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Steering The Unicorn: Tips For Working With Startups

By **Elise Hansen**

Law360 (November 12, 2019, 12:16 PM EST) -- Emerging companies and late-stage startups can present attorneys with a different set of challenges than those offered by more traditional, established clients. Here, Law360 explores insights and advice from veteran practitioners guiding an industry whose mantra is "move fast and break things."

Get Ready to Move Fast

Speed is a key aspect of the startup business model, which relies on being the first to make inroads with a new product or service. The scramble for first-mover advantage means attorneys have to prioritize.

"There's an overwhelming energy in startups for 'get it done fast,'" Ivan Gaviria, partner at Gunderson Dettmer Stough Villeneuve Franklin & Hachigian LLP, told Law360. "Most lawyers are trained both in law school and in a lot of big, traditional law firms to hunt down every detail, to crush every problem, to make sure no stone is left unturned."

For a cash-strapped startup, some stones may not be worth a lengthy investigation. "You can't be running around spending $5,000 to solve $5 problems," Gaviria said. "The startup world doesn't really permit that."

Particularly when it comes to evaluating risk, startup attorneys can't spend too much time obsessing over low-likelihood events and "pinning them down to perfection," Gaviria said.

The ramped-up pace also applies to attorney responsiveness, Gaviria said. And because this is the startup world, clients may use some unconventional communication methods, such as LinkedIn, Twitter or video conferencing. Get used to it, said Gaviria.

"From a lawyer's perspective, you cannot be old school," he said. "You have to be much more nimble about responsiveness and you have to be prepared sometimes to get out of your comfort zone."

Know When to Pump the Brakes

At the same time, attorneys can help make sure their clients aren't racing into bad deals. "There's such a strong pull to agree to things to get that first customer, to get that first round of investment or get that check in the door," Gaviria said. "It can be challenging sometimes to pause and make sure you really understand what the potential long-term consequences are."

Startups may hastily agree to guaranteed pricing or exclusivity terms that could hinder growth in the long run. That's where attorneys can come in and explain what the fine print really means for the business in practice.

When investors come in with their term sheets, "talk through what [the terms] are, which are out of market, which they might try to push back on," said Mark Leahy, co-chair of Fenwick & West LLP's startup and venture capital practice. "And there may be some things that [the client] has in mind, that they care about in particular off the bat."

The playing field is not level in these negotiations, and reading the fine print while prioritizing the core issues can help startups navigate deal-making even with limited leverage.

Be Selective When 'Breaking Things'

Because startups are moving fast and prioritizing, not everything about the business is embalmed in amber. Certain kinks can be reworked, amended or dealt with as they arise. But there are some things you don't want to have to break. The two main categories that Josh Seidenfeld of Cooley LLP singles out are issues of equity ownership and intellectual property.

"If there's an accounting issue, you can solve that; if there's a contractual issue, you can amend for that," Seidenfeld said. "It's very, very difficult to go back and fix a defective equity grant, and it can be expensive to do so. And if you don't own your intellectual property, going in and trying to negotiate that when you're on the eve of a deal to sell the company can be very costly or impossible to get done," he said.

Baker Botts LLP partner Brian Lee said another area where startups can get ahead is by setting up a vesting scheme early.

"Often, founders will issue stock upfront without vesting or repurchase terms," Lee said. "When an investor comes in, that's going to be part of the negotiations."

Startups that grapple with vesting at the outset have a framework in place to show potential investors. Investors may still push for changes, but having an existing process in place can give startups a little extra leverage in negotiations, Lee said.

"It's always easier to set things up properly than to fix them later," Lee said.

Be Ready to Be a Mentor

Many startups are formed by someone with a would-be revolutionary idea or technology, not by a business guru. Especially in the early days, some founders will be stretched thin and unfamiliar with the terrain, and they lean more heavily on attorneys for a range of questions.

"The types of questions that you get span a much broader category of things that are beyond the normal blocking and tackling of being a lawyer, and kind of touch on the bigger ecosystem for their particular business," Seidenfeld said.

Outside lawyers for emerging companies often find themselves acting as de facto general counsel and trusted adviser who contribute to business decisions. Leahy said his clients frequently solicit his opinion on the best route for the company.

"Our client base is really looking for a recommendation from us," Leahy said.

Often his clients want to hear "not just what can they do, but what should they do," he said. "They won't necessarily always follow it, but they want me to make a call."

Lee agreed. "For younger companies or first-time entrepreneurs, what they're really looking for is not just someone who can come in and drop the documents," he said. "They're looking for a partner and someone who can provide not just the legal advice but the business advice."

Don't Forget Who the Client Is

Many lawyers who work with startups are hired by the founders and work with them for years. But the company's founders are not the client — the company itself is, Craig Sherman of Wilson Sonsini Goodrich & Rosati PC noted.

"It's a hard line to draw, because as outside counsel you're working directly with management, but it's not the individual members of management that are your client; it's the company itself," he said.

And sometimes, startups need to shed their founders.

"If it's the position of the board on behalf of the company to remove a founder-CEO that you've worked with for 10, 15 years in some cases, you need to represent the interest of the company and negotiate and facilitate the exit of that founder who you've worked with for years," Sherman said.

Interpersonally, those situations can be a challenge. The best way to get through it is to stay professional, Sherman said.

"There's a challenge in managing the personal relationship while making sure that you're taking care of your ethical responsibilities as counsel to the company. Those ethical responsibilities to the company have to come first," Sherman said.

Gaviria noted the same thing. In these situations, "you have to put on your professional hat and do the right thing," he said.

--Editing by Orlando Lorenzo.