GETTING ADVICE, COMMITTING TEAMS AND INCORPORATING ©

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WHY SHOULD A START UP GET LEGAL SUPPORT?

LEGAL SUPPORT IS CRUCIAL

1. Setting up a business is exciting, but without the right legal advice, it can be a disaster…
2. You are a business owner, not a legal expert. Yet, many complicated legal issues might arise during your journey… and you might do mistakes

SOME COMMON MISTAKES…

1. **No founders agreement**: working with a co-founder without signing a founders agreement and ending up in litigation over ownership of shares or IP;
2. **No adequate business structure**: setting up a type of company that is not appropriate;
3. **No adequate employment advice**:
    a. Hiring employees without adequate legal documentation (NDAs, non-compete, etc.);
    b. Firing employees illegally which might expose you to litigation and indemnities.

SOME COMMON MISTAKES…

4. **No adequate operating contracts**: Signing contracts downloaded from the internet with clients, suppliers, etc. with terms that are not appropriate or that are contrary to mandatory laws;
5. **No adequate IP protection**: this might expose you to third parties claims or put your IP at risk of infringement.

COMMITTING THE FOUNDERS

1) FOUNDERS AGREEMENTS

CONTEXT

1. You are teaming up…
2. Several stakeholders, you need to distribute roles and equity ownership…
3. You need to avoid potential problems with your partners and set everything clear…
4. You want to make it official…

CONCERNS

1. If no confidentiality agreements are signed: risk of disclosure
2. If no proprietary rights agreements are signed: no visibility on owner of IP rights
3. Financial needs are increasing and funds are invested (What are the implications on ownership of shares?)
4. What if one of the founders leaves the business and quits?
5. No clarity on the distribution of roles (who's doing what?)
6. No visibility on future company: when will we incorporate? Type? Chairman? etc.

SOLUTION – SIGNATURE OF THE FOUNDERS AGREEMENT

Common clauses:

a. Testing phase: you test your product and based on the tests results, you decide to incorporate or not.
b. Commitment of the founders to devote their business time to the project.
c. Distribution of roles and responsibilities (pre and post incorporation).
d. Funds management (if you receive grants, opening of a joint account, withdrawal and spending policy).
e. Identification of the initial investment (portions to be paid by each founder)
f. In case more money is needed, who will advance it? In which proportions?
g. Founders remuneration (pre and post incorporation).

g. Approach of potential investors/angel investors.
h. General provisions re. future company (name, type, capital, ownership percentages, chairman and BOD members).
i. Shares vesting.
j. IP rights.
k. Confidentiality.
l. Exclusivity.
m. Term and termination / amendments.

Enforcement of the Founders Agreement:

a. Binding agreement → Breach = contractual breach = recourse to the courts or to an arbitrational body
b. Damages
c. Forced performance
d. Penalty clauses

2) VESTING

What is vesting?

1. Process by which a Founder accrues definitive rights over the ownership of shares in the company
2. Vesting schedule → when ? in which percentage?
3. Vesting and reverse vesting.

Vesting objectives

1. Upon incorporation, distribution of shares on the basis of:
   a. financial contributions,
   b. continuing efforts and commitments of the founders.

2. It would be unfair for one of the founders to quit the venture after a few weeks or months, but still be permitted to keep all of his shares.

→ impose reasonable vesting restrictions upon incorporation

Vesting mechanism

1. Usually, 25% every year for 4 years on a monthly basis.
2. Possibility:
   a. to provide for a one-year cliff (where no shares will vest and all shares shall be unvested); or
   b. to vest a portion of shares “up front” (portion already vested)
3. Easier in some foreign systems where:
   a. The capital is authorized and not issued. Stock is issued as the shares vest; or
   b. Where the company can buy back the Founders’ shares if they quit.
4. In Lebanon, due to particularities of the law, vesting terms can be adapted through a mechanism of reciprocal options to buy/sell.

3) SHARES LOCK-UP

- Period of time during which the Founders are not allowed to transfer their shares in the Company
- Usually 3 years
- Negotiate a certain percentage of shares to remain free from lock-up, usually 10%
- Or negotiate a progressive unlock.

4) MANAGEMENT LOCK IN

- Founders will sign management contracts with the Company.
- Clause by virtue of which the Founders cannot resign from their management position before a certain period of time.
- Usually 3-5 years.

COMMITTING THE EMPLOYEES

1) STOCK OPTIONS

What are stock options?

1. Right given to an employee to **buy** some of the Company's shares at a certain price (strike price).
2. Stock options v/s shares grants.
3. Options are vested → the right to exercise the option is conditional upon the employee remaining at the Company → options shall vest progressively (4-5 years).

Founders’ concerns

1. Who is going to bear the stock options? The Founders only or the Founders and the Investor? (dilution)
2. Negotiate that the ESOP shares will dilute everyone (including the investors)

2) CONTRACT DURATION

DETERMINED PERIOD CONTRACT

- Securing that the employee will stay for a minimum period
- However, if the employee’s performance is bad, the contract can hardly be terminated.

UNDETERMINED PERIOD CONTRACT

- Risk that the employee leaves the company at any time
- Termination by the employer can be difficult

3) SOCIAL SECURITY ENROLLMENT

Enrollment is mandatory…

1. Irrespective whether the contract is a determined or undetermined period contract / full time or part time.
2. Contributions:
   1. Sickness and maternity: 11% (3% borne by the employee / 8% borne by the employer)
   2. Family allowances: 6% borne by employer
   3. End of service: 8.5% borne by employer

INCORPORATING YOUR COMPANY

Type of company

1. Most common types of companies in Lebanon: joint stock company (SAL) and limited liability company (SARL)
2. The most suitable type of companies for a start-up is the joint stock company (SAL)
3. To benefit from circular 331 of the CBL → company must be incorporated as an SAL (including holdings but excluding offshores)

Status and limitation of liability

1. The SAL is an independent legal entity
2. Shareholders are not liable on their own patrimony
3. Advantage in comparison with:
   - Establishments
   - Other types of companies

General information about an SAL

1. Minimum number of shareholders: 3
2. Minimum capital: 30,000,000 LBP
3. Corporate bodies (Board of Directors, General Assemblies, Chairman General Manager, Assistant General Manager)
4. Auditor / supplementary inspector
5. Legal advisor

Incorporation process

1. Signature of by-laws (notary – stamp duties)
2. Bank account opening (deposit of capital – certificate of deposit)
3. Signature of constitutive documents (minutes of meetings, commercial circular etc.)
4. Registration with the Register of Commerce

Timeline: 3-5 days

Costs, expenses, fees

1. Incorporation and registration expenses (Notary Public, Register of Commerce, fiscal stamp duty, etc.): approximately 3,000,000LBP
2. Legal fees (incorporation / maintenance)
3. Auditor fees

Taxation

1. 17% corporate tax
2. 10% on dividends distribution tax
3. 2,000,000 LBP per year (lump sum tax).