowledge of any material fact, condition, or information not disclosed in the Business Plan which has adversely affected or may adversely affect the business of the [type of organization].

### 14. Vesting of Shares

### 15. Vesting of Shares

All of the shares owned by the parties shall be subject to the right and option of the [type of organization] and the founders to purchase shares. The shares shall cumulatively vest in accordance with the following schedule:

Date	Percentage of Share Which Are Vested Shares as of Such Date
[date]	[amount of percentage]%

The shares shall cease to vest further in accordance with the above schedule on the date (“Termination Date”) on which a party shall cease to be a “Service Provider” (as hereinafter defined) (a “Termination”). Hereinafter, the shares which are vested are sometimes referred to as the “Vested Shares,” and the shares which are not so vested are sometimes referred to as the “Unvested Shares.”

For the purpose of this Agreement, a party shall be deemed to be a “Service Provider” to the [type of organization] for so long as the party is employed by the [type of organization], or a parent or subsidiary of the [type of organization]. A leave of absence (regardless of the reason therefor) shall be deemed to constitute the cessation of Service Provider status as of the commencement date of the leave, unless such leave is authorized by the [type of organization] in writing and the party recommences providing services prior to the expiration date of such leave. Accordingly, the party shall receive credit as a Service Provider to the [type of organization] during a leave of absence only if the leave is authorized by the [type of organization] and the party recommences providing services on or prior to the expiration date of the leave.

## **16. Option to Purchase Vested Shares**

In the event of a Termination of any party, for any reason or for no reason, including involuntary termination of employment, termination of employment for cause or without cause, or temporary or permanent disability or death, then the [type of organization] and/or the founders shall have an unconditional option to purchase from the party, or his or her personal representative, as the case may be, all or any part of the Vested Shares owned by the parties on the Termination Date, at a price equal to the original issue price of such Vested Shares.

## **17. Forfeiture of Shares**

Notwithstanding anything contained herein to the contrary, if any party engages in wrongdoing, the founders shall have the right, in their sole and good faith judgment, to suspend (temporarily or permanently) the vesting of any or all of the party’s Unvested Shares, extend the date for such vesting, suspend (temporarily or permanently) the transferability of any or all of the Vested Shares, require the forfeiture of any or all of the Vested Shares then held by the party, or take any other actions in respect of any or all of the Vested Shares or this Agreement.

## **18. Governing Law**

This Agreement shall be governed by and construed in accordance with the laws of the State of [name of state] applicable to contracts between [name of state] residents entered into and to be performed entirely within the State of [name of state].

## **19. Survival**

The representations, warranties, covenants, and agreements made by the parties herein shall survive any investigation made by any founder or the [type of organization] and shall survive the closing of the transactions contemplated hereby.

## **20. Successors and Assigns**

Except as otherwise provided herein, the provisions hereof shall inure to the benefit of, and be binding upon, the successors, assigns, heirs, executors, and administrators of the parties hereto, provided that none of the parties is intended to have any right, remedy, or privilege hereunder.

## **21. Entire Agreement**

This Agreement and the other documents delivered pursuant hereto constitute the full and entire

understanding and agreement between the parties with regard to the subjects hereof and thereof.

## **22. Amendments and Waivers**

Except as provided above, any term of this Agreement may be amended and the observance of any term of this Agreement may be waived (either generally or in a particular instance and either retroactively or prospectively), with the written consent of the [type of organization] and the holders of at least [amount]% of the [outstanding shares (including any converted shares that have not been sold to the public)]. Any amendment or waiver effected in accordance with this section shall be binding upon and equally affect each holder of any securities purchased under this Agreement at the time outstanding (including securities into which such securities have been converted), each future holder of all such securities, and the [type of organization].

## **23. Remedies**

Each holder of Unvested Shares and Vested Shares will be entitled to enforce its rights under this Agreement specifically, to recover damages by reason of any breach of any provision hereof and to exercise all other rights existing in its favor. Each holder of Unvested Shares and Vested Shares agrees and acknowledges that money damages may not be an adequate remedy for any breach of the provisions of this Agreement and that each holder may, in its sole discretion, apply to any court of law or equity of competent jurisdiction for specific performance in addition to injunctive relief in order to enforce or prevent any violations of the provisions of this Agreement.

## Notes:

These notes provide guidance on clauses in the Founders' Agreement.

### 1. Recitals

The recitals provide the general background for the agreement and proposed relationship between the parties. The recitals should contain:

- An acknowledgment that the parties intend to form the chosen type of organization with a specified name; and
- An acknowledgment that the proportionate interests of the parties in the capital of the organization will be as set forth in the agreement.

If appropriate, the recital may include an acknowledgment that the parties intend to enter into various other agreements relating to their relationship to the organization or and among each other (e.g., buy-sell agreements, employment contracts).

### 2. Formation of [Type of Organization]

As a general rule, the ownership structure of the business should protect the rights of the founders while still providing incentives and flexibility to grow and adapt the business. The parties should set out their intent and agreement to form a new organization under the applicable laws of the state specified in the agreement. If appropriate, the parties might include some of the procedural details regarding the formation and organization process, such as:

- Preparation of a [type of organization] agreement; and
- Filing of fictitious business name statements.

In some cases, the proposed [type of organization] agreement will be appended to the agreement (see Alternative: [Type of Organization] Agreement Attached below).

### 3. Alternative: [Type of Organization] Agreement Attached

If there is sufficient time, the parties might elect to draft the [type of organization] agreement and attach it to the agreement as an exhibit. This forces the parties to address the various issues which will ultimately come up in organizing the [type of organization] before the fees and costs of forming the entity are incurred.

### 4. Name of [Type of Organization]

The parties should set out the proposed name of the [type of organization]. Steps should have been taken to check on the availability of the proposed name and, if necessary, reserve the name before use. If a name has not been reserved in advance, provision should be included for selecting an alternate name. The parties should also review the trade name laws of the given state and professional ethics rules before selecting a name. The name clause of the [type of organization] agreement might also include a clause requiring that the organization's property be held exclusively in the name of the organization, rather than in the name of one or all of the parties.

### 5. Duration

While, in most cases, the duration of the agreement will be for a fixed term, the parties may also wish to include a brief description of any events which might cause the agreement to end (e.g., death of one or more of the owners, failure to achieve specified financial or business milestones, etc.). A sentence may also be included that states that once the legal entity is formed, the entity has perpetual life.

### 6. Initial Owners

A general description of the proposed capitalization of the [type of organization] should be included in the agreement. In particular, the parties should include:

- A list of each of the initial owners;
- A list of their respective shares in the capital of the [type of organization]; and

- The amount and type of contributions that each will be making in exchange for their interest.

## **7. Buy-Sell Agreement**

The parties may wish to enter into a Buy-Sell Agreement relating to transfers of their interests. If desired, a copy of the agreement may be attached to the agreement as an exhibit. If no copies are attached, the parties should include:

- A general description of the terms of the Buy-Sell Agreement, including the trigger events (e.g., death, termination of employment, etc.);
- Whether occurrence of a particular trigger event creates an option or an obligation to purchase an interest;
- The purchase price; and
- The terms of payment.

## **8. Alternative: Right of First Refusal**

In lieu of a full buy-sell arrangement, the parties might consider more modest restrictions on the ability of the owners to transfer their interests. For example, the parties may impose a right of first refusal procedure on any transfer under which a party proposing to transfer his/her interest must first offer the interest to the other owners on the same terms or on terms specified in the agreement.

## **9. Matters Requiring Unanimous Consent**

While authority regarding day-to-day operations may be delegated to one or more managers, there are almost always certain matters which should require the consent of all the owners or some percentage of the owners rather than just a mere majority-in-interest. For example, dissolution and/or sale of all the entity's assets will typically be events that must be approved by all the owners, and any other events should also be specified in the agreement.

## **10. Employment of Attorney; Expenses of Organization**

Assuming that the parties wish to employ an attorney to assist them in organizing the [type of organization], provision should be made in the agreement for the appointment of such an attorney and describing the task to be carried out by the attorney (e.g., drafting the [type of organization] agreement and other documents, as well as applying for any regulatory approvals). Provision should be made for the expenses associated with organization, including legal fees and other fees payable to the state or local agencies. In general, the parties will agree to advance such expenses, subject to reimbursement by the [type of organization] after organization.

## **11. Effect of Agreement**

Since this is a preformation agreement, intended only to establish the mutual understanding of the prospective owners as to the business and management of the organization that will be formed, the parties should include:

- An acknowledgment that the agreement is not intended to form a [type of organization];
- Any conditions which must be satisfied for the [type of organization] to come into existence, such as finalization and execution of the [type of organization] agreement by a specified date; and
- An agreement by the parties that they will each indemnify the others for liabilities incurred by any party representing that a [type of organization] has, in fact, been formed.

## **12. Intellectual Property Rights and Competitive Activities of Parties**

Parties active in the organization business will, along with every other key employee of the organization, execute and deliver a standard form of assignment of inventions and confidentiality agreement.

- The assignment is intended to convey all of the party's legal rights in the organization's basic technology to the organization and to remove any incentive for the party to attempt to exploit the

technology other than through the organization.

- The assignment should be permanent and survive the party's departure from the organization.
- The assignment should include the party's agreement to assist the organization in effecting the transfer, such as by executing documents which might be required to assign patents and patent applications.
- The party might be required to prepare appropriate documentation, including a full written description of know-how and trade secret information.

Some founders will request additional agreements and representations from certain persons with respect to the intellectual property rights underlying the organization's business plan. These agreements and representations can either be made in the founders' agreement or can be set out in a separate agreement delivered to the organization and the founders before the closing.

When the proposed business activities of the organization are dependent upon technology, inventions, and ideas which may have been developed by the party before the establishment of the organization, it is incumbent on the organization to secure from the party a full assignment of all of the party's right, title, and interest with respect to such items. The scope of the assignment is often difficult to define and it usually is convenient to refer to the technology and products referred to in the organization's business plan. For example, the assignment might cover technology, inventions, and know-how related, necessary, or useful to the design, engineering, development, manufacture, and/or sale of the products referred to in the business plan.

The assignment of inventions agreement will be accompanied by various restrictions on the party's ability to disclose specified confidential information of the organization that the party may have acquired during the establishment of the organization. In many cases, the parties may have been involved in extensive research and product development efforts before the financing.

- The purpose of this type of representation is to make it clear that the results of that work, including the know-how, data, plans, and designs arising therefrom, are owned by the organization and are to be treated as trade secrets of the organization by the party.
- The scope of the agreement might even extend to financial information, customer and supplier lists, and organization business strategies that, while not strictly meeting the classic definition of trade secrets, nonetheless can be quite valuable to a competitor of the organization.
- The party will also be called upon to execute the organization's standard non-disclosure agreement to cover proprietary information that may be developed in the future.

Some founders will seek some sort of agreement from the parties that will provide the founders with assurances that the parties will not compete with the organization, either during the term of the party's affiliation with the organization or after the party is no longer actively involved with the organization.

- The lawful scope and validity of a non-competition agreement will vary between states.
- The general thrust of the representation will usually be that the party will refrain from competing with the organization in any capacity (e.g., advisor, principal, agent, partner, officer, director, or shareholder) in any phase of its business.
- The party will be restricted from assisting or encouraging others (e.g., other employees) in competing with the organization.
- The term of the restrictions will depend upon the negotiating strengths of the parties and applicable law.
- It is not uncommon for the agreement to extend for as long as 2 to 5 years after termination of the party's employment.

### **13. Representations of Parties**

Parties are often asked to provide a number of representations and warranties regarding their personal activities as they relate to the organization's business. These representations may be included as part of all of the general representations provided by the organization; however, it is probably better practice to place them in a separate section so that it is clear to all parties what statements are being made by the party. In some cases, the separate section may also include other important agreements of the party, such as agreements to assign various tangible and intangible assets to the organization and covenants not to engage

in competitive activities in relation to the organization.

One important area of concern for founders is the existence of any contract or agreement between a party and any third party that might restrict the party's ability to perform his or her specified duties for the organization.

- Founders will want the opportunity to review any contracts or agreements that the party might have with a prior employer that might restrict the party's ability to practice any inventions or new ideas that may be key elements of the proposed business of the organization or that might attempt to impose restrictions on the party's activities in specified business areas.
- Prudent founders will not close a financing transaction until they are completely satisfied that the parties will not become embroiled in a dispute with former employers regarding a prior confidentiality or non-competition agreement.

If it appears that the party's proposed activities with the organization will conflict with a prior contract or agreement that the party has with any of his or her former employers, counsel for the organization and for the founders should carefully consider appropriate options and strategies.

- The party may be able to simply approach the former employer on an informal basis and obtain the requisite approvals.
- If there is little or no possibility that the former employer will be willing to waive any of its protection, the founders must decide whether or not they are willing to take the risks associated with potential litigation at some point, probably after significant funds have been expended and the organization's product is about ready to come to the marketplace.

While the founders may rely upon the representations that are provided by the parties, it is important that the founders and their counsel have the opportunity to review the precise terms of any contract or agreement on the subject that might exist between the party and the third party.

- The prior agreement may contain a detailed list of those areas in which the activities of the party may be restricted.
- Entrepreneurs will frequently take comfort that a former employer has shown little or no interest in developing a specific new product or technology.

Nonetheless, the non-disclosure or non-competition agreement that remains in place with the former employer will cover technology that is essential to the new venture's proposed business. As such, it is important to carefully review the scope of prior agreements and the precise terms of any restrictions (e.g., duration, location, and activities). Related party transactions, which generally include any transaction between the organization on the one hand and a party, officer, director, or significant shareholder, or a relative or affiliate thereof, on the other hand, can raise many conflict-of-interest considerations.

- Certain transactions will be the subject of a separate representation and warranty by the organization.
- It is important to have each of the parties' shareholders provide information on this subject.
- Some representation should be provided to the effect that, except as otherwise disclosed, neither the party, nor any members of the immediate family of such person (e.g., spouse or children), nor any corporation or other form of business entity in which the party, or any member of his or her immediate family, has a material interest (e.g., more than a 5 percent equity or income interest) is a party to any transaction to which the organization is also a party and does not have any material interest in any person with whom the organization does or intends to do business.

Parties are often involved in the day-to-day business activities of the organization and the founders will want some assurances that such persons will continue to be able to devote their full efforts to performing their duties and responsibilities.

- A representation might be provided to the effect that the party will devote himself or herself to the organization on a full-time basis and will not engage in any other business activity, either on a full-time or part-time basis, without regard to whether the person is to be compensated for such other activities.
- Appropriate exceptions are permitted for participation in charities and similar types of organizations.
- The representation might be supplemented by some type of employment agreement.

## **14. Vesting of Shares**

Whether or not shares held by parties are to be subject to vesting provisions is often a heated topic of negotiations. In startup situations, vesting provisions of some type are typically imposed. When investments are made in more mature organizations, vesting provisions may not always be imposed.

The primary purpose of vesting provisions and associated repurchase rights is to provide a mechanism for the parties to earn their equity by continuing to work for the organization. In most cases, the parties will have purchased their interest in the organization for a nominal or relatively low purchase price, usually at a price per share much less than the current market value of the shares inherent in the price paid by the founders. The founders have an interest in ensuring that the parties continue to serve the organization and help generate the returns anticipated by the founders before the parties are able to capitalize on the appreciation in their interest created by the financing.

Many combinations can be used in establishing the vesting period and the rate of vesting. Many outside founders have their own preferences that are expressed during the course of negotiating the terms of a financing arrangement. As a general rule, vesting occurs over a period of 4 to 5 years. In most cases, none of the shares will vest until the employee has been with the organization for a specified period of time.

Once the employee has been with the organization for the agreed-upon minimum period, a portion of the shares will vest and the remaining shares usually will continue to vest on a linear basis over the remainder of the vesting period. For example, none of the employee's stock may vest for the first 2 years of the purchaser's employment, but then 50 percent of the shares will vest when the 2-year period is completed. Thereafter, the remaining 50 percent of the shares might vest at the rate of 2 percent a month for the next 25 months, although it is possible to use daily, quarterly, or annual vesting.

If the organization has been in operation for some period of time and the parties and key employees have already made a significant level of contributions to the organization, many founders will agree to exclude a portion of the parties' and key employees' shares from the vesting provisions when putting new money into the organization. For example, if a party has been active with the organization for 2 or 3 years and has drawn a salary that is well below that which he or she might have received at another firm in order to fund the business' activities, the founders may agree to limit the vesting provisions to only 50 percent of the party's shares and to allow those shares to vest over the next 2 years, rather than the typical 4 years.

## **15. Option to Purchase Vested Shares**

The repurchase option for Vested Shares is intended to impose a risk of forfeiture of the party's interest in the organization if his or her employment is terminated before the interest is earned by vesting. The repurchased shares may also be needed to attract a qualified person to replace the party. This option generally does not hinge on the nature of the termination of employment, so as to avoid costly disputes over the organization's motive or the facts and circumstances surrounding the termination.

The organization's ability to exercise the repurchase option is also restricted by the provisions of the applicable state corporation laws regulating distributions to shareholders. For example, the law may limit the organization's ability to redeem shares if the organization's net worth, after taking into account the redemption, is less than a specified amount. For that reason, the organization should consider retaining the right to assign its rights to a third party or parties to preserve the ability to obtain the benefits of the repurchase rights. However, since the founders also have this right, this may not be necessary.

This repurchase option may constitute a substantial risk of forfeiture within the meaning of Section 83 of the Internal Revenue Code of 1986, as amended. Counsel for the parties, or if there is no separate counsel, counsel for the organization should consider whether or not appropriate elections should be filed under federal and state tax laws to avoid the possibility that ordinary income will be recognized by the party as the shares vest. See Section 14 (§ 74:330). The election provides that the party elects to be currently taxed on the difference, if any, between:

- The fair market value of the shares; and
- The price paid by the party.

If the election is not made, the party may be taxed at the time the shares vest, or are no longer subject to a risk of forfeiture, in the amount that the then-current fair market value exceeds the original purchase price

paid for the shares.

In this form, the repurchase price to be paid will equal the original purchase price of the shares.

Provisions may be negotiated to allow an interest rate factor or other pricing formulas.

The language in this form makes clear that the right of the organization and the founders is an option and not an obligation and that all or any part of the Unvested Shares may be purchased. While the repurchase rights have only been granted to the organization and the founders in this form, depending upon the circumstances, the parties may also negotiate the ability to obtain such rights on a proportionate secondary basis with the founders.

## **16. Forfeiture of Shares**

This clause is intended to impose a risk of forfeiture of the founder's interest in the business for any wrongdoing. The vesting of a founder's Unvested Shares can be delayed temporarily or permanently so as to discourage founder wrongdoing before the Unvested Shares vest. The provision that the founders can require forfeiture of Vested Shares by a founder who has committed a wrongdoing equally deters founders from engaging in such conduct.

## **17. Governing Law**

All of the issues concerning the relative rights of the organization and its shareholders arising as part of the transaction will typically be governed by the laws and statutes of the state where the organization is established. All other questions and issues concerning the construction, validity, and interpretation of the founders' agreement will generally be governed by the laws of the state in which the organization's principal offices are located, which usually is the state in which the closing of the transaction occurs. In some cases, the parties will make an attempt to have some other law apply to the interpretation of the founders' agreement, usually by conducting the closing in the another state and providing for the delivery of funds to some location in that other state. For example, in a debt financing where there is some concern about the application of the usury laws of the state in which the organization's principal offices are located, the parties may look to shift the nexus of the contract to another state where applicable laws are more favorable.

Governing law provisions affect the types of legal opinions that might be required in the transaction. As noted above, in many cases, organization counsel may be uncomfortable with giving an opinion concerning laws other than those of the jurisdiction in which such counsel is located. If the parties are attempting to have the contractual agreements governed by laws other than those of the state in which the principal offices of the organization are located, a legal opinion regarding the efficacy and validity of the governing law provisions should be obtained; however, it is often quite difficult to obtain an unqualified opinion in this particular area.

## **18. Survival**

The representation and warranties of the parties included in the agreement are intended to survive the closing of the sale and purchase transaction. Accordingly, a party will continue to have a cause of action after the closing in the event that the party discovers that the other party's representations were inaccurate at the time of the closing.

## **19. Successors and Assigns**

The agreement will generally include a provision that makes it clear that its terms are intended to be binding on successors and assigns of the parties, including third parties who purchase the securities that were sold to the founders.

## **20. Entire Agreement**

The founders' agreement should contain a provision that clearly states, if true, that the document is intended to be the full and entire understanding and agreement between the parties. This type of provision reduces the risk that some other term or provision described in a term sheet or another document was intended to bind the parties. One common exception to the foregoing arises when the parties have previously executed a

confidentiality agreement covering any of the information provided to the founders by the organization. If such an agreement exists, the founders' agreement might contain a clause that reaffirms the obligations of the founders under the prior confidentiality agreement.

## **21. Amendments and Waivers**

The founders' agreement should specify the procedures that will be followed with respect to making any amendments to the agreement and waiving the observance of any specific term of the agreement. The key provision in this area is the percentage-in-interest of the founders who must act for an amendment or waiver to be effective. In many cases, a simple majority-in-interest of the founders will be sufficient; however, the exact percentage will vary depending upon the relative interests of the members of the founding group. For example, if there are three co-lead founders, then the percentage usually will be set at a level which assures that all, or at least two out of the three, of such founders agree on an amendment or waiver before it can become effective.

The right to consent to amendments or waivers of a term or provision of the founders' agreement is akin to a voting right, particularly if the founders' agreement contains substantive covenants regarding the election of directors and certain actions that the organization might elect to take (e.g., issuances of shares, acquisitions, mergers). It is important to consider when such voting rights will terminate. For example, in most cases, the rights of founders purchasing convertible preferred stock will survive any conversion of such shares, so long as the shares received upon conversion (i.e., common stock) have not thereafter been sold to the public. This type of provision extends the rights of the founders beyond the period typically provided for in the terms of convertible preferred stock, since the special rights of convertible preferred stock holders terminate at the time such shares are converted into common stock.

The general provisions relating to amendments and waivers frequently will be overridden by any specific language on that subject which might apply to particular subjects in the agreement.

- Termination provisions with respect to certain covenants and agreements of the organization may effectively eliminate various rights of the founders (e.g., rights of first refusal) after the completion of the organization's initial public offering.
- Certain rights of the founders may not be waivable by a vote or consent of the other founders, such as the right to receive any scheduled payments of interest and principal on a debt security.

Finally, amendments or waivers with respect to any registration rights granted to the founders are typically decisions that are left only to those founders who retain registrable securities at the time of the amendment or waiver. Accordingly, a founder who disposes of his or her registrable securities will no longer have a right to vote on any changes in the registration rights provisions.

## **22. Remedies**

Since damages may not be an adequate remedy in the event that a party breaches its covenants regarding voting of shares, the parties have agreed that specific performance should always be available for violations of the agreement, as well as injunctive relief. In some cases, the founders may seek some further protection by requesting that the common shareholders deliver their irrevocable proxies to allow them to vote the common shares in the manner provided in the agreement.

# **Business Plan Essentials**

## **DO'S**

### **Describe each team member**

Having the right team in place is significant to investors. The résumé section should convey the expertise and knowledge of the team members, their networks and connections, and their reputation in the field. This information can be inferred from providing details about education, work experience, residential history, accomplishments, past experience overcoming adversity, commitment to the venture, motivation for starting the venture, ability to make difficult decisions, and how realistic the person is in analyzing the venture's chances of success.

### **Pinpoint the opportunity in the marketplace**

Investors are looking to take a share of a rapidly growing market. The most attractive markets to investors are those that can reach a significant scale in five years. In addition, investors are looking for markets that have an attractive structure. This means that the market actually allows businesses to make money. For example, an industry that is constantly experiencing major shifts in technology and customer needs, or an industry with intense rivalries, will be less attractive.

### **Include evidence related to context**

With pieces of evidence related to the context in which the opportunity exists, investors know that the entrepreneur has a heightened awareness of current events, the marketplace, and how those will affect the venture. It is also important to include how the context may change and how this will affect the venture. After providing the evidence, the entrepreneur should include what the management team can do to affect the context in a positive way if it becomes unfavorable. For example, being knowledgeable about a tax reform can help the entrepreneur plan for when such a bill is enacted.

### **Provide a realistic analysis of risks and rewards**

Although the future is impossible to predict, the business plan should confront the possible risks, especially with respect to the people, opportunity, and context. It is difficult to be honest and realistic about these risks with the goal of seeking capital, but it will help the entrepreneur to ultimately secure the best deal.

### **Talk about the end goal**

Investors are often looking to take a company public in the future. However, this may not be possible if going public would reveal information that would harm the company's competitive position. For example, a competitive position can be harmed when the newly public company reveals profitability and that information angers customers. Investors like to know when they will eventually get money out of the business and particularly like when they are provided with a broad range of exit strategies.

## **DONT'S**

### **Flood the plan with too many numbers**

Experienced investors are aware that there are many unknown variables that could affect revenue and profit projections. Often, entrepreneurs will be overly optimistic and pad their projections. Investors realize that this padding occurs and often discount many of the figures in a business plan. However, answers to questions, such as at what level of sales does the business make profit and cash flow turn positive, are important and deserve space at the end of the business plan.

### **Claim there is no risk involved in the new venture**

Any experienced investor knows that there is no such thing as a no-risk business. Although the ultimate goal will be to obtain capital, it is still important to recognize risks and provide a discussion about what the entrepreneur will do to mitigate these risks.

### **Claim there is no competition**

Many times, inventors and entrepreneurs believe that they are the first people to enter a market space. However, every business has direct and indirect competitors. It is helpful to analyze the competition by imagining which companies would try to enter the same market space if the business becomes successful. Identify the company's competitive advantage and the ways that the company can compete against others.

### **Present a sloppy plan**

It is easy to focus on the content and forget that the presentation of the plan is equally important. The business plan should be written in a formal, confident, and authoritative style. Investors appreciate uniformity in margins, headings, tables, etc. In addition, make sure no pages are missing. The business plan should be complete and thorough, while keeping the technical details to a minimum.

### **Provide a business plan with no plan**

It is appropriate to include an overview of what the business will look like in the short term and in the long term. However, that is not enough. Describe how the business will move from one stage to the next. Include reasonable, definite milestones and an outline of steps that have to be taken to reach these milestones.

### **Try to be everything to everyone**

Although it is good to identify multiple different markets, it is better to provide investors with a more focused strategy. Finding one large market where the product or service solves a problem will be the most successful strategy. However, these smaller, different markets can still be useful to mention and support the strong core strategy.

## **Founders' Memorandum of Understanding for Starting a Business**

Founders, especially in the technology industry, may be more interested in focusing on the research and development of their product, but they should be aware of several business issues that can cause real trouble in the future if not addressed early on. This Memorandum of Understanding (MOU) provides guidance on critical, difficult, and divisive issues that should be discussed at the beginning of a business venture.

1. \_\_\_\_\_ Agree on goals
2. \_\_\_\_\_ Discuss the roles of each founder
3. \_\_\_\_\_ Determine each founder's ownership
4. \_\_\_\_\_ Address the resources each founder will contribute
5. \_\_\_\_\_ Discuss ownership percentage and vesting
6. \_\_\_\_\_ Establish an option to purchase vested ownership
7. \_\_\_\_\_ Determine how decisions will be made
8. \_\_\_\_\_ Identify matters that will require unanimous consent, if any
9. \_\_\_\_\_ Discuss retaining an attorney and other advisors
10. \_\_\_\_\_ Address circumstances under which it is appropriate to remove a founder
11. \_\_\_\_\_ Determine procedures for protecting intellectual property
12. \_\_\_\_\_ Form a legal entity
13. \_\_\_\_\_ Open a bank account and obtain an EIN for the company
14. \_\_\_\_\_ Obtain funding
15. \_\_\_\_\_ Hire additional talent to supplement the management team

## **1. Agree on Goals**

Before making the final decision to actually launch a new business, the founders need to be sure they have thought through all the steps that might be necessary for the venture to be successful. The founders should agree on the goals of the business because all of the early decisions that must be made reflect these goals. Discussing goals as the first step allows founders to carefully consider whether they are launching a new business with the right people.

## **2. Roles of the Founders**

After agreeing on the goals and moving forward to launch the business, the second step founders should take is to carefully discuss the ownership structure of the business and determine the respective management roles of the founders in the business. The founders should decide the duties and responsibilities of each founder and their management role. Founders have a fiduciary duty to each other. It is up to the founders to decide what they expect from each other at the outset of the business. This can include such items as regular meetings, hours dedicated to the company, and duties of loyalty in business activities.

## **3. Founders' Ownership**

Next, founders should decide what percentage of the business each founder will own and what rights each of the founders will have with respect to the management and control of the company. This is important because there needs to be a decision of how to allocate profits and losses. Founders should consider both actual and potential contributions of each founder. Actual present contributions can include, but not be limited to, cash and property (including intellectual property) at the time the new business is launched. Potential contributions can include cash and property, and also business development assistance, introduction to business partners, and opportunity costs to the founders for launching the new business.

### **3a. 50/50 Dilemma**

The 50/50 equity business arrangements have numerous inherent problems. These problems generally arise upon the return of the initial investment. The founders may differ on the view of how the business should grow, especially when the level of contribution of the founders is significantly different. Decisions of growth, such as when to expand by adding assets or purchasing more equipment, are the sources of conflict. Also, if one of the founders introduces an intellectual asset that is profitable, deciding how to value this intellectual property will be an issue. Finally, deciding whether to sell the company can be problematic. By this point, the financial status of each founder has likely changed, the company could be purchased through cash, stock, or both, and many times, the founders do not agree on the deal. There are many potential problems and pitfalls to a 50/50 equity arrangement, and this should be a major consideration when deciding the equity arrangements of the business.

## **4. What Assets or Cash Does Each Founder Contribute or Invest?**

It is difficult to value many of these contributions, especially potential future contributions. Regardless, a founder contributing intangible property should feel as recognized as a founder who provides cash. If the founders cannot reach an agreement, they should seek experienced counsel. Counsel will be able to provide a method to value intangible property and services for the purposes of determining equity ownership in the business. If a mutually agreeable schedule is created to divide profits and losses, the founders can assign percentages to each owner.

When valuing each founder's contribution, it is important to also consider how ownership interests might be diluted by future events while growing the business. If the business accepts investments or hires new management members, the founders may grant ownership interests to investors and members to facilitate agreements. By granting these ownership interests, the founders' ownership interest becomes diluted. An example of this consideration could include setting aside 10 to 20 percent

for a management team, 10 to 20 percent for a pool of incentives for new employees, 40 to 60 percent for sale to venture capitalists.

## **5. Vesting of Ownership**

The primary purpose of vesting provisions and associated repurchase rights is to provide a mechanism for the parties to “earn” their equity by continuing to work for the organization. The investors have an interest in ensuring that the parties continue to serve the organization and help generate the returns anticipated. As a general rule, vesting occurs over a period of 4 to 5 years. In most cases, none of the shares will vest until the employee has been with the organization for a specified period of time. However, it is common that a portion of the shares designated to each founder will vest each year, leading up to the total in 4 or 5 years. For example, if there are 5 founders, each with a potential to earn 20 shares, an agreement can be made that 4 of those shares will vest each year that the founder is with the organization. This will place an incentive for the founders to stay with the company for 5 years or their shares will not vest and remain with the company.

## **6. Option to Purchase Vested Shares**

The repurchase option for vested shares is intended to impose a risk of forfeiture of the founder’s interest in the organization if his or her employment is terminated after the interest is earned by vesting. The repurchased shares may also be needed to attract a qualified person to replace the party. This option generally does not hinge on the nature of the termination of employment, so as to avoid costly disputes over the organization’s motive or the facts and circumstances surrounding the termination.

The repurchase price to be paid will equal the original purchase price of the shares. It is important to note that with startups the shares will not be worth anything originally, so additional provisions should be negotiated to allow for an interest rate factor or other pricing formula. The language of the agreement should make clear that the right of the organization to repurchase vested shares is an option and not an obligation and that all or any part of the vested shares may be purchased. While the repurchase rights have been granted only to the organization, depending upon the circumstances, the founders may also negotiate the ability to obtain such rights on a proportionate secondary basis.

## **7. Decision-Making Procedures**

Regardless of consideration provided for ownership interests in the business, the founders must decide how decisions will be made concerning the operation and control of the business. Several issues are key to constructing a decision-making process for the business. First, the founders should consider what voice each owner will have in the election of the members of the managing body (board of directors). Second, the founders should consider the daily responsibilities of operating the business and assign roles to managers and officers. Next, the founders must determine the level of consensus among the ownership required for large-scale transactions, such as sale of the business, merger of the business, major debt financings, and issuances of securities.

The founders should also agree on the employment agreement between the founders and the business, including salary and benefits awards to owners who are active in the business. Additionally, founders need to decide a procedure for resolving disputes among members of the ownership group. Finally, founders must agree on the restrictions placed on outside activities of the owners in addition to restrictions on their ability to transfer their ownership interest. This decision should also include procedures that should be followed when a founder dies, becomes disabled, reaches retirement age, or voluntarily leaves the company before retirement age.

## **8. Matters Requiring Unanimous Consent**

While authority regarding day-to-day operations may be delegated to one or more managers, there are almost always certain matters which should require the consent of all the owners or some higher percentage of the owners rather than just a mere majority-in-interest. For example, dissolution and/or sale of all the entity’s assets are typically events that must be approved by all the owners, and any other events

should also be specified in the agreement.

## **9. Retaining an Attorney**

Parties should employ an experienced attorney to assist in organizing the company, and a provision should be made in the agreement for the appointment of such an attorney that includes a description of the tasks to be carried out by the attorney (e.g., drafting the company agreement and other documents, as well as applying for any regulatory approvals). Provisions should be made for the expenses associated with organization, including legal fees and other fees payable to the state or local agencies. In general, the parties will agree to advance such expenses, subject to reimbursement by the business after organization. The attorney may agree to wait and invoice the company once it is formed.

## **10. Removal of Founders**

There may come a time when disagreements among founders or other divisive issues may be too difficult to overcome and attempts to resolve end up wasting company resources. Under these circumstances, it is necessary to have a plan in place for removing a founder. The issues to address include the voting procedures and number of votes required to approve a removal, the transfer of equity in the company to the remaining founders or shareholders, and the compensation required for the departing founder.

## **11. Intellectual Property Management**

Founders active in the organization's business will, along with every other key employee of the organization, execute and deliver a standard form of assignment of inventions and confidentiality agreement. The assignment should make it clear that the technology/intellectual property belongs to the organization. Alternatively, the founder bringing the technology/intellectual property can exclusively license it to the organization for the specific field of use related to the organization's business. The assignment is intended to remove any incentive for the party to attempt to exploit the technology other than through the organization. The assignment should be permanent and survive the founder's departure from the organization. The assignment should include the founder's agreement to assist the organization in effecting the transfer, such as by executing documents that might be required to assign patents and patent applications. The founder might be required to prepare appropriate documentation, including a full written description of know-how and trade secret information.

After having previously discussed the founders' intellectual property rights, the founders should discuss procedures to protect the organization's rights in inventions developed by its employees. Further, the founders should develop a program for identifying and protecting trade secret information used in the operation of the business. Finally, the founders should discuss procedures for ensuring the business copyright protection in creative works developed by employees and/or independent contractors.

## **12. Form a Legal Entity**

There are several advantages to forming a legal entity. First, individuals can protect their personal assets from any liabilities incurred or claims against the company. The business will be treated as a separate legal entity from the founders. Second, the business lends itself to a legitimate purpose in that clients will feel more comfortable dealing with someone who is part of a corporation with its own corporate bank account compared to an individual who simply opened a separate checking account. Last, there are tax benefits to forming a legal entity; the founders, on their individual tax returns, can count certain losses and profits. In addition to these benefits, most investors will require that the company be incorporated, allowing for the distribution of stock in the company. Be aware of the associated costs and complexity that come with certain forms of legal entities.

## **13. Open a Bank Account and Obtain an EIN for the Company**

Once the company is a legal entity, the parties should open a bank account in the company's name to hold revenues and from which to draw distributions. It is advisable that a CFO or an advisor with financial experience manages the account. Be cautious of who is allowed to draft checks on the company account. To

reduce the chances of fraud or misappropriation, require a countersignature on all checks drafted on the company account.

In addition to opening an account, be prepared for the tax consequences of owning a business. For the company to properly pay taxes, it needs to have an employer identification number (EIN). An EIN is the Social Security number for a legal entity. There is no cost to obtain an EIN, and the federal government will use it for all tax purposes. If the company pays employees, realizes profits or losses, or liquidates or acquires assets, this number will be needed.

#### **14. Obtain Funding**

To help grow the company, many founders solicit investments. If the company is affiliated with a research institution or university, small business innovation research (SBIR) and small business technology transfer program (STTR) grants are available from the federal government. If the parties are not affiliated with a research institution or university, private investors are a reasonable option. Early-stage investment would be from angel investors, who would require most (if not all) steps on this checklist be complete before signing any funding agreement. Later-stage ventures are likely to attract funding from venture investing firms. In both cases, the investors are generally looking for a profitable return on their investment. Counsel should be consulted for required disclosures to investors.

#### **5. Hire Employees to Supplement the Management Team**

As the company begins to grow, the parties may need to take on additional talent. Because the company has formed a legal entity, obtained an EIN, and opened a company bank account by this point, compensation of additional employees is not an onerous task. Investors can be helpful here. They are often connected to entrepreneurs with extensive skill sets who can help grow and develop the company. In many instances, additional employees of early-stage companies are compensated with equity or stock to reduce cash expenditures in a capital-strapped venture; this allows all liquid finances to go toward developing, improving, and growing the company.

## Resources

Incubate your business at UConn Technology Incubation Program

<https://tip.uconn.edu/>

Browse available UConn technologies using the UConn Innovation Portal

<https://innovation.uconn.edu/>

Guideline document for Faculty, Staff and Students who are affiliated with a Company

<http://bit.ly/2sJyega>

Employee handbook

Policy examples: <https://www.cbia.com/resources/hr-safety/issues-laws/your-employee-handbook-does-it-protect-your-company/>

SBA Business Guide/ Employees: <https://www.sba.gov/business-guide/manage-your-business/hire-manage-employees>

UConn Faculty are required to comply with the University's policy "Use of Students in Outside Employment" See:

<http://policy.uconn.edu/2011/06/02/use-of-students-in-outside-employment/>

Employee agreement for onboarding (link to be added)

Cap table template

Google search shows many templates. Suggesting:

Gust.com tools <https://gust.com/equity>

Simple NDA

Template - <https://core.score.org/resources/non-disclosure-agreement-template>

LLC Operating Agreement

Template: <https://startabusiness.org/ct/llc/operating-agreement/>

LLC Articles of Organization (link to be added)

C Corp Articles of Incorporation (link to be added)

Intellectual Property primer/guides

Read: What Startups Need to Know about Intellectual Property

<https://www.wiggin.com/publications/what-start-ups-need-to-know-about-intellectual-property/>

Insurance primer for startup companies

Essential Insurance for Startups

<http://www.youngupstarts.com/2018/06/02/essential-insurance-for-startups/>

CT and Federal registration guide for businesses

CT Start a Business Guide (startabusiness.org)

<https://startabusiness.org/ct/>

Federal SBA Start a Business Guide

<https://www.sba.gov/business-guide/10-steps-start-your-business/>

The Connecticut Economic Resource Center (CERC) directs businesses to the appropriate agencies to ensure they are properly registered, licensed or permitted within the state.

<https://www.cerc.com/licenses/>

#### Fundraising

- Comprehensive pitch deck template  
(plus which slides you need for 5 min, 10 min, 15 min pitches)

<http://bit.ly/PitchDecktemplate>

Read: What belongs in a Startup Pitch deck

<http://blog.gust.com/startup-pitch-deck/>

- Valuation calculator or metrics  
Read: Valuing Pre-revenue Companies

[https://www.angelcapitalassociation.org/data/Documents/Resources/AngelCapitalEducation/ACEF\\_-\\_Valuing\\_Pre-revenue\\_Companies.pdf](https://www.angelcapitalassociation.org/data/Documents/Resources/AngelCapitalEducation/ACEF_-_Valuing_Pre-revenue_Companies.pdf)

#### Grant resources

- Accounting system procedure – Visit your grant site for requirements.

Consider:

- o An established, compliant accounting system
- o Chart of accounts set up for grants
- o A time and effort reporting system
- o Policies and procedures for financial management

SBIR/STTR Webinars and articles

<https://www.sbir.gov/search-result-page?search=chart%20of%20accounts%20for%20grants>

- Grants opportunities
  - o Sample Phase I Grant Applications (links for NIH, NSF, SBIR)
  - o NIH samples grants - <https://www.niaid.nih.gov/grants-contracts/sample-applications>
  - o NSF Guide, Preparing Proposals - <https://www.nsf.gov/funding/preparing/>
  - o SBIR Grants - <https://www.sbir.gov/>

#### SCORE.org –

[Business Planning & Financial Statements Template Gallery](#)

These tools can be your first step towards small business success. Find business planning, finance, sales, marketing and management templates and guides.

[Financial Projections Template](#)

Download this financial projections Excel template to calculate your startup expenses, payroll costs, sales forecast, cash flow, income statement, and more.

## **Acknowledgements**

I. NY Science and Technology Law Center (NYS-STLC) Startup Guidebook [nysstlc.syr.edu](http://nysstlc.syr.edu)

II. Founders' Memorandum of Understanding for Starting a Business

- Alan S. Gutterman, Business Transactions Solutions, THOMSONREUTERS.
- Rand M. Curtiss, The 50-50 Dilemma, AMERICAN BUSINESS APPRAISERS, [http://www. businessval.com/resources/articles/5050.pdf](http://www.businessval.com/resources/articles/5050.pdf).

III. Startup Checklist

- Anita Campbell, A 30 Point Checklist for Your Startup, SMALL BUSINESS TRENDS, April 18, 2013, <http://smallbiztrends.com/2013/04/startup-checklist.html>.
- Steps to Starting a Small Business, THE COMPAY CORPORATION, [https://www.incorporate.com/ completing\\_startup\\_tasks.html](https://www.incorporate.com/ completing_startup_tasks.html).
- 10 Steps to Starting a Business, THE U.S. SMALL BUSINESS ADMINISTRATION, <http://www.sba. gov/content/follow-these-steps-starting-business>.
- Startup Checklist, Fundable, <https://www.fundable.com/learn/resources/guides/startup-guide/startup-checklist>.

IV. Founders' Agreement Format and Guide

- Alan S. Gutterman, Business Transactions Solutions, THOMSONREUTERS.

V. Business Plan Essentials

- Andrew Clarke, Top 10 Business Plan Mistakes, ENTREPRENEUR.COM, <http://www.entrepreneur. com/article/81188>
- Akira Hirai, Why Business Plans Don't Get Funded, CAYCON.COM, <http://www.caycon.com/why-business-plans-dont-get-funded.php>
- William A. Sahlman, How to Write a Great Business Plan, HARVARD BUSINESS REVIEW, July- Aug 1997.

If you are looking to work with the UConn TIP or TCS  
or have a specific request for assistance please contact us at:

UConn Technology Incubation Program (TIP)

Contact – [\[email\]](#)

<http://tip.uconn.edu>

UConn Technology Commercialization Services (TCS)

Contact - <https://ovpr.uconn.edu/services/tech-transfer/contacts/>

<https://ovpr.uconn.edu/services/tech-transfer/>