

21. In Establishing the Company, It Is Important to Pursue Sound Legal Advice from Proven Firms

There are countless things to consider when entrepreneurs make the decision to establish their corporation in the earliest days. While the fee structures of the elite law firms that specialize in shaping startups are difficult to swallow, their experience in putting definition around sensitive areas of the business is essential. Many of the startups I have worked with have engaged high-end specialty firms like Fenwick and West that are well-versed in the startup game. The knowledge and experience they bring to the conversation when it comes to putting the foundational pillars in place make partnering with them in those key areas a solid strategy.

So, what are those facets of the business that demand legal counsel from an elite firm? There are several that fall into the categories of Executive Compensation and Conduct; determining the size of the equity share pool and how it will be distributed and vested; putting sensible revenue recognition and tax/accounting plans in place; and establishing a Director and Officer Liability Insurance plan. When it comes to locking down a sound fundamental strategy in these important areas of the business, the most reputable firms are worth their weight in gold.

From the earliest days, it is important to create an alignment of interest between all of the company's stakeholders. All things being equal, investors are attracted to simple capitalization tables and will look to avoid exotic terms such as super voting rights or other preferences for founders that can be overly onerous. Beneath it all, it is critical to distinguish between the following functions:

- Ownership—who legally owns the company's equity?
- Possession—who actually runs the company on a day-to-day basis?
- Control—who formally governs the company's affairs?

Most conflicts arise when functions overlap, making the establishment and maintenance of these key pillars an early priority for every startup.

For most other legal matters, it is worth considering a more practical approach, which can help guard against becoming overly reliant on high-priced legal services. Leaning on junior attorneys at premium firms to handle the less strategic work makes good sense but finding a trustworthy attorney that works on their own or with a smaller firm can provide even greater savings. From my experience, startups that leverage their network to identify such a resource have not only contained their exposure to runaway legal fees, many have forged early relationships with their eventual chief legal counsel. While I am certainly not suggesting a legal strategy that would ever put a business in harm's way, this dual-track approach has proven to be an effective way to sidestep the cost multiplier that comes with the deployment of talented attorneys at large, established firms. In that spirit, the ability to add another engineer in the early going with the savings on legal services makes this Playbook strategy a no-brainer!