

BCIC New Ventures
Corporate Structure

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About Fasken Martineau DuMoulin LLP

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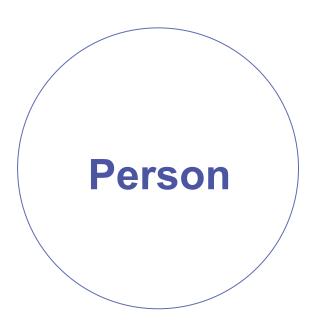
Overview

The initial corporate matters you need to consider in building your technology company:

- Initial Corporate Structuring Issues.
- Allocating Founders Shares.
- Preparing a Financing Plan.
- Sourcing Seed Capital.
- Allocating Stock Options.
- Financing a New Venture.



The Founder





The Others









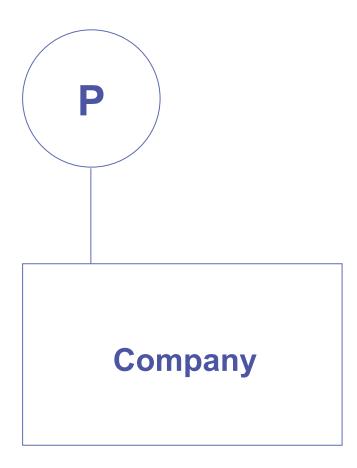


Options for Association

- Proprietorships
- Partnerships
- Limited Partnerships
- Joint Ventures
- Companies
 - Provincial
 - Federal
 - International

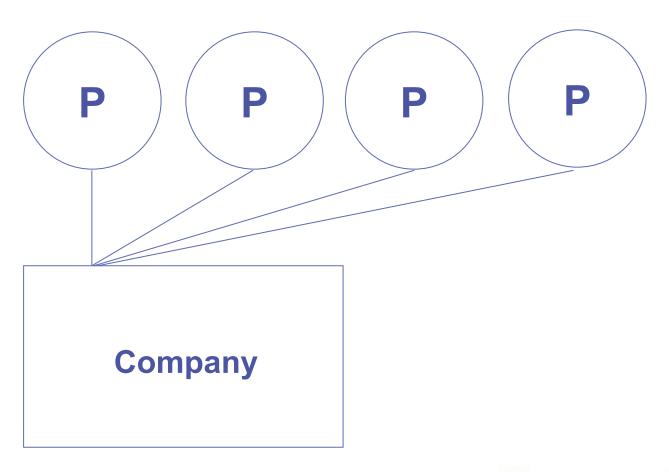


Incorporation



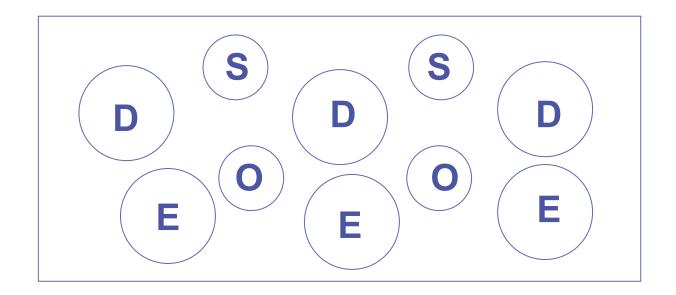


Incorporation



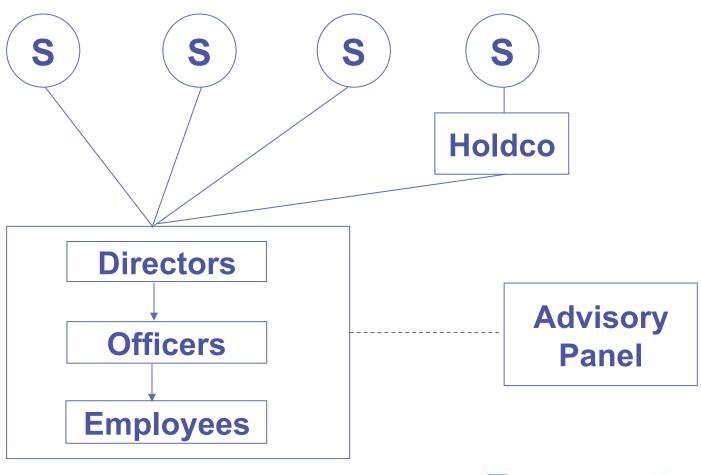


The Company



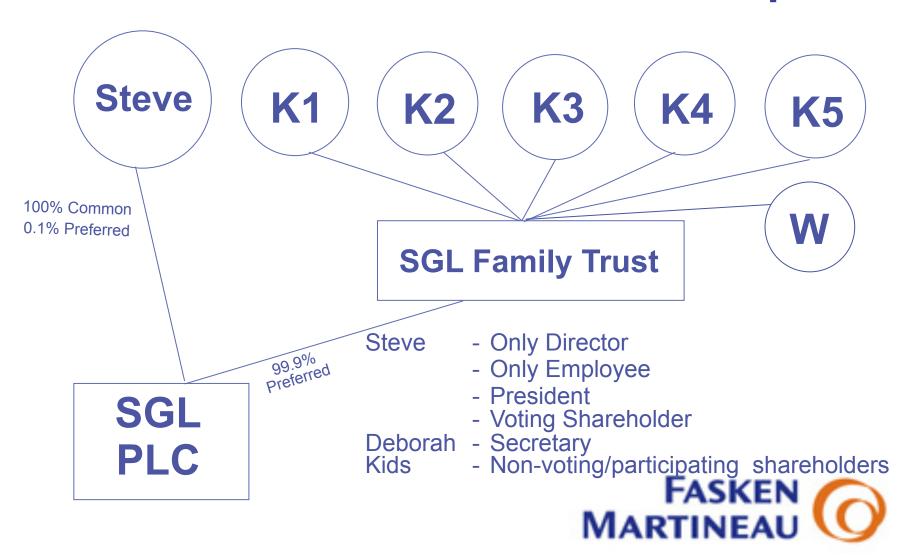


The Structure





Steven G. Lukas Personal Law Corp.



Shareholders

- Anybody can be a shareholder
 - o individuals
 - companies
 - o partnerships
- As many as you want
 - rules change at 50 "people"
 - rules on how you find your shareholders (ie: see a lawyer!)



Shareholders (cont'd)

- No liability aside from the initial investment in the shares of the company
 - (unless a contract says otherwise ie: shareholders' agreement, guarantee)
- Variety of share classes, rights, restrictions
 - voting, non-voting
 - participating/non-participating
 - options, warrants, rights



Shareholders (cont'd)

- Exclusive right to elect directors
- Pre-emptive rights
- Relationship governed by Articles,
 Shareholders' Agreements



The Policy Setters

Directors



Directors

- Elected by the shareholders
 - (but can fill "vacancies" and increase number in certain circumstances)
- At least one
- If BC, no residency requirement
- Qualifications

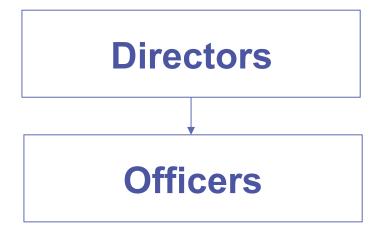


Directors (cont'd)

- Power to manage the affairs of the Company
 - (subject to articles, shareholders' agreements, etc.)
 - o determine policy
- Duties to the Company and the "shareholders as a whole" to act fairly and diligently
- Potential personal liability
 - breaching duties
 - taxes, wages
- Appoint the Officers



The Instructors





Officers

- Appointed by the Directors
- As many as you want, any titles at all:
 - President, Chairman, CEO, COO, CTO, VP, Secretary, etc.
- In charge of day-to-day affairs of the Company



The Doers





Employees

- O Do all the real work
- © Employee v. Contractor
- Employment agreement
 - confidentiality
 - o assignment of intellectual property
- Compensation
 - o cash
 - o shares
 - options



The Advisors

Advisory Panel

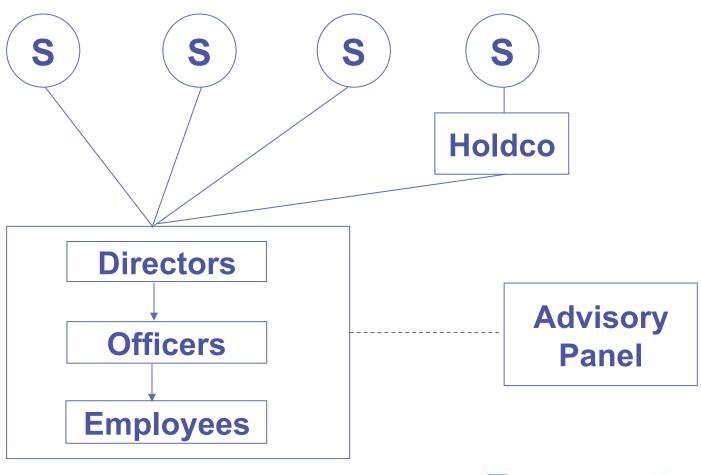


Advisory Panel

- Non-Director Experts
 - o focussed on the field in question
- Advise the Board



The Structure





Other Issues

- Conflicts of Interest
 - within the structure ie: your role as Shareholder v. Director
 - within other companies ie: director of this Company and director of contracting company
 - between the Company and the educational institution - ie: technology transfer/pricing/ time
 - o between investor and inventor
- Public v. Private



Initial Corporate Structuring

Incorporation – U.S. v. Canada v. Offshore; Canada because:

- Financing Issues Investors don't like offshore companies.
- Government grants In most cases, only available to Canadian companies.
- Taxation and Employment issues Are simpler if you are building the company here.

B.C. (BCBCA) v. Federal (CBCA):

Either BC Business Corporations Act (BCBCA) or Canada Business Corporations Act (CBCA) are fine and both are investor friendly.



Initial Corporate Structuring – cont'd

Create a structure with:

- Output Description of Common Shares.
- Unlimited number of "blank-cheque" preferred shares.

Financiers dictate financing terms:

Obebt vs. equity, price, preferences, terms of SHAG, etc.

If you can, avoid:

- Issuing secured debt.
- Using shareholders' loans.
- Using multiple share classes.
- Incorporating offshore.



Founders' Shares

What are Founders' Shares?:

- Large block of shares issued at a low price to position the Founders.
- To recognize their "sweat equity" contribution.

What class of shares should they be?:

© Common shares.

At what price should they be issued?:

Nominal - \$0.0001 to \$0.01 per share.



Founders' Shares – cont'd

To whom should they be issued?

- Founders and senior officers.
- Not to employees or outside investors.

Common mistakes in allocating Founders' shares:

- Not setting aside enough Founders' shares at time of incorporation: 4.0M – 8.0M.
- Not setting aside some Founders' shares for future additions to the management team: set aside 15% -25%?
- Not vesting the Founders' shares: 2 4 years, or providing for "reverse-vesting".
- Issuing them to the wrong people.



Preparing a Financing Plan Determine a "Road-Map" for financing:

The company determines its developmental "milestones":

- What they are.
- By when they will be met.
- o How much funding is needed to meet them.

The milestones are integrated with the budget and a timeline to determine how many tranches of financing will be needed and when.

This info is used to prepare a sample capital structure table - a "road map" for the financing trail (e.g. – to raise \$5.0M).



Sources of Financing – Debt/Grants

Non-equity financing might come from:

- Government grants/credits/refunds:
 - VCC Program.
 - NRC, IRAP, TPC, SRED.
 - Telefilm Canada and other industry specific organizations.
 - Environmental/"green" grants.
- Quasi-governmental organizations like:
 - BC Innovation Council, Business Development Bank of Canada etc.



Sources of Financing - Equity

Initial (equity) seed financing may come from:

- The "Founders".
- Their "Friends and Family".

Follow on rounds (pre-public) from:

- Angels.
- Venture Capitalists.
- Investment bankers (both private and institutional).
- Output
 Underwriters (i.e. brokers).
- Public financing Initial Public Offering.
- Strategic Partners.



Sources of Equity Financing – Revisited

Categories of Financiers:

Founders: Variable

Friends and Family:
\$50K - \$150K

• Angels: \$250K - \$500K

Venture Capitalists:
\$1.0M - \$3.0M

• Underwriters:
\$1.0M - \$5.0M

Strategic Partners:
Variable

Match potential investors with your Financing Plan to maximize chance to secure investment.



Securities Legislation

Requirement:

- o If you distribute a security, you must:
 - o file a prospectus

OR

 Rely on exemption from prospectus requirement



Exemptions

- Family, Friends and Business Associates
- Accredited Investor
- O Private Issuer
- Offering Memorandum



Family, Friends & Business Associates Exemption

Can sell securities in any amount without any disclosure to:

- Director, senior officer or control person
- Family member of a director, senior officer or control person



Family, Friends & Business Associates Exemption (cont'd)

- Close personal friend or close business associate of a director, senior officer or control person
- No limit on number of purchasers or amount that can be raised



"close personal friend" or "close business associate"

- Mas known the director, senior officer or control person for a "sufficient period of time"
- Is in a position to assess the capabilities and trustworthiness of the director, senior officer or control person



Accredited Investor Exemption

- "accredited investors" can purchase any securities in any amount at any time
- No limit on number of purchasers or amount that can be raised
- Either public or private companies, partnerships, etc.



"accredited investor"

- Individual, corporation, limited partnership, trust or estate with net assets of \$5 million
- Individual with cash and financial assets over \$1 million
- Individual whose net income exceeds \$200,000 (\$300,000 with spouse) in each of the past 2 years



"financial assets"

- Meaning of financial assets
- Does not include real property



Private Issuer Exemption

Can sell securities in any amount without any disclosure to:

- Director, officer, employee or control person
- Family member of a director, senior officer or control person



Private Issuer Exemption (cont'd)

- Close personal friend or close business associate of a director, senior officer or control person
- Current holder of designated securities
- Accredited investor
- Person or company that is not the public



"private issuer"

- Not a reporting issuer
- Common shares are subject to restrictions on transfer
- Fewer than 50 shareholders
- Has only distributed its common shares to persons listed in exemption



Offering Memorandum Exemption

Issuer can sell securities to anyone in B.C. in any amount if Issuer:

- Delivers an offering memorandum in the prescribed form
- Obtains a signed Risk Acknowledgement from the purchaser



Risk Acknowledgement

- Clear, blunt statement of risks of investing in exempt market securities
- Issuer must give a copy of the signed Risk Acknowledgement to purchaser prior to making investment



Liability for Misrepresentation

If the offering memorandum contains a misrepresentation, the purchaser has:

- A right of action for rescission
- A right of action for damages



Other Exemptions

- © Employees
- Permitted consultants



Capitalization Table Founders' Round

	No. of Shares	Price	Funds Raised
Founders (3)	6,000,000	\$0.0001	\$600
Type of Investor (?)	?	?	?
Type of Investor (?)	?	?	?
Type of Investor (?)	?	?	?
Type of Investor (?)	?	?	?
Total:	6,000,000		\$600

VALUE: \$ 600 FOUNDER'S INTEREST: \$600 (100%)



Capitalization Table Friends & Family Round

	No. of Shares	Price	Funds Raised
Founders	6,000,000	\$0.0001	\$600
Family and Friends	400,000	0.25	100,000
Type of Investor (?)	?	?	?
Type of Investor (?)	?	?	?
Type of Investor (?)	?	?	?
Total:	6,400,000	-	\$100,600
PRE-MONEY VALUE: POST-MONEY VALUE:	\$ 1,500,000 \$ 1,600,000	FOUNDER'S INTEREST	FASKEN \$\$\ferror{\partial \text{FP} \text{PP} \text{PP} \text{PP} \text{PP} \text{Q3.75} \text{V})

Stock Options

What are stock options?:

- The right to purchase a number of shares at a predetermined price.
- Used to incent the team building the Company.

How many should be issued?:

o 10% - 30% of issued share capital.

At what price should they be issued?:

Last round of financing or higher.



Stock Options – cont'd

Companies must plan for growth and make a notional allocation of their options.

Allocate stock options by category:

Senior Management: 35% - 50%

Remaining Employees: 25% - 35%

Board of Directors: 13% - 20%

Board of Advisors: 2% - 5%

Contingency: 10% - 15%

Companies should:

- Integrate Stock Option Plan with their HR Plan.



Capitalization Table Stock Option Plan Added

	No. of Shares	Price	Funds Raised
Founders	6,000,000	\$0.0001	\$600
Family and Friends	400,000	0.25	100,000
Type of Investor (?)	?	?	?
Type of Investor (?)	?	?	?
Type of Investor (?)	?	?	?
Total:	6,400,000		\$100,600
Option Plan	1,500,000	n/a	n/a

PRE-MONEY VALUE: **POST-MONEY VALUE:**

\$ 1,600,000

\$ 1,600,000 FOUNDER'S INTEREST:



Capitalization Table Angel Round

	No. of Shares	Price	Funds Raised
Founders	6,000,000	\$0.0001	\$600
Family and Friends	400,000	0.25	100,000
Angels	1,200,000	0.35	420,000
Type of Investor (?)	?	?	?
Type of Investor (?)	?	?	?
Total:	7,600,000		\$520,600
Option Plan	1,500,000	n/a	n/a

PRE-MONEY VALUE: \$ 2,240,000 FOUNDER'S INTEREST: \$2,100,000 (79%)

POST-MONEY VALUE: \$2,660,000



Capitalization Table Series "A" VC Round

	No. of Shares	Price	Funds Raised
Founders	6,000,000	\$0.0001	\$600
Family and Friends	400,000	0.25	100,000
Angels	1,200,000	0.35	420,000
Venture Capitalists	3,000,000	0.50	1,500,000
Type of Investor (?)	?	?	?
Total:	10,600,000		\$2,020,600
Option Plan	1,500,000	n/a	n/a
New Options	500,000	n/a	n/a

PRE-MONEY VALUE:

\$ 3,800,000 FOUNDER'S INTEREST:

MARTINEAU

POST-MONEY VALUE:

\$ 5,300,000

Capitalization Table \$5.0M Raised

	No. of Shares	Price	Funds Raised
Founders	6,000,000	\$0.0001	\$600
Family and Friends	400,000	0.25	100,000
Angels	1,200,000	0.35	420,000
Venture Capitalists	3,000,000	0.50	1,500,000
VC/IPO	3,000,000	1.00	3,000,000
Total:	13,600,000		\$5,020,600
Option Plan	2,000,000	n/a	n/a

PRE-MONEY VALUE: \$ 10,600,000 FOUNDER'S INTEREST: \$ 6,000,000 (44%)

POST-MONEY VALUE: \$ 13,600,000



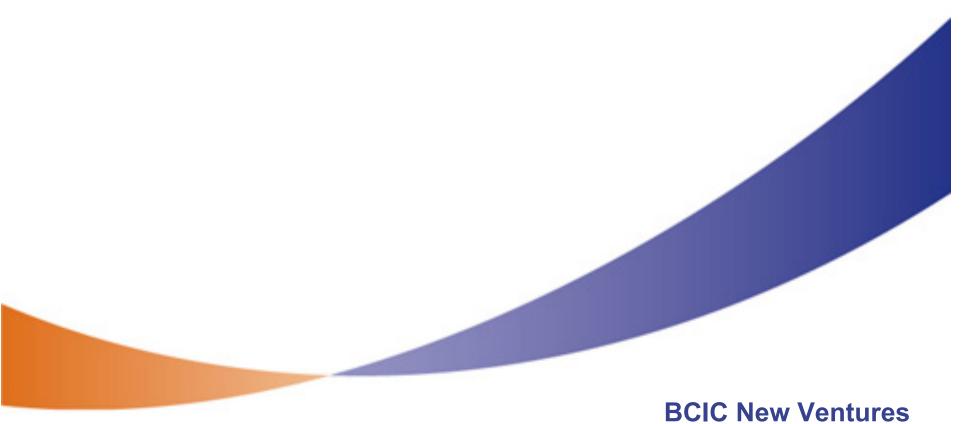
Capitalization Table After Option Exercise At The Time of IPO

	No. of Shares	Price	Funds Raised
Founders	6,000,000	\$0.0001	\$600
Family and Friends	400,000	0.25	100,000
Angels	1,200,000	0.35	420,000
Venture Capitalists	3,000,000	0.50	1,500,000
VC/IPO	3,000,000	1.00	3,000,000
Options	2,000,000	0.35	700,000
Total:	15,600,000	n/a	\$5,720,600

PRE-MONEY VALUE: \$ 13,600,000 FOUNDER'S INTEREST: \$ 6,000,000 (42%)

POST-MONEY VALUE: \$ 14,300,000





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