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Too much lawyering hurts technology companies

By Jeffrey R. Glassman

The passing of technology mogul and Apple founder Steve Jobs made headlines globally this week, which shows the profound impact his iPod, iPhone and iPad have had on our culture and economy. Though the technology community continues to mourn the loss of this titan of innovation, a technology renaissance is currently afoot almost a decade after the downturn of a once thriving “.com” boom. And compared with the rest of America, Silicon Valley and other technology corridors around the country are starting to experience a rebirth of sorts.

While I celebrate this renewed interest in financing and launching new technology companies, I think it is important, in light of our recent experience, to take a moment and ask ourselves this question: “Why do so many technology startups fail?” Some say it’s the result of a flawed business model. Others suggest weakness in the underlying technologies themselves. But I offer up another theory for your consideration: too much “lawyering.”

Facebook Inc. and Twitter are all the rage, valued in the billions of dollars. LinkedIn, Zillow and Pandora Media Inc. all went public this year and their stocks immediately surged. Several high-profile venture-backed technology companies like Home Away and Kayak Software

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are queuing up to go public once the markets stabilize. In addition, Microsoft Corp. recently made an offer to buy Skype for nearly \$8.5 billion, U.S. regulators gave their approval to the proposed merger in June, and European regulators approved the merger just this month. Moreover, companies like Second Market have created a web-based venue for pre-initial public offering liquidity events, and new exchanges in the private secondary markets are creating a lot of hype for emerging growth technology companies.

In my opinion, lawyers are uniquely positioned to be the lynchpins in facilitating the development and fostering the growth of the technology start-ups they represent. By structuring and negotiating deals, reducing legal risk, and building and protecting their clients’ intellectual property portfolios, attorneys can almost single-handedly make or break a new technology company. As counsel to a variety of technology companies, however, I have found that too much “lawyering” can be a company killer.

In the “.com-boom” of the late 1990s, I was in-house counsel for a software development company in San Francisco. My first order of business was drafting a comprehensive, airtight, fool-proof 15-page licensing and distribution agreement — that virtually nobody would sign. There were a few takers, but negotiating that agreement with prospective partners would take weeks, if not months; and time is not a luxury that companies have when trying to bring a new technology to market.

Based on feedback from our business development executives, I tried a new tactic: Stop being such a lawyer. I took that 15-page behemoth of



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A man walks past an Apple store, covered with notes from supporters, on Oct. 19. The store was closed for CEO Steve Jobs’ memorial service.

an agreement and boiled it down to its bare legal essentials in the form of a one-page document. Lo and behold, the pipeline started to empty — and deals began to flow. Though that one-page agreement didn’t work for every type of engagement, it prompted our company to create separate, standardized versions of the agreement that varied based on three criteria: complexity of the proposed transaction or relationship; a risk assessment of each prospective partner; and a cost-benefit analysis. The smaller, simpler, less risky, less profitable partners got the one-pager, and we executed them in large volumes. The larger, more complex, higher-risk, higher-reward partners, received a more full-bodied version of the agreement. The “tweeners” received a hybrid of these. Within six months, we went from 50,000 users to 3.5 million.

To curtail the excessive “lawyering” at technology companies, senior executives need to rely on the quasi-Buddhist mantra of Jobs: focus and simplicity. To that end, you must require that legal counsel keep it simple (despite their legal training) and make sure to stay focused on the business of business rather than the business of law when structuring your deals.

Apply this same approach to raising seed capital from angel investors, and don’t forget that less is more. In light of the relatively simple relationship you want with your angels, and the low risk associated with raising convertible debt rather than equity, you should keep your investment documents simple and standardized, and be fair and reasonable in your approach to initial investors. By using a balanced, non-negotiable, convertible preferred note to raise money from angels that lets them either get their money (plus interest) back soon or convert their investment into preferred stock at a 10 to 30 percent discount from the subsequent Series A valuation, you will not only speed up the process of raising seed capital, you will also reduce the legal fees you incur.

Also, don’t raise too much money from your angels — remember, less is more. Raise just enough to enable your company to stay true to your business plan, build and launch the initial version of your technology, and get you to the

Series A round of financing. By delivering a viable product on a limited budget, you will create goodwill with initial investors, encourage them to not only convert but also invest new capital in the subsequent rounds of financing, get the valuations you so desire, and lay the foundation for smooth negotiations with Series A investors over dividend and liquidation preferences, voting rights and anti-dilution provisions.

Finally, when it comes to protecting your intellectual property portfolio, internally make sure that all of your employees sign comprehensive confidentiality agreements that include restrictive covenants related to non-disclosure, non-solicitation and non-competition. In addition, all employees must sign invention assignment agreements and independent contractors must sign work-made-for-hire agreements that assign to your company all of their rights in works of authorship that you pay them to create, and disclose any technologies that they are in the process of developing, or have developed on their own, and in which they claim an independent ownership interest.

Moreover, you must go to great lengths to ensure that your company has a trade secrets policy that is understood by all, skillfully implemented and aggressively enforced. The last thing you can afford as a new technology start-up is to have your trusted developers, programmers and engineers stealing your ideas and using them to compete against you.

Focus and simplicity may seem like foreign concepts to lawyers, but this approach to legal counsel can help new technology companies become the next Apple; and if your business model is solid and your idea is innovative, don’t let too much “lawyering” prevent you from building a successful, sustainable technology company and becoming the next Steve Jobs.



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