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Steps to a successful venture capital financing round

July 8, 2021

An entrepreneur who invests time and energy raising the funds necessary to launch a startup, usually from family and friends (love money), will necessarily want their startup to grow exponentially. Achieving exponential growth requires always more capital, and so the entrepreneur will need to find additional sources of financing. One of these could be venture capital financing. For an entrepreneur, going this route may seem daunting, but if well prepared, it can also be a very wise choice. Here are the steps to take in order to succeed in a round of venture capital financing and get the most leverage out of this type of financing.

What is venture capital?

Venture capital is a non-guaranteed equity investment, made with an investment horizon of typically five to ten years, with a view to realizing an exponential gain and participating in the strategic decisions of the startup in which the capital is invested. Investors who provide venture capital do not undertake to play a passive role—quite the opposite! Entrepreneurs who opt for such financing must be prepared to exchange ideas with investors and justify certain decisions they intend to make as managers. On the flip side, they'll also benefit from their investors' advice and networks.

Application for financial assistance

Once you've grasped how venture capital works and resolved to resort to it, you're ready to launch a round of financing with one or more potential investors. Our advice: don't wait until you really need the funds to take this step. As soon as your startup takes off, get into networking mode! Meet with dozens of investors and present your vision, team and business plan. Investors will be more interested in your vision, talent and the growth potential of your business than in its current results, and they will probably be as much interested in these aspects as they are in your business plan. And if things don't immediately go your way, don't give up! Often all it takes is for one investor to bet on you for others to follow.

Letter of intent

If the ?nancing round is well received, investors will con?rm their interest by submitting a letter of intent. A letter of intent states an investor's intention to invest under certain conditions, but it doesn't constitute a binding undertaking. It will set out the terms and conditions of the proposed investment (form of investment, subscription price, etc.) which, while not binding on the investor, are nonetheless binding on the company once it has accepted them. Once an entrepreneur has accepted a letter of intent, it may be very dif?cult to get the investor to waive the rights granted in their favor by the letter.

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Due diligence

Once the letter of intent is agreed to, the investor will conduct a due diligence review on the company. A due diligence investigation allows an investor to better assess the legal, ?nancial and other risks associated with a startup and validate certain statements or assumptions stated in the company's business plan. In a due diligence review, the following will usually be scrutinized, among others :

Accounting and corporate records
Material contracts
Intellectual property (patents, trademarks, etc.)
Disputes involving the company
Environmental aspects

Negotiation of final agreements

Generally speaking, in venture capital ?nancing, two main acts key documents will con?rm the terms of the agreement between the company and the investor: a subscription agreement and a shareholders' agreement. A subscription agreement is a document similar to a share purchase agreement, except that it isn't concluded with a shareholder but with the company itself. It speci?es the form of the subscription (common shares, preferred shares, subscription rights, etc.) and contains numerous representations and warranties on the part of the company for the bene?t of the investor, as well as an undertaking to indemnify the investor should one of the representations or warranties prove to be false and cause a loss for the investor to suffer prejudice. A shareholders' agreement is a document signed by all the shareholders of a company and the company itself. Typically, such an agreement determines who will sit on the board of directors and how it will operate. It contains a number of clauses that govern the issuance and transfer of the company's shares and grants the investor a right of oversigh —and often even veto power—over certain decisions.

Closing

Once the ?nal agreements are negotiated, closing can take place. At the closing, the parties will sign all relevant documents agreements and certi?cates, including the subscription agreement and shareholders' agreement, and deliver the documents required to meet all conditions. The parties will also sign the subscription agreement and shareholders' agreement. The company's lawyers will provide a legal notice opinion to con?rm to the investors that the securities subscribed to are validly issued, that the company has the legal capacity to enter into all the agreements prepared by the investor's legal counsel, that the agreements have been duly approved, and that the signatory has the authority to sign the agreements and bind the company.

A forewarned entrepreneur is forearmed!

You now understand that for an entrepreneur, the secret of a successful ?nancing round lies in being properly prepared, being realistic about investors' expectations and requirements, and having a large dose of con?dence in the business. If you've started to solicit ?nancing from potential investors or are planning to do so soon, there's still time to get legal advice to avoid unpleasant surprises at a critical moment.

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