

Course Syllabus

Entrepreneurship, Venture Capital, and the Law
Professor Lipshaw
Three credit hours*
Spring 2018

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Important Preliminaries

First, I am going to ask you in the first class to affirm that you have read this entire syllabus. You will need to read it, regardless of the affirmation, because there are two “problems” at the end of the text portion we will be discussing in the first class.

Second, I will use Blackboard (accessible through Campus Cruiser) and the e-mail function within Blackboard as my primary means of communicating with you outside of class. Please check it regularly.

Third, I have become aware that I am using the same book as Karl Hartmann uses in his Business Planning class. If you have taken that class, you shouldn’t be taking this one.

Overview

The class will not be easy, and it is a lot of work for three credits, but it ought to be stimulating. When you represent a startup business, whether it is Mom and Pop starting a corner wine shop, or a Ph.D. engineer building a platform technology that has the possibility of being a publicly held industry generating multi-billion dollars in revenue, technical mastery of the relevant law is just one tool in your toolbox. It’s very likely that your client will be relying on you for all sorts of advice that goes beyond what you learned in your doctrinal law classes, and it will call upon your business sense, your common sense, your ability to do a fair amount of arithmetic (lots and lots of adding, subtracting, multiplying, and dividing), and your willingness to admit what you don’t know and to learn along with your client. We will touch on most of these issues along the way.

I have limited the number of students in this class because I want it to be an intense interaction among all of you and me. It’s not a clinic but we will approach some things clinically. It’s not a lecture course, but I will lecture to you from time to time. There will be math because there is math when you do this kind of law.

* I am required by the school administration to advise you that a “credit hour” is an amount of work that reasonably approximates not less than one hour of classroom or direct faculty instruction and two hours of out-of-class student work per week for fifteen weeks, or the equivalent amount of work over a different amount of time.

But because this is a shared experience in a way that my big doctrinal courses have not been, the rules here are going to be less libertarian than you may be used to from me. If you cannot commit now to full participation in this class, drop it before we get started.

Book and Materials

The book for the course is Maynard & Warren, *Business Planning: Financing the Start-Up Business and Venture Capital Financing*, 2d ed.

The book is designed to be self-contained, but I'm going to deviate from it. I also post (and may continue to post) additional materials on Blackboard under Course Materials for the particular unit.

I have also listed supplemental reading. There is a ton of literature on entrepreneurship and many times I've selected a small bite of it, some very theoretical and some less so. Don't be intimidated. You don't have to read it, but I recommend the material and will sometimes refer to it in our class discussions.

For a narrative rather than "analytical" sense of the entrepreneurship experience, I recommend two books:

1. Seth Goldman & Barry Nalebuff, *Mission in a Bottle* (Crown Business, 2013). Barry Nalebuff, a professor at the Yale School of Management and one of his former students, Seth Goldman, founded Honest Tea (and later sold the company to Coca-Cola). This book is their story, written and drawn in graphic novel style.

2. Diana Kander, *All in Startup* (Wiley, 2014). Kander is an entrepreneur and investor, as well as a fellow at the Kauffman Foundation, which supports entrepreneurship. Kander amalgamated her experiences into a "novel" (complete with romantic relationships, etc.) that emphasize her particular point about startups: the important thing is *not* to have a product, but to have customers.

Class Participation

For those of you who took my large doctrinal courses, you will see that I am not quite as laissez-faire here about attendance and participation as I was there, because the course has a different purpose, and the grading is going to be somewhat different.

You will get a realistic sense of what it is like to be a junior corporate associate at a law firm, both what is expected of young associates and the type of work assignments that they are likely to be asked to do when they start practicing law as a transactional lawyer.

You should think of each session of this class as a business meeting and me as your senior partner. Every class is important, not just for grading purposes, but for the substance of what we cover.

There will be a sign-in sheet. If you aren't going to be here, you need to let me know in the

same way you would let a partner or a client or the other party know if you couldn't get to a meeting.

The Law School's student attendance policy is set forth in Section II.B of the Rules and Regulations, which can be found at the following URL:

<http://www.suffolk.edu/law/student-life/rulesandregs.php#rule2B>.

Recording

I ask the IT department to record and make ALL classes available via an MP3 posted under "Course Media" on Blackboard. I want to remove some of the note-taking (particularly the "transcription" kind) pressure.

If you take notes, concentrate on engaging with what's important - you can always go back and pick up details later.

NOTICE: YOU MAY ONLY LISTEN TO THE RECORDINGS VIA THE LINK PROVIDED ON CAMPUS CRUISER, AND MAY NOT DOWNLOAD OR RECORD THEM. THE RECORDINGS ARE MY PROPERTY, AND YOU ARE PERMITTED TO USE THEM FOR THIS CLASS ONLY. ANY REBROADCAST, REPUBLICATION, OR RETRANSMISSION WITHOUT THE EXPRESS WRITTEN CONSENT OF ME IS STRICTLY PROHIBITED.

Assignments and Grading

There *will* be grades, but this class is not bound by the curve. When I grade exams in classes to which the curve does not apply, the only thing that keeps me from giving out all As is my sense of intellectual and pedagogical integrity – in other words, there are students who go above and beyond in demonstrating mastery, and if I don't distinguish them from the students who simply didn't get it or have mailed it in, I feel like I have cheated the former group. My assumption is that you enrolled in this class because you intend to go above and beyond, and that I won't face that issue here.

There will be no final exam, and your obligations to me will be complete as of the last day of class.

Grades will be determined as follows:

The maximum number of points available in the class is 200.

Class participation: 25% (50 points). You will be able to earn up to 50 points by way of your attendance and meaningful participation. This is primarily quantitative – I put a little check mark next to your name if you say something substantive.

Homework assignments: 30% (60 points). There are five homework assignments, all of which must be handed in on time. The first one will not be graded – you get 12 points for handing it in. Each of the remaining four assignments is worth 12 points. There will be three grades: Superior (12 points); Acceptable (9 points); "Mailed in" (6 points) Unacceptable (0

points). You will receive group feedback on these assignments in addition to the assigned grade.

Graded Substantive Writing Assignment: 30% (60 points). You will be provided with a venture capital term sheet and forms of an Amended and Restated Certificate of Incorporation and a Preferred Stock Purchase Agreement drafted by opposing counsel. Acting as counsel to SoftCo, you will review the draft documents for conformity to the term sheet, as well as for general drafting issues, and provide detailed marking noting the changes needed to each document. You will write a memo that I can read alongside your markup so that I understand from you why you did what you did. (You will need to have access to the “Review” function in Microsoft Word. You will show redlined changes.) I will provide you with extensive individual comments on your markups and memos.

Capstone Term Sheet Negotiation: 15% (30 points). During the last weeks of the course, you will assemble in teams and negotiate a term sheet in a simulated deal. The exercise is competitive among the teams, although not in a way you might expect. Teams will be able to earn game points under a system that will be made clear. Top teams will earn prizes, and the members of the first-place team will earn a 1/3 bump in the final grade, above the total point calculation. Each of you must also hand in a confidential self-assessment of your role and performance in the negotiation (not to exceed 1,000 words).

Out of Class Availability

I am almost always available by phone or e-mail or in my office. When I’m here my door is almost always open, and I invite you to come see me. Don’t be shy if you need to talk about this class or anything else.

Mental health, stress and substance abuse

As a student, you may experience a range of issues that can cause barriers to learning, such as strained relationships, increased anxiety, health issues, alcohol/drug problems, feeling down, difficulty concentrating, lack of motivation, or feeling ill. These concerns or other stressful events may lead to diminished academic performance or may reduce your ability to participate in daily activities. Suffolk University services are available to assist you in addressing these and other concerns you may be experiencing. You can learn more about the broad range of medical services and confidential mental health services available on campus at the following websites:

[Counseling Center](http://www.suffolk.edu/offices/989.html) -- <http://www.suffolk.edu/offices/989.html>,

[Office of Health and Wellness Services](http://www.suffolk.edu/offices/932.html) --<http://www.suffolk.edu/offices/932.html>

Law Students may also wish to access the services of Lawyers Concerned for Lawyers –

www.lclma.org

In addition, the Law School Dean of Students Office is available to discuss resources and possible approaches to address the academic/enrollment impact of the above issues. (The Law Dean of Students Office is on the 4th floor, within the Dean’s Suite –

LawDeanOfStudents@suffolk.edu

First class problems:

1. “One morning, exactly at sunrise, a Buddhist monk began to climb a tall mountain. A narrow path, no more than a foot or two wide, spiraled around the mountain to a glittering temple at the summit. The monk ascended at varying rates of speed, stopping many times along the way to rest and eat dried fruit he carried with him. He reached the temple shortly before sunset. After several days of fasting and meditation he began his journey back along the same path, starting at sunrise and walking at variable speeds with many pauses along the way. His average speed descending was, of course, greater than his average climbing speed. Prove that there is *a spot* along the path that the monk will occupy on both trips at precisely the same time of day.” (from James L. Adams, *Conceptual Blockbusting*, 2d ed. (Stanford Alumni Association, 1974)).

2. In which of the following two situations would you feel most comfortable? In each you have been asked to make a cake for a friend’s birthday.

a. You find a great recipe online, go to the store, buy the ingredients, and follow the directions in the recipe.

b. You look in the cupboard to see what ingredients you have available, research online the kind of cake that is possible using only those ingredients, and then follow the recipe from that point on.

Reading and Class Sessions:

With the caveat that it is subject to change, here are the readings and assignments by class session.

Class/Date	Topic	Reading	Unit Outline	Homework/Assignments
Jan. 17	1.0 Business startups, the entrepreneurial mindset	<p>Required: M&W: pp. 1-24</p> <p>1.01 Exercise: Read and consider the problems from the syllabus</p> <p>1.02 Wasserman, <i>The Founder's Dilemma</i>, HARV. BUS. REV. (Feb. 2008)</p> <p>1.03 Sarasvathy, Causation and Effectuation: <i>Toward a Theoretical Shift from Economic Inevitability to Entrepreneurial Contingency</i>, 26 ACAD. MGMT. REV. 243 (2001).</p> <p>1.04 Reed, <i>Doing documents vs. doing deals: a lawyer confronts a venture capitalist</i>, BUSINESS LAW TODAY 13 (Sept./Oct., 2001)</p> <p>Supplemental:</p> <p>1.05 Lipshaw, <i>Why the Law of Entrepreneurship Barely Matters</i>, 31 W. New Eng. L. Rev. 701 (2009).</p> <p>1.06 Jennifer Conlin, <i>At Zingerman's, Pastrami and Partnership to Go</i>, New York Times, July 5, 2014.</p> <p>1.07 Puri and Robinson, <i>Who Are Entrepreneurs and Why Do They Behave That Way</i> (pre-publication version, 2006).</p> <p>1.08 Jonsson, <i>What's in a Name? On Language, Concept Formation, and the Definition Disputes in the Entrepreneurship Literature</i>, 7 J. Cultural Sci. 1 (2014).</p>	<p>I. Introductions</p> <p>A. The professor</p> <p>B. The course</p> <p>C. The students</p> <p>II. Background on Entrepreneurship and New Business Financing</p> <p>A. What is an entrepreneur?</p> <p>1. In concept</p> <p>2. The casebook business hypothetical (SoftCo)</p> <p>B. Investors and typical startup scenarios</p> <p>III. Thinking like a lawyer or an entrepreneur</p> <p>A. Entrepreneurial mindset – causation versus effectuation</p> <p>B. Lawyerly mindset – models and contracts</p> <p>C. Blockbusting and creativity</p>	
Jan. 22	2.0 Intro to deal structuring – term sheets	<p>Required: M&W: pp. 617-37; 726-30 (Sample Term Sheets)</p>	<p>I. Introduction to Term Sheets</p> <p>II. Term Sheet Complications and Disputes</p> <p>III. Homework Assignment</p>	<p>Homework Assignment #1:</p> <p>House Sharing Term Sheet (due and to be discussed on Jan. 29 – must be written; bring two copies to class).</p>

Jan. 24	3.0 Short- and long-term entity selection considerations for startup companies	Required: M&W: pp. 75-90; 101-131	I. Basic Choice of Entity Issues A. SoftCo's situation B. Factors to consider 1. Administrative complexity 2. Personal liability 3. Management and control 4. Term of existence 5. Tax 6. Raising capital 7. Fiduciary responsibility 8. Transfer of ownership interest C. Comparison of basic forms of organization II. Organizing for Investment (Consequences for investors - IRC Section 83 and other consequences for founders covered in Unit 8.0)	
Jan. 29	2.1 Intro to deal structuring – term sheets		I. Negotiate house sharing term sheets II. Discussion of exercise	Homework Assignment #1 Due.
Jan. 31	3.1 Short- and long-term entity selection considerations for startup companies		I. Completion of Unit 3.0	Homework Assignment #2: Analyzing an LLC Operating Agreement (#2 in M&W: pp. 697-98) (Hypos 1, 4, and 5 only; no more than two pages; due and to be discussed on Feb. 7 – must be written; bring two copies to class).
Feb. 5	4.0 Angel funding and venture capital fund structures	Required: M&W: pp. 429-456; 465-468 4.01 Zider, <i>How Venture Capital Works</i> , HARV. BUS. REV. 131-139 (Nov.- Dec. 1998). 4.02 Mulcahy, <i>6 Myths About Venture Capitalists</i> , HARV. BUS. REV. (May 2013). 4.03 <i>Getting Started with Angel Investing</i> , ENTREPRENEUR.COM Supplemental: 4.04 <i>What Angel Investors Want Now</i> , ENTREPRENEUR.COM (Apr. 2013) 4.05 <i>5 Worst Mistakes Entrepreneurs Make When Pitching Angel Investors</i> , ENTERPRENEUR.COM (Aug. 2011) 4.06 Herzlinger, <i>An Angel Investor with An Agenda</i> , HARV. BUS. REV. (Mar. 2011)	I. Overview of Capital Formation II. Angel Funding A. Who are they? B. What do they want? C. Investment structures III. Venture Capital Funds A. Industry overview B. Fund structures	

Feb. 7	5.0 Valuation and Evaluation	<p>Required:</p> <p>M&W: pp. 456-465</p> <p>5.01 Sahlman, <i>How To Write a Great Business Plan</i>, Harv. Bus. Rev. (July-August 1997).</p> <p>5.02 Lerner, <i>A Note on Valuation in Private Equity Settings</i> in LERNER, VENTURE CAPITAL AND PRIVATE EQUITY (2000) at 161-201.</p> <p>5.03 Koh and Winkler, <i>Venture Capitalist Sounds Alarm on Startup Investing</i>, WALL ST. J., Sept. 15, 2014</p>	<p>Unit 5.0</p> <p>I. Evaluation</p> <p>A. What VCs Do</p> <p>B. The Nature of the Game</p> <ol style="list-style-type: none"> 1. Uncertainty 2. Asymmetric Information 3. Nature of Assets <p>C. Controlling Risk</p> <ol style="list-style-type: none"> 1. Financing Techniques 2. Monitoring <p>II. Valuation</p> <p>A. Time Value of Money</p> <ol style="list-style-type: none"> 1. Basic Concept 2. Discount Rates <ol style="list-style-type: none"> a. Mature Firms b. Startups <p>B. Internal Rates of Return</p> <p>C. Methodologies</p> <ol style="list-style-type: none"> 1. Comparables 2. NPV (or DCF) 3. Venture Capital Method <ol style="list-style-type: none"> a. Pre-Money, Post-Money, and Fully-Diluted Values b. Calculation <p>III. Sahlman's Deal Rules</p>	<p>Homework Assignment #2 Due. To be reviewed at the beginning of class.</p>
Feb. 12	5.0 Valuation and Evaluation (continued)			<p>Homework Assignment #3: Venture Capital Valuation Hypothetical (due and to be discussed on TBD – must be written; bring two copies to class).</p>

Feb. 14	5.1 Valuation Exercise 6.0 Staged Investment Structures, Term Sheets, and Related Documentation	Required: M&W: pp. 479-510; 577-611; 617-690 Supplemental: 6.01 Boyce, <i>Understanding Convertible Preferred Stock</i> , NYLJ (Feb. 14, 2000) Vol. 224, No. 52. 6.02 Hoffman and Chisholm, <i>Trends in Venture Capital Financing Terms</i> , METROPOLITAN CORPORATE COUNSEL, April, 2002, at 14	I. Overview of Venture Capital Financing – Convertible Preferred Stock Investment II. Transaction Documents A. Convertible Preferred Stock Documentation and Rights 1. The amended and restated certification of incorporation 2. The nature of preferred stock 3. Substantive terms a. Dividend preferences b. Liquidation preference c. Conversion rights (anti-dilution in Unit 7) d. Redemption rights e. Voting rights B. Preferred Stock Purchase Agreement C. Investor Rights Agreement D. Right of First Refusal and Co-Sale Agreement E. Voting Agreement III. Transaction Process A. Documentation B. Due Diligence C. Closing	
Feb. 21	6.0 Staged Investment Structures, Term Sheets and Related Documentation	Required: M&W: pp. 479-510; 577-611; 617-690	Continued (see above)	
Feb. 26	6.0 Staged Investment Structures, Term Sheets and Related Documentation	Required: M&W: pp. 479-510; 577-611; 617-690	Continued (see above)	
Feb. 28	6.0 Staged Investment Structures, Term Sheets and Related Documentation	Required: M&W: pp. 479-510; 577-611; 617-690	Continued (see above)	

Mar. 5	6.0 Staged Investment Structures, Term Sheets and Related Documentation	Required: M&W: pp. 479-510; 577-611; 617-690	Continued (see above)	Graded Writing Assignment handed out. Due April 2.
Mar. 7	7.1 Conversion, Dilution, and Down Round Issues	Required: M&W: pp. 528-576 Supplemental: <i>7.02 Aidun, How VCs Can Limit Their Liabilities in a Down Round</i> , VENTURE CAPITAL JOURNAL (October 2002) at 40. <i>7.03 Bartlett, Understanding Price-Based Antidilution Protection: Five Principles to Apply When Negotiating a Down-Round Financing</i> , 59 BUS. LAWYER 23 (2003).	7.0 – Conversion, Dilution, and “Down Round” Issues I. What is Dilution? II. Good Dilution in the VC Context III. Bad Dilution A. Why It Happens B. Adjustments for Technical Dilution to the Participation Right C. Real Dilution to the Economic Value of the Shares 1. How It Happens (Arithmetically) 2. Anti-Dilution Protection a. What it is b. Full Ratchet c. Weighted Average Ratchet (i) Broad-based (ii) Narrow-based d. Predominant Forms e. Trigger Provisions	Homework Assignment #4 (#7 in M&W (Hypo 1 only, and solve only for the sales after 1 year and 3 years): p. 704) (due and to be discussed on March 19 – must be written; bring two copies to class).
Mar. 19	7.1 Conversion, Dilution, and Down Round Issues		See above	Review Homework #4
Mar. 21	7.1 Conversion, Dilution, and Down Round Issues		See above	Homework Assignment #5 (#8 in M&W (Hypo 1 only): p. 705) (due and to be discussed on March 28 – must be written; bring two copies to class).

Mar. 26	8.0 Employee compensation	<p>Required: M&W: pp. 327-376 IRC §83 on Blackboard</p> <p>Supplemental:</p> <p>8.01 NCEO Employee Stock Ownership Materials</p> <p>8.02 Institutional Shareholder Services, <i>Binomial Stock Pricing: The Most Prudent Model for Valuing Options</i>.</p> <p>8.03 Sutton & Donohue, <i>Repricing Underwater Stock Options</i>, VENTURE CAPITAL JOURNAL, Vol. 41, Issue 11 (Nov. 2001)</p>	<p>I. Founders' Stock</p> <p>A. IRC §83 issues</p> <ol style="list-style-type: none"> 1. Stock for services 2. Cheap stock 3. Timing issues 4. Valuation/consideration <p>B. Stock Purchase Terms</p> <ol style="list-style-type: none"> 1. Repurchase rights 2. Transfer restrictions <p>C. Employment agreement</p> <p>II. Equity-Based Compensation</p> <p>A. Philosophy</p> <ol style="list-style-type: none"> 1. Arguments for 2. Arguments against 3. Practical issues 4. Strategic decisions <p>B. Forms</p> <ol style="list-style-type: none"> 1. Restricted stock 2. Stock options <ol style="list-style-type: none"> a. Definitions b. NQSOs <ol style="list-style-type: none"> i. Plan parameters ii. Exercise price iii. Tax treatment iv. Accounting <ol style="list-style-type: none"> (A) FAS 123(R) (B) Valuation <ol style="list-style-type: none"> (I) Black-Scholes (II) Binomial 	
Mar. 28	8.0 Employee compensation 10.0 Intro to Capstone Project	Required: M&W: pp. 327-376		Review Homework #5
Apr. 2	10.1 Capstone project – VCs' lawyers only 9.0 The Role of the Lawyer (Founders' lawyers only) Startup.com (Founders' lawyers only)	Required: M&W, pp.24-29; 38-64		Graded Writing Assignment Due. VCs' lawyers term sheet drafting assignment
Apr. 4	10.1 Capstone project – VCs' lawyers only 9.0 Startup.com (Founders' lawyers only)			VCs' lawyers term sheet due by 5:00 pm on Friday, April 6 Founders' lawyers markup assignment

Apr. 9	10.2 Capstone project – Founders’ lawyers only 9.1 The Role of the Lawyer (VCs’ lawyers only) Startup.com (VCs’ lawyers only)”	Required: M&W, pp.24-29; 38- 64		
Apr. 11	10.2 Capstone project – Founders’ lawyers only 9.1 Startup.com (VCs’ lawyers only)”			Founders’ lawyers markup due by 5:00 p.m. on Friday, April 13
Apr. 17	10.4 Capstone project – negotiation			
Apr. 18	10.4 Capstone project – negotiation			
Apr. 23	10.4 Capstone project – negotiation			Final term sheets and confidential team self- assessments to Prof. Lipshaw due by 5 p.m. on April 25
Apr. 25	10.5 Capstone project – Post mortem and scoring			