15.617, Spring 2004
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Lecture 16: 4/12/04

Guest: Edward Freedman, Corporate Counsel, Flagship Ventures

- Venture Capital (VC) is a subset of private equity (a class of investments)
- He refers to venture capital as early state venture capital
- Friends, Family, Fool

- VC firms invest in C corps
- How you decide to incorporate depends on your liquidity.
- VCs prefer preferred stock to invest in.
- C: taxed at entry level and when you take it out.
- You typically pay with stock, usually options.
- Investors put in about $10 M over a period of time
- 83b
    - Under tax code when you are taxed every time the repurchase price lapses. Every quarter you have to tax liability.
    - You give 25-30% of stock immediately

- Structuring the Venture Financing
    - Charter: sets out rights and preferences
    - Stock Purchase Agreement: contract between VC and company, so VC can buy the stock, Representation and warranties. Check on IP.
    - Stock holders agreement: voting agreement. Right of first refusal and co-sale. (And if any stockholder wants to sell shares, she has to see if VC wants to buy it, if not, VC can co-sell.

- Investor Right Agreement
    - Registration rights (you have to go public)
    - S3 form: needed to register SEC
    - "piggy back" form
    - Information Rights: you have the rights to get information

- Biggest issue is valuation
- Cumulative dividends: accumulation over time and at a rate of 8% or 10%. Built-in return.
- Anti-dilution: downside protection.
- Usually more than 1 investor comes to a deal, which is good for the company and the investor.
- Once anti-dilution goes down, it never goes back up.

- Relationship with lawyer’s in house perspective: at the beginning of the deal you have to set parameters and budget. Early deal: maybe $20000-$25000
- Set time constraints
- Good communication (look at handouts)