THE BARCODE PODCAST

Episode 029: Matt Bair – Success Is In the Details

BEN Welcome to the Barcode Podcast. My name is Ben Ponder, I'm your host. I'm really excited to have Matt Bair in the studio with me today and we're going to be talking about all kinds of interesting things that you may not think are interesting. Hopefully, we're going to make it interesting in the context of our conversation and that relates to legal stuff, which you think, oh man, this is going to be like contracts and stuff, but as I think you'll see, everything hinges on this. Your success and failure in your business really is going to be determined to some large extent by how well you execute with some of these nitty gritty details. We're going to talk through all that in just a moment.

A couple of things. I want to remind everybody that the Barcode Podcast is presented by Titanium CPG Insurance. Titanium protects forward-thinking consumer brands with a range of commercial insurance products and risk management services that are designed specifically for natural and organic food and beverage companies. You can learn more online at TitaniumCPG.com and I do want to say before we even kickoff the conversation that we're going to be talking about legal stuff today. Matt is a lawyer, so obviously, there will be some legal banter here, but that no one should construe anything we say here as legal advice or counsel and we encourage you to talk to your own attorney and representation about anything that we talk about here today.

With that, I want to introduce you guys to Matt Bair. He's a partner at Egan Nelson here in Austin. Welcome, Matt.

MATT It's a pleasure to be here. Thanks Ben.

BEN Really glad to have you. You focus on corporate finance and securities and you've worked with a variety of family offices and venture capital and private equity firms, as well as startups all the way from formation through exit. We're going to touch on all that stuff, but before we do that, tell me and tell us about your favorite meal ever.

MATT My favorite meal ever. I would have to say that it would be at restaurant Don Alfonso 1890, which is in Italy. This was 25 years ago. I went with a group of four other friends. It was my first time to go to Italy and we went to Rome and then south to the Amalfi Coast. At the time, I was a real big fan of wine and learning about wine. We'd done some reading that there was this great restaurant. It was in the hills above Sorrento, so we had made a reservation months in advance. It was a Michelin two-star restaurant, so when we checked in to our hotel in Sorrento, which was also kind of up from the town, we said, "Look, we've got dinner reservations tomorrow night at Don Alfonso, how far is that?" He said, "Oh, well Don Alfonso is my cousin. That's just up the walking path from here."

BEN Which is how you get around to all the places there.

MATT Exactly, I was like, well this is really starting to come together already.

BEN That's right. You also wonder if any other restaurant he'd have said, "Oh, he's my cousin."

MATT He's my cousin as well. Absolutely, and it's just down the path. Yeah, no doubt about it, so it was one of those real fine-dining restaurants where you better be prepared for three and a half hours and that's exactly what it took us.

BEN Everything is a presentation.

MATT Oh, it was incredible. It was a nine-course meal, we did the tasting menu, of course, and they grow everything there, they catch the fish that day and they're just so deliberate about the food and the freshness of the food and how it's crafted. We just said, "Please pair it with wines. Don't kill us." We weren't rich. We said, "Just make it reasonable," because the wine steward there, they had a 25,000-bottle cellar, so they knew exactly what to pair it with that were not necessarily these big labels that all Americans had heard about and that were local.

BEN That's right. You trusted their expertise more than your own expertise.

MATT No doubt about it. No doubt about it. I can just sort of remember three of the courses, they actually said, "Voila," when they took the cover off the plate. Of course, they all came out at once, so they had all of the servers come, so that everybody was served at the same time.

BEN Yeah, the big reveal.

MATT They literally said, "Voila," and I said, "That's it. I've arrived." This is as nice as it gets and in fairness, the food, everything was remarkable. They didn't over-serve you; they weren't huge plates. I didn't mind that they were small, little bites because there was another one on the heels of that. And we had some great wine in the process.

BEN Perfectly paired with the right wine for each course.

MATT Yeah. I think it's still to this day is maybe the most expensive meal that I've ever paid for, but it seems to have been worth it and I don't think I'm just talking myself into justify it.

BEN Clearly memorable. Well, it sounds like you were there with friends, too.

MATT Yeah.

BEN Being there with friends, being in a gorgeous place along the Amalfi Coast and that sort of thing doesn't hurt, but it's about that moment, the food, everything about it being perfect.

MATT Yeah, and I think that's exactly right. It was with a friend of mine that I'd known, actually, my earliest childhood friend, who I'm still very close with and we keep in touch. He lives in New York and his wife and brother and sister. It was a really fun event and he and I still talk about it as sort of this mythical evening at Don Alfonso. One day, I feel like I want to go over there and go with my wife and even take my kids.

BEN I know. I love it. You're giving all of us great recommendations if we ever travel.

MATT If you're ever there-

BEN That's excellent.

MATT ... I don't know if it exists, but yeah, it does in my mind.

BEN May be another cousin that runs it now.

MATT Undoubtedly.

BEN That's right. Let's talk a little bit about, so your practice, as a corporate finance and securities attorney, you're focused, but you're focused on what is very fitting for Austin as a town, kind of these two areas of technology and then, also consumer packaged goods.

You've done a lot of stuff in those. Then, as a creative problem solver, you've had to do a variety of different types of work. A lot of our listeners are early stage CPG founders. First of all, they're trying to make a decision about kind of everything. Right? They come up with an idea, whether it's a consumable product, a food or beverage, or it's a widget that they think they're going to sell on Amazon or some other place.

MATT Right.

BEN What is the first point in the life of a startup where they should begin to think about legal stuff?

MATT Yeah. Good question. For sort of on behalf of all of the lawyers in the community, very early in the process I would say.

BEN That's right. Not too late. Yeah.

MATT By the way, that doesn't mean that you necessarily need to go pay a lawyer, it means that you need to start thinking about the legal stuff early in the process. In particular, I would say if you're at the moment a solo proprietor and you're developing a product and it's really just a matter of trying to find out if there's interest in the product and things like that, there's probably not a lot of things that you have to do and spend money on and I would discourage you from spending any money on that. Spend money on the product and getting it out there.

BEN Getting it right.

MATT Exactly. I'll contrast that with the technology companies, I've represented quite a few of them and during the several different booms that we've had in Austin and technology, and this one I'm recalling was back in the late '90s, working with the technology company that had not even launched their product, but they had like 50 patents that had been filed and applications done for things all over the world because the assumption was that they were going to be wildly successful, so they needed to spend all this money to protect their IP. Guess what? They never sold one product and that company is now gone.

BEN Ouch. Well, and I think that's a good point. We probably won't talk about intellectual property that much today, but I think it's important for people to understand, particularly like with food and beverage stuff, that your idea, let's say it's a recipe, it's a trade secret. Right? It is typically not patentable unless maybe you've invented some new equipment that is the only way you can make the thing.

MATT Right. Or a pharmaceutical combination or something. Yeah.

BEN That's right, yeah. Some sort of novel chemistry thing that you did, but in most cases, what I see, and I think is important for people to understand, you want to be guarded. Perhaps, I think sometimes people are maybe overly protective of that stuff where they feel like the idea itself is the magic.

MATT Right.

BEN It's not. I promise you. The execution will determine your success or failure, not just having an idea, but even the Colonel's Original Recipe, or the recipe for Coca Cola, those are trade secrets. They're not patented.

MATT Correct.

BEN I think it's important to even know that going in that if you spend too much of your time, energy, or potentially money on that stuff too early, you're probably wasting your time. You should just probably be more careful.

MATT Well, and that, I think, you bring up an important point that I tell clients all the time because they'll say, "We're going to show somebody a lot of information about our product and even some of the processes by which we make it and things, so I need an "iron clad NDA," non-disclosure agreement.

BEN Right.

MATT The answer is, it's only as good as the piece of paper that it's written on. Yes, if you have an ethical person on the other side that signs it and abides by it, it's useful, but at the end of the day, if it's really important to you, unless there's a strong, strong business reason, maybe this is a potential buyer or this is somebody that's going to bring you a lot of money or help you in some way, don't give them the recipe. Don't show them how to make the secret sauce.

BEN That's right.

MATT Keep it to yourself. I think that that is really the reason I brought up the IP story or the idea of spending a lot of money on patents. I think it is IP that you have to be thoughtful about very early on if you're truly sort of a solo and that is just being thoughtful about. If there is something that you regard as proprietary, the ingredients for the cookies or how long you put them in the oven and then putting them in the icebox, whatever it is, keep that to yourself. If you're going to engage friends in it, there's no reason that you couldn't ask them to sign a non-disclosure agreement as well. Those are available online, they're all about the same. There's bells and whistles that people may want to add in some circumstances, but make sure that you're not giving up the keys right out of the box.

BEN Right. Well, I think that's a great point and I think it's also about choosing partners who are trustworthy, that you have a level of confidence in and you're not just being willy nilly about these things because to your point, that's a signal that both parties, a mutual non-disclosure agreement, is signal that both parties are committed to an environment of confidentiality in proprietary information, but it doesn't keep loose lips from sinking ships either, right?

You want to be, I think, thoughtful about that stuff. Let's say it's a food product, your product can be reverse engineered. It just can. Like a sophisticated person can reverse engineer just about anything. Your brand, if you're building a company that you anticipate, particularly if it's a company that you anticipate will sell one day or maybe IPO or whatever, then actually the value of your company is in the brand. Right? Which is not just the logo, it's the whole kit and caboodle, but the logo and the name and all that kind of stuff does matter a lot for that because that's going to be what people recognize.

MATT Right.

BEN If you're going to focus your energies on the intellectual property side, particularly in the consumer brands world, you should probably be very, very aware of some of the differences and interesting things there and you might want to pay more attention to trademark related stuff, even then patent related stuff. Like, you're at the farmer's market, you're at some small scale and you grow. Then, all of a sudden, you get a cease and desist letter from somebody else who said that because you're using somebody else's name or something they have a right to and you didn't take the probably five to 10 minutes it might have taken to search the US Patent and Trademark Office database to see, oh, there's actually somebody else whose named that and they're doing the exact same thing that I'm doing.

MATT Yeah. Great point and I think that in my mind, that's really, again, putting aside collaborating with other people and having multiple people that are going to be your partners or investors in it because that's sort of the next step, but really thinking about the brand and protecting the brand. Honestly, again, step one, you don't have to pay a lawyer to go figure out if there's another product that's identical to yours out there on the market today. There's thing called Google, number one, and as you said, the Patent and Trademark Office has a very good search engine, it's free, you can type in the information and maybe it's going to be the same name, but in a completely different application or use, so you might be okay.

Honestly, if you've got a name that you think that you've worked hard to identify and you think it really is clever and fits your product and somehow it creates that certain panache or connection to your product that you want your consumers to associate the product with, consider calling up a trademark attorney and getting that advice.

BEN Right. This is someone who's really focused on that.

MATT Absolutely.

BEN I think this is an important point because there are attorneys, they're generalist attorneys and that's fine, but in general, when we're talking about this, and I think this is some general advice for folks. What I tell people as a non-attorney is, for this kind of work, in general you're not trying to use your cousin, Vinnie, who does random, all kinds of divorces and whatever else, you're really trying to have somebody who has a little bit of experience or pattern recognition around the types of problems that you're facing because even if you feel like you got a better deal because you paid a lower hourly rate, they're probably learning on your dime in that case. Versus somebody who they do this all the time.

MATT Right. Well, and in the long run, you will save money because what happens is, particularly with branding and marks, the name logo or something like that, you're going to spend a lot of time and effort. The name of the game, in addition to sort of having a product that people just love, is to create that brand and the brand awareness in people's minds, so much of your focus about growing the business is to create that brand awareness. The early days, no one really cares or notices, but as soon as you start trying to get onto the shelf at one of the local supermarkets or something, people will begin to take notice and you say, that's when you get the cease and desist letter. That's two years in, who knows what you've spent on your packaging and other things.

Your graphic artist and all the other things associated with this, and then you've got to make the hard decision to change the name. Again, even as you say, don't get too hung up on the nature of the product. Anybody can reverse engineer it and go do it. Don't get overly hung up on the name, but guess what? It's important to distinguish yourself from something else, so selecting a name that you think is protectable, and ultimately protecting it, I'm a big fan of filing an application, an intent to use application, which gives you some early rights in the Patent and Trademark Office to protect that mark from others using the mark or selling a similar product under the same name.

In my opinion, it really just is some money well spent in the early days that can save you a lot of money later because a lawsuit, you're only going to pursue a lawsuit is if you spent so much that you now can't turn back and that's no good or you're young as a company and you can't afford it and you just have to change your name because you've gotten a cease and desist from General Mills that says we've got some product that you've never heard of, but that they've got on the shelves in the Northeast or something.

That is where I would say spend a little bit of money. The work is not terribly expensive. Most good trademark attorneys will quote you on a fixed-fee basis for a mark and they'll do a search and help you appraise whether it's a protectable mark and how strong it is and advise you on that. Then, get something on file.

Then, from there, honestly, that's also something that you can use later when you're talking to investors because they'll say, "Well, tell us what you've done to protect your brand." You'll say, "Well, I've got a trademark and I filed it two years ago," or, "I've got a mark that hasn't issued yet," or maybe I do have that issued trademark. Just in the same way that investors in the technology space always like to ask, do you have patents on your technology, and oftentimes they never really look at the details, they just check the box, and they love knowing that you do.

BEN Right. It's a signal that you have your act together.

MATT Exactly. Yeah, that's it.

BEN If you're an investor preparing to part with your own money in this new venture, the more signals you can get that this person has his or her act together, that's a thumbs up, that's important.

MATT Absolutely.

BEN Probably for most startups, the first time, not always, but the first time that they have a deeper engagement with or relationship with an attorney is when they're thinking about fundraising. Right?

MATT Correct.

BEN Walk us through what does that process look like. Normally, and I think this is important because sometimes people think, "Well, how do I even start the process of fundraising?" One of the things that I recommend to people is you should know who your attorney is and have a relationship with that person before you begin the process of fundraising. Right?

This is not like, I've been trying to get investors for a long time, this sort of thing, and now I just need to paper some things up. That's a little bit later in the game, so kind of walk through maybe an ideal scenario in terms of how a first time or a smaller startup might engage with the right attorney.

MATT One thing to keep in mind, I mentioned it earlier, and that is the nature of the business, whether it's a solo proprietorship or a group of people that have come together and you need to get your house in order before you go out and try to raise money from third-parties. If you have several people that have already spent time and effort to develop the product and working on it together, get with an attorney and get the entity formed. You wouldn't operate as a general partnership, no one does. It creates unlimited liability for all the individuals involved, so even before your fundraising, sometimes you're asked to sign contracts and particularly if you're getting a product on the shelf or putting it even as a demo or freebie, sometimes people will ask for insurance.

BEN Right.

MATT Having an entity set up I think is important and we can talk about sort of the history of the entity.

BEN Yeah, we have an entity, so you're doing, you're registering that with the right states. If you're in Texas, you might have a Texas entity. Other places, you might decide for any number of reasons, typically upon the advice of counsel, that maybe you're going to form in Delaware or some other business friendly state, but you choose an entity type. You file that paperwork, perhaps you're getting an EIN, so you're kosher from a tax perspective. This is just the basic blocking and tackling of this is no longer just an idea or a project, but I'm actually trying to build a business.

MATT Yeah. Admittedly, you didn't ask about that, the formation of the entity, although that's a very important decision and there's a lot of factors that go into that about what entity to form, whether it's a limited liability company or a corporation. Those are the two most common that people use in the CPG space. What jurisdiction, whether it's Texas or most commonly outside of Texas, people choose Delaware. Let's assume for a moment that you have it formed, you've got your "partners" in the deal, the other two founders or your co-founder, and you're out to raise some money. I will say that in the early days for CPG companies, my experience has been that the first ask is kind of the rich family member or neighbor.

BEN The rich uncle, the friends and family.

MATT Yeah, exactly, but it's important, I think, to realize that what you do at that time can have an effect or consequence for many years to come. Most importantly, if you take money from the neighbor, from the aunts, the uncle that's not themselves a sophisticated investor, then you've financed the company with someone who is not considered to be an "accredited investor" under the FCC rules. As you grow, that can create problems for you, so it's better to at least get some advice before you take in third-party money. If it's just the people around the table that are getting the product off the ground and you're contributing money to the bank account that's okay, but as soon as you get that third-party investment, it's useful to have a better understanding of the structure by which that comes in.

BEN Let me pause there because I think that's an important thing. An accredited investor is an individual who... and this is according to the securities and exchange commission, SEC, and individual who has a net worth of a million dollars or more outside of their primary residence or there's another thing, they have to make over 200 something thousand dollars.

MATT $200,000.

BEN Yeah, for three years in a row or something along those lines. There's sort of a minor loophole about a sophisticated person. Maybe they don't have all those resources, but for some reason, they have special knowledge about investing or things like that. The point is, the reason the SEC created this rule, it really ultimately goes back to the great depression and all the people who lost their entire life savings through speculation.

MATT Right.

BEN The US Government, and the laws are structured so that your grandma, you don't say, hey, I've got a track of land in California and I want you to invest in making a gold mine out somewhere. Write me a check for your whole life savings and that sort of thing and then people get duped or bamboozled. They're doing it to protect investors, but it actually, to your point, also protects you as a founder because it makes sure that you are working with people who have the resources to actually invest the money, but then also frankly, not ruin every Thanksgiving for ever and ever as well because you lost their entire life savings, so you can't show your face around the family dinner anymore.

MATT That's absolutely right and you have a very good understanding of the background in securities laws. With the SEC and the Securities Exchange Commissions, the Securities Act has essentially a rule that says if you're going to sell stock to third parties or any kind of equity in your company, it has to either be registered with the SEC or subject to an eligible exemption. The exemption that people take advantage of is some or fashion of a private offering exemption, one that's not marketed widely, but when you hear of companies going public, they've prepared very detailed disclosure documents that they file with the SEC and the SEC spends time reviewing them and looking at them, making sure that they provided adequate disclosures, so that those investors that invest in that IPO or public company have all the information they need to make an informed decision.

In the private offering context, they shift the burden to the investor, in a sense, make sure that the investor is capable of taking care of themselves and that's why they put together that test that you mentioned earlier or that requirements for an accredited investor, mainly somebody that can afford to lose the investment or somebody that has gained enough net worth that you would hope is capable of being smart and thoughtful about what they're looking at and make good investment decisions. The reason that it becomes an issue is if you have those "non-accredited" investors in your deal, it can be a challenge for growing the business and doing transactions later because most of the transactions that companies that we deal with or engaged in are private transactions.

In my former, at a large law firm I was a securities' lawyer and we took companies public. At our current firm, that's not what we do. That's a very specialized practice as well. We focus on emerging companies and take them all the way through the lifecycle, but that usually means an exit, a buy by one of the larger players in the space. Those transactions are done pursuant to these private offering exemptions and one of the requirements is, is there be no unaccredited investors and if you've got unaccredited investors in the deal, you've just made it harder to sell your company. When investors that are more sophisticated are doing the due diligence and review of your books and records before they make, say, an investment in the company, they're very keen to note do you have unaccredited or non-accredited investors in the deal because their sophisticated to know that that itself can present that problem for your exit.

BEN It's a yellow to red flag for them.

MATT Yeah, so it's just something. Now, it doesn't mean that you can't survive with that. I've worked with plenty of companies that do that and, by the way, if you need the money to pay the rent to keep your ovens baking and things like that, you do what you got to do. I'm not suggesting that you let these esoteric issues of the law prevent you from surviving with your business.

BEN Yeah, there's the pragmatic of the approach to.

MATT That being said, the point is they can make a difference later, so part of that then means developing a relationship with the lawyers. Say, "Hey, we're doing this. We're going to try to raise some money. Should there be some things that we should do in advance?" Sometimes people like feel confident enough about their business that they want to create a set of terms and their lawyer can help them understand what sort of are current market terms for a business their size and a common device that people are using right now is convertible notes or convertible debt. It avoids having to make a valuation decision about what the company's worth, so rather than issuing equity, they'll issue debt that in a future transaction would convert into equity and maybe a little bit better terms in that later transaction.

BEN Because you're trying to reward that early investor, they made a bet on your earlier than anyone else did, so there's some different terms and we won't necessarily get into the weeds of all of that now, that will benefit that investor down the road whenever you have a price round at some point.

MATT Exactly.

BEN One of the reasons why people do that is it tends to be a little quicker and simpler. There are fewer points to negotiate at that point and the key issue that you pointed out is you don't have to make a determination of valuation yet. You can kind of make that determination depending on if you put a valuation cap. In that convertible note document, there's an implicit valuation where it cannot be more than a certain amount. Right?

MATT Yeah.

BEN There are ways that, even all of this legal stuff can be highly nuanced, but to your point, a lot of the time early stage companies are structuring those seed rounds or maybe even pre-seed or friends and family rounds in the form of convertible debt, which has a number of other benefits including that, at that point, before it converts over into equity, if you're an LLC, you don't have to issue a schedule K1 for that person because it's not equity yet. Technically, it's still debt for now.

MATT Yeah, good point. The reason that I also brought up that go call your lawyer is the people that you're looking for money from, they may not be regular investors in this space, so if you were to go to them and say, "Hey, I need a hundred-thousand-dollars, I'm trying to raise a total of $500,000 and I'd love it if you can come in for a hundred-thousand-dollars because we need to go buy some new baking equipment." I keep using the idea of baking cookies. We can stick with that.

In any case or we need to sign a lease and the landlord needs some sort of a deposit and all these other things, so we're at the point of raising money. That investor may not be very familiar with the structure that would be typical, so if you've got a set of terms that at least you validated are market terms, you can feel confident about that going out. You get that advice from your attorney and you can say, "Yes, here's a set of documents that my lawyer has put together that... and he tells me or she tells me that these are very standardized terms in the space and they're kind of middle of the road. They're fair and all." Of course, they'll want to read it, but you create your book of offering materials, including the structure and if there is a cap or valuation cap, like you mentioned earlier, you've thought about that in advance and put in a number. If you leave it blank, well now you're going to have to have a discussion about it and people will then want to understand why you think one number verse another as opposed to just saying here are the materials.

That's different than when you're at a later stage and negotiating with more sophisticated investors, institutional investors, say venture capitalists even at the series A level, they're going to have their set of terms and the way that they like to do it. You don't need to get ahead of yourself and present a term sheet. If you're truly the next great, great consumer brand, well maybe you can get away with your term sheet and just allowing people to bid on it.

BEN If there's a market frenzy around your deal.

MATT Yeah, yeah, exactly but 99% of the time, that's not the case.

BEN Right.

MATT Working with someone to help establish the parameters that you might take in that money, both because it makes the process easier when you're going out and talking to people because you've already got the terms that you've laid out and you hopefully, have understood them and can explain them a little bit. Then, secondly, there's structured in a way that their typical and so as later investors come in, the more sophisticated investors, the series A or series B institutional investors, there's nothing surprising about what you've done and there's no real gotchas in your capitalization structure that would be worrisome to a later investor.

BEN Yeah.

MATT I think it’s certainly an important milestone for a company in its lifecycle is taking in those first dollars from really outside money and taking in meaningful dollars. I'm a big believer that at least you call your attorney and do it right.

BEN No, that's great. We touched on this briefly. Are you seeing more often companies, CPG companies in particular, are they more often formed as LLC's or are they more often formed as C corporations or subchapter S corporations and why? What are some of the reasons why people go in one direction or another?

MATT Yeah. Well, it's a great question and one that there's a lot of information out there that sort of the pros and cons, so I would encourage any of the listeners, don't feel the need to go call your lawyer and spend all that money per hour to get their version of this, just do a Google search. There's a lot of information out there and there're some very good law firm websites that maintain startup support information.

BEN One reason I asked that is if you're a tech startup, the default scenario is you're going to be a C corporation a lot of the time. Right?

MATT Correct.

BEN Typically, formed in Delaware, etcetera. There's some more diversity when it comes to CPG companies.

MATT Yeah, and it's interesting. I think that there're some reasons for that, that are not necessarily that one entity is better for a CPG company verse the other entity. As much as it is that tech companies tend to start in a garage, to get any real traction, you have to hire on employees and take in a meaningful amount of money, so they get moving pretty quickly and scale up quickly. Then, the very common exit is to get bought by another company. They tend to do what is standard and customary in that space because that's also what the investors are familiar with and that's a Delaware C-corp. For CPG companies, because you might spend a year or two just really getting the word out about your brand in your local market and you would like an entity in place because maybe you are signing some contracts or release or getting some insurance or something like that, you will have already formed an entity and for a small entity for tax reasons, a limited liability company is more favorable to the founder, as well as the investors in a company, than is a C corporation.

MATT The reason is, is that an LLC is generally the default rule for an LLC is it's taxed like a partnership, which means that there's not a dual layer of tax. When the LLC earns money, it's deemed to be earned by the individuals, so those earning are divided up.

BEN Profits or losses pass through to the various owners of that entity.

MATT That's exactly right. Those individuals will see either a profit or a loss on their personal returns and for some of the investors who maybe they're, again, the rich uncle that's investing, they might appreciate the loss so it’s not bad.

BEN It’s a weird mentality if you kind of haven't ever been in that world, but if your investor has a bunch of money and they make a bunch of money, then they're looking for things like “hey, can I take that loss?”

MATT Right.

BEN They're actually very interested in that.

MATT Right. The result of that is, is that I just find that more CPG companies that come to us, if they've already been formed, are LLC's than say tech companies and when we're forming a company, we don't always recommend the LLC because of the tax benefits. You really have to understand what their objectives are for their company, and ultimately, what their exit strategy is because I still believe, even though LLC's are more and more common these days, and I've worked with a number of them that have been wildly successful and worked with the investors that have invested in those, it's still more common, more customary for the investors to invest in corporations. It's a little easier because there's a set of forms that everybody uses, the forms that corporate lawyers have developed for startup companies have become pretty standardized and that's good, saves money for the clients and things.

BEN They're not starting from scratch.

MATT Exactly. I can tell you there is no standardized LLC form, so it's whatever the law firm or individual lawyer that has produced it is using, so when you're then using that form and showing it to other potential investors, it's new to them and they have to spend time with it. They've got to go get their lawyer to review it, so it can be an impediment and slow down the process.

Again, for tax reasons, there is a plus because in addition to the idea that when you earn money, it's taxed directly to your return, your personal return. If you were to distribute that money, since you've already paid tax on those earnings, you can distribute those to the investors tax free. That's the real benefit there. With a corporation, once it earns money, the corporation pays tax and then if you want to distribute that money in the form of a dividend, the individual stockholder pays tax.

BEN If there's any money left over after that. Thus, the term double taxation.

MATT The term double taxation. The difference though and the reason why that's really not been an issue in the tech space is that rarely do tech companies pay dividends.

BEN They don't make money.

MATT Well, some of them do, you hope, but even if they do, they tend not to distribute the cash to the investors.

BEN They're going to reinvest it.

MATT They want to reinvest, build the business, and time it with the right exit and sell the company to a third-party. That's their big event in which they make the money. Part of the reason that I've seen CPG companies that have been very successful that are LLC's is because, just as we described way back when, when they were making that energy bar in their kitchen, they needed and entity and they did what everybody suggested, which is your small and you can avoid the double tax and it's easier, let's form an LLC. They've grown and grown, so when they've grown organically and they're now very successful and in some of the cases I'm thinking of, I've represented the investor that's made anywhere from a 20 to an 80 or 90-million-dollar investment in these LLC's and guess what? At that point the investor doesn't have the clout to tell you need to convert to a Delaware C corp.

BEN Right.

MATT You take what you've got, so you're going to invest in the LLC and structure it in a way that works. Also, you don't mind spending all the legal fees required to develop a set of terms that integrates with that company but an LLC, it's a bit more complicated than a corporation for people to wrap their minds around and one of the things that I've noticed that's an issue for entrepreneurs or founders is when you award equity to the employees. If you're doing it with an LLC, it's a bit more complex and it's also a little less familiar to the recipients of those. In the technology space, it's very customary for an employee to receive a stock option. They've been doing it for decades in Silicon Valley and I have an option to buy one share of stock at 10 bucks a share and if the company goes public at a hundred bucks, I get to spend 10 bucks and I can sell my stock for a hundred.

BEN Right.

MATT Make a pretty penny. If you award an equity interest and it's usually structured as what's called a profits interest because that's not taxable to the employee-

BEN Right. Either profits interest or a phantom equity in some way, too. Right?

MATT Correct. It's interesting you say phantom equity, that has historically not as common as it's been lately and that is because the historical method of granting an equity incentive to a service provider for an LLC, which I sometimes use partnership interchangeably, is a profits interest, but what that does is that it immediately makes that person a partner or a member. When you talked about seeing the income reflected on your personal K1, that company issues a K1 to that employee, it's not a W-2, you don't take out tax, that employee is now responsible for the employer's portion of the employee withholding.

BEN Because they are a co-owner.

MATT So, because they are a co-owner. That's something that a lot of people don't appreciate, they don't do the accounting right in the early years and it takes a bit of effort to fix it in the later years, but the reality is that if you give someone an equity interest in an LLC, then they're now a "partner" and they're treated as such. That means that they have to do estimated tax filings on a quarterly basis. That is often a lot more for a small company and then you're hiring on maybe some just relatively low paid employees, to have to change over the way they're filing their tax return is kind of a pain.

BEN That's right. Yeah, because again, there's a different way of approaching taxes. There's the I'm trying to get my income tax refund as early in the new year as I can and then there are other people who are actually filing extensions. Taxes are their own world.

MATT Yeah, that's why there's tax lawyers by the way, and lots of them.

BEN So, you might be introducing levels of complexity to people's personal tax situations that unintentionally might not help them as much as you are trying to help them.

MATT Right.

BEN I think another important point here is that as you grow, and as situations change, it is you can convert your entity from an LLC to a C corporation and at least what I've always understood from people is, it's work, but it's not insurmountable. Going in the opposite direction is terribly painful and costly.

MATT Yeah, that's exactly right. We do conversions quite often. We have a fixed fee package for a conversion from an LLC to a corporation. Because we represent so many startups and emerging growth companies, we have a variety of fixed fee packages for the basics. Things that you're going to do and there's not a lot of-

BEN Things that are replicable.

MATT Replicable, exactly. I personally find that every time I get into something, it suddenly is much different than anybody anticipated and if I do a fixed-fee deal, I'm going to lose my shirt just because it turns out it was not as we thought.

BEN It was a lot more involved than you thought.

MATT That being said, for a variety of these things, including a formation package and getting the basic corporate documents together, we have a fixed fee package for that, but the conversion, it's a few thousand dollars, there's a filing fee, of course, that you've got to pay to the state to pay to incorporate your business and then convert it. The key is that it's a non-taxable event that you can convert from an LLC to a corporation. There're some legal fees and state filing fee, but that's it. With a corporation going to an LLC, the IRS treats that as if you have sold the corporation at whatever the value is and it incurs a tax based on that value.

BEN If you're pretty big, that's going to be costly.

MATT Yeah. Big or even of any size. I mean, people love to throw out these valuations for their little bitty company. They say, "Yes, we're out raising money and we think we're worth $5 million bucks."

BEN Yeah, it's just Monopoly money.

MATT Yeah. Maybe, maybe not, but guess what? If in fact you've got an investor to bite and pay you based on $5 million, well, it will be hard for you to prove to the IRS that you're not worth five million, so you assume that for tax purposes, you don't have really much basis in the entity and its basis is zero and that's a tax term, but it means that you could have $5 million of taxable gain, which you then have to pay tax on to the IRS.

BEN Yeah, basis is the money that you put in and then there's the unrealized or whatever, realized gain on top of that, so if you put in nothing and you sold the thing for five million, then you had $5 million in gain. If you put $4 million into something and you sold it for $5 million, then you had one million in gain.

MATT Correct.

BEN Then, you wouldn't pay money because theoretically, you had already paid taxes on the thing that you put in there. Right?

MATT Right. In most instances, if you're doing that conversion, there's at least, again, some value that has to be assigned to the business and usually, that value exceeds what you've put in in the early days, so it can be painful from a tax perspective to go the other way.

BEN Yeah, you're paying capital gains tax.

MATT I can't say that I've ever seen anybody do it. They do the opposite quite frequently, but I've never known someone that finds that there's a strong enough reason or benefit to being a limited liability company rather than a corporation unless it's just very early on, they talk to their accountant, their accountant says, "You're crazy if you don't do an LLC," and then you can maybe affect a conversion without much tax exposure.

BEN Right, but even then, you might want to start over.

MATT Yeah, exactly.

BEN You're probably better off. Now, and then as you get larger, I mean, certainly this doesn't happen as often now for a variety of reasons, but should you ever get big enough that you wanted to go public, at that point you're going to be a C corporation for a number of reasons. Then, sometimes because there are restrictions around what limited partners in larger funds can or can't invest in, you will find some of the bigger funds that are writing bigger checks that want you to or, theoretically, require you to be a C corporation. I see that is becoming less rigid than it had been in the past. They can create block or entities or other things that like that allow them to invest in LLC's as well, even at scale.

MATT Yeah. I think that traditionally the word was a venture capitalist or venture capital firm will not invest in an LLC because they've got limited partners who may have tax exempt funds in there and other things.

BEN Pension funds, universities things like that, yeah.

MATT What they can't have is the flow through of profits or losses all the way up the stream to that limited partner investor. Historically, it's just been the case, you need to be a C corporation because there are no then tax gains or losses to an owner of a corporation until there's an event. Whether it's them receiving a dividend or you selling the company. As you said, it's changed a bit, relaxed a bit and I don't know if it was always available or it's just people, their mindset is a little different, because I would have thought that blocker corporations would have been available 25 years ago, but it's not uncommon where you will create special blocker entities to put between the fund that has invested in the company and that limited partner. Sometimes they're specially done for a limited partner or group of limited partners, so some limited partners have that as an issue, others don't. When you have one that does have a problem with it, you usually find a way around it without having to force the company to go through that conversion to a C corp.

BEN Right, and to your earlier point, the more a firm or an investor wants in the deal, often the more flexible they are willing to be. Right?

MATT No doubt about it. Yeah.

BEN As you have navigated your way through these waters that can be really complicated and working with CPG companies, at some point, hopefully you grow and you are attracting not just the friends and family money, but maybe some angel investors and then eventually, maybe some venture capital or even private equity money. Paint the picture for us, just because you've worked in this world a lot. I'd like you to help our listeners and viewers understand just a little bit more about what that world is. Let me give you an example.

I think for a lot of people, if their exposure is simply Shark Tank or maybe some media narrative, then the assumption is that venture capitalists are rich people, which may be the case, but it's not necessarily the case. Right? It is that they have a job and that job requires them to raise money typically from either wealthy people or entities, then, they're stock pickers. They're finding things that aren't on the market, these are early stage companies and their specialty is hopefully selecting and grooming and helping those companies grow. I guess, paint the picture for us of that world that feels foreign to so many people of like family offices and all of that stuff. How do you make sense of it if maybe you didn't grow up in the country club set?

MATT I would say that for most people, that not an area that they're terribly familiar with. Obviously, that's sort of a broad question to lay out the ecosystem of investors in both the types as well as at the different stages in which they might be interested in your company, but I think it also reminds me to suggest that people early on go find mentors and advisors. There are people, in this town in particular, in Austin, that love to help young entrepreneurs, and they don't have to be young in age, they can just be first time entrepreneurs of any age.

BEN Early in the journey.

MATT Early in the journey and there are these really wonderful mentors and programs even that are available to these startup companies and founders and things, that can help advise them. People, I think, sometimes ask too much of their lawyers. They think, in the old days, I say the old days, it ages me a bit, but I think the assumption used to be go find the right law firm and they'll introduce you to those venture capital firms. They've got the inside scoop because they do work with those firms and things like that, and it's a real kind of old boys' system and stuff.

BEN Yeah.

MATT Not as much true anymore and, by the way, there's a whole lot of lawyers out there that are purporting to do startup company work, so they may not be really familiar with the ecosystem of folks than other lawyers. Plus, depending upon the nature of it, I mean, lawyers are going to charge you by the hour.

Why pay for it if you can get it for free? I would argue that if you've found the right mentor, or the right advisor or group of advisors, you're going to get a lot more, I don't want to say value if you're not paying for it, but just a lot more useful data because these are people that have actually had to knock on the doors and have figured out. Like hey, I’ve had a lot of luck going and approaching this group of an angel network. I just sort of sent them a book and they put it through their system, and I got a call and they showed some interest or they, themselves, have connections and they say, "I'd love to introduce you to so and so. You're probably too early of a stage for them. They invest in more mature companies, but I bet you they could give you some advice on how to position your company for an investment for them at a later date and time."

BEN That's right and you want to have those conversations before you get to that point as well. Right?

MATT No doubt about it. Yeah. It really is important that you have some help navigating that system. People say, well, we're going to go out for institutional money. Well, okay, great. You go to a venture capital firm. Well, who's to say that they're actually interested in CPG companies. Maybe they only do tech companies, maybe they've just started in the CPG space. Who's to say that they're interested in investing in a company that's got sub $5 million in revenue, which for you is fantastic, you've worked your tail off to get to that point, and then from their perspective -

BEN They have a $500 million fund.

MATT Exactly.

BEN They have to write bigger checks because a million-dollar check, they can't write 500 of those.

MATT Correct.

BEN That doesn't work. They're trying to write like 20 checks, max.

MATT That's exactly right, so each of those groups of investors that you mentioned earlier, have their own, let's call it objectives or strategy in terms of how they invest and they tend to stay within a fairly narrow field of certain kinds of companies that are at a certain stage of growth and, for some of them, they have to be profitable. Then, finding the right group of investors that have the right risk tolerance for your deal, which is if you're talking early stage, it usually is high risk. Find somebody that's really fascinated with the CPG space, has money to spend, has done it before and made some really good returns on those, so they're always open and excited to help a new founder get into business and maybe they, because of their connections, can introduce you to their buddy that's a buyer over at Whole Foods or Central Market or something like that.

BEN That's right. They can be more of a value-added investor as well.

MATT Yeah. Yeah, exactly. I think that there can be great value beyond the money for from each of those groups that I mentioned, but finding the right investor, the right group of investors that have the same vision for the company that you do and that can provide something more than just their capital I think is really important to individuals. People under, I think, underestimate or undervalue the significance of that connection with your investor because if you've got an investor that's not really aligned with you in terms of your vision for the business, it may be that while they're the only ones standing there with that million dollar investment, in a year or two when you want to move in a slightly different direction or maybe you didn't have such a good year that you thought you were going to have and suddenly, they're freaked out because this is now not what they thought they had invested in and they've got some accountability to somebody higher up that beating on them to show results. You're now going to have a bad relationship with your investor.

BEN It could get really ugly, really fast.

MATT Yeah, it can.

BEN Yeah, you're exactly right. Yeah. I think that's an important, if you can find aligned investors, people who love you, who love the product, who believe in what you're doing, that's always preferable over somebody who it’s just a check to them and they don't care about any part of what you're doing or who you are. They want a return and they want it quick kind of thing.

MATT Yeah.

BEN To your point, there's this broader ecosystem and there's everything from angel investors who typically are investing. They tend to be higher net worth individuals who are investing their own money, often smaller checks, often earlier rounds. Sometimes you could have a family office in that world, depending on the scale of it. Some family offices are huge, some are more modest, and they might be involved in that kind of early to middle stage. Then, as you get larger, there are different levels of venture capital firms. There are venture capital firms, and largely you can find this stuff out, just Google it and you can see that if a venture capital firm, if they raise a fund of $25 million, then that means that they're writing smaller checks. If they raise a fund of $500 million, then they're writing bigger checks. These funds want to own typically, let's say roughly 20% to 30%, in that range, maybe more, rarely less, and maybe over time they want to gradually kind of own more and more and more if they like the bet that they've made.

You can just kind of do the math that if a VC wants to write a check, they a have a huge fund, $500 million let's say, in tech it could be a billion dollars or more, but in CPG, a big fund would be $500 million. They can only write so many of those, so they have to move a meaningful amount of capital and they have a target ownership percentage, then the implied valuation of your business is pretty good size. To your point, if you have $5 million in sales, that's excellent, congratulations, that's wonderful. That doesn't mean that you are a good candidate for getting a check from a big VC because they might need to write a $50 million and that's probably like a hundred percent or more of the value of your company at this point.

But they weren't interested in buying your company. They wanted to invest in your company. It's understanding that world and then understanding that there is, beyond that this world of the strategic acquirers or the financial acquirers and everybody's going to say they're strategic on some level, but in general that means if it's a big CPG company or some other affiliated thing there, and/or a private equity firm. Typically, and you've alluded to this before, the exit path for a lot of these more successful, not everybody makes it here, it's a very small subset of the people who start out in the race.

MATT Right.

BEN They are likely to sell, if you get to that point, you're likely to sell to either a private equity firm or a strategic in some form. Help us understand the decision-making process around those two scenarios.

MATT Yeah. There's, I guess, a key factor that people will consider is whether they think that there's a lot of future in their particular business and a lot of growth opportunity, but they'd like to see a liquidity event. They've been at it for 20 years, but they think there's still more to do and, in fact, if they can just get maybe an injection of additional capital, they can really push it.

BEN Right, and the liquidity for those who don't traffic in this world very much, is kind of a fancy way, finance and legal way, of saying that you have assets, but you can't spend those assets. You might even be wealthy on paper, but it's an exchange of cash. You get liquidity for some or all or part of your assets that had to that point been illiquid.

MATT Exactly. One option is you sell to a large CPG company and there are certain things that happen in that instance. It may be that the company that you are running is going to get completely gobbled up, they're maybe complementary to one or two other particular product lines that this large company has. If you want to work as senior manager in some division of some huge company, well then you've got an opportunity to continue to work with the company and the brand, but those strategic buyers are going to pay sometimes a greater amount for your company, so that "liquidity" event means how much you get for the stock that you've got in the company and can go off and retire.

BEN The assumption they have is that by plugging your brand into their machine, that they can create more value for their machine.

MATT Correct. Many companies, they really rely upon those small, whether it's craft beers or other types of CPG, particularly in the food and beverage base. People that develop the next brand figure out what the consumer wants. The big companies are never terribly good at that.

BEN That's not what they're good at.

MATT They look for those brands, they wait and find the right time and then make a significant investment, then the next thing you know, suddenly you see that brand, which has only been in two states or the Southwest, it's now all over the United States.

BEN Effectively, it's an outsourced R and D operation. Right? Instead of spending a hundred million dollars developing a brand from scratch, a lot of these big strategics realize they're not very good at that, so it's actually better for them to spend that hundred million dollars to buy this other company and then fold that in.

MATT I think that's exactly right. A couple of years ago Coca Cola bought Topo Chico and for those of us in Texas who see it everywhere, you wouldn't necessarily know that it wasn't very commonly available outside of Texas or in a few adjoining states.

BEN Yeah, it's like it's a Northern Mexican product that is cult phenomenon levels in Texas. Of course, you know Topo Chico, but it was foreign to most people.

MATT That's right. Coca Cola said, "Great. We think that the same thing that makes this exciting and interesting and a good play for Texas will translate to the rest of the country." For them, there's this huge upside because they're going to be paying Topo Chico based on their current market, as well as an expectation of what it can do, but then they're going to take it national or maybe global.

BEN And put it on all those red trucks and it can go anywhere.

MATT That's exactly right. On the private equity side, the key to remember is these are financial investors and they have their own investment strategy, which is to buy a company, build it, add value in some way, sometimes they may split it up to create two different companies that they think are individually worth more than what the prior company was.

BEN Sometimes they may buy several little companies and roll them up into one thing.

MATT Correct, correct. There's a whole variety of ways that they have to make money, but at the end of the day, it's all about them selling that investment at a later time to strategic or to another private equity firm. It's a pretty different trajectory for the founder who, if they're critical to the business and it's really been important to them and it's their baby and they think I've got more I want to do, well a private equity buyer just might be the perfect fit for you because they will keep the management team, assuming that they're excited about the team, which usually they are. They're not going to buy based on a product only. The team is a critical factor in their decision.

They'll keep the team in place, they'll buy the whole company, but then they'll create additional incentives for those team members, so that they can all have a piece of the pie and then make money again when that business is sold to a third party.

It's a good outcome if it's at the right price under either of those scenarios, but it can mean a quite a bit different life event for the individuals that are working for the business.

BEN That's great insight there. So, in the last few minutes we have together, I think anybody who talks with a lot of startups, you get asked the same question pretty frequently. Right? Or the same questions, and I'm sure you have your kind of standard answers to many of those things, too. What are the most common questions you get from early stage to growth stage CPG founders that maybe as an attorney you go, "Oh, yeah, I guess I haven't thought that you wouldn't have thought about it this way."

MATT Right. Well, I wish I could give you some really clever, insightful things that we haven't discussed, but the honest truth is we've touched on some of those key things. One of those things is, should I incorporate or if I am going to organize an entity, should it be a corporation or an LLC?

BEN Right.

MATT Second, it's very common that people say, "I've got somebody else. I think that they can add a lot of value. They've got some real operational experience. I had this great idea, but I don't know how to build up a company and they've already built up and sold a company. What's the best way for us to work together?" You have to guide them through that process of how to bring them on as not just an employee, but as a partner effectively.

BEN Co-founder or partner-

MATT Correct.

BEN ... what does that look like?

MATT There's a lot of information and it's a well-educated group, so people have good, specific questions. Hey, I'm raising money, should I use a convertible note or a SAFE instrument? A SAFE instrument or SAFE is-

BEN Simple Agreement for Equity.

MATT ... Simple Agreement for Future Equity, exactly. It's somewhat like a promissory note, but it's never actually payable. It will always convert into equity under some circumstance. As a practical matter, I don't see convertible notes getting paid off all that much, but they do come due and they can create some real headaches for the founder when they do.

BEN Correct. Right.

MATT They are different instruments.

BEN Yeah, in general, most of the time when you have a convertible promissory note, the assumption is this is something that if it were to fail, the investor will write off. Although, practically, you're making some assumptions there because-

MATT Well, you are.

BEN ... there's teeth to it.

MATT Absolutely. Yeah, I mean, I could tell you example after example, someone they went to their rich uncle, got that money, there's a hundred thousand dollars. The rich uncle said, "No problem. Take it. I don't need it anyway." Then, it's three years down the road and you haven't converted, you haven't had a success, and now that money's due and they're at your door every day saying, "When do I get my money?"

BEN Yeah, that's right.

MATT Suddenly, the relationship is soured. In any case, some good specific questions about what sort of fundraising instrument should I be using? They also ask a lot of questions about how to create equity incentives for employees. I want to bring somebody on, I want to create a little incentive, it's a good way to do it without paying cash, small companies can't pay heavy salaries or meaningful bonuses if at all on the bonus side, so creating of an equity incentive so they feel like they've got an ownership interest in the upside of the business and the potential success later is a good, smart way to bring on and get your employees excited.

There are some standardized processes and, by the way, more so with a corporation than an LLC, but in both instances, there are a number of decisions that you need to make. It's not just a simple answer for any scenario. It will depend upon how valuable your business is, what's the nature of the people that you're bringing on that will help decide whether you should be granting a stock option? Maybe it's early enough and you grant restricted stocks where they actually own the shares. There're some tax issues that you need to be aware of in that instance and even a filing that you need to make, to make sure that you don't get caught later with some tax that you didn't anticipate.

BEN That's right and that's the 83 B, yeah.

MATT Exactly.

BEN I get my numbers confused sometimes.

MATT The dreaded 83 B election. People all think it's due, well not all people, but some think it's due 30 days after the end of the year or when your tax return is due and the answer is it's due 30 days after you receive the stock.

BEN When you receive it. Yeah.

MATT You can't fix it later, so if you miss that 30 days, forevermore-

BEN The window closed.

MATT Yeah, the window closed.

BEN There can be tax implications for that. Every time if you're vesting, if it's on a vesting schedule, then it's as if you were granted extra compensation, but you were not practically. You didn't get any extra money, so you could have tax consequences where you're paying for something that you actually didn't get compensated with cash for which could put you in a in a tight situation.

MATT Yeah. Usually it's a surprise when that happens, when your accountant tells you that that's the case, but questions about providing compensation to employees through equity compensation is a frequent question. For contracts and things, CPG companies can operate a little bit differently than technology companies. Technology companies, to allow somebody else to use your technology, you're forced to create some sort of a licensed document or depending upon the nature of the technology, a SAAS agreement or software as a services agreement. When you engage with third parties to help, you'll have to deal with their master services agreement to provide the assistance to you. It's a little more contract intensive on the technology side than the CPG side. People for the vendors aren't going to necessarily have detailed... I mean, they'll give you the terms and conditions that are their terms and, by the way, that's what you're going to have to accept and you may not get much credit with them. You've got to pay them upfront or in a very short period of time.

Then, for the people that you're selling to, again, you're selling maybe to distributors, maybe to the direct retailer or online through Amazon or something like that. There's not a lot of contractual agreements there. There's standardized purchase order terms and things that you may have to live with. From a contractual point of view-

BEN You have some agreements, but there’s typically not a lot of wiggle room in those.

MATT Well, that's a fair point. If, for example, you're working with a vendor that's going to do all of your outsourced packaging and distribution on your behalf, called a co-packer, you're going to have an agreement, but there again, if it's early days, there's probably not a lot you can do to negotiate with them.

As you get bigger and the agreement comes up for renewal, maybe you can rethink the terms. We don't get in the CPG space for very early stage companies, quite as many questions about that, but people ask about NDA's, gee, do you have an NDA, when should I ask someone to sign an NDA? I'm going to tell somebody that is interested in making an investment in my business, should I give them an NDA to sign?

BEN A lot of times, investors just sort of roll their eyes at you.

MATT Yeah. Yeah, that's exactly right and I'll make a comment on that point because the general assumption is that no self-respecting VC signs NDA's.

BEN Which is a longstanding thing. Yeah.

MATT It's just a longstanding thing. The argument is that they look at companies in this space all the time. If they sign an NDA with you and elect not to invest in you and go and invest in another company or let's say they're invested in another company that comes out with a product that's similar to the product that you've been shown over here, for which you signed an NDA, you've just created an opportunity for that other company to sue you.

So, they're very clear, "We won't sign NDA's." That sort of the party line. The reality is they sign them all the time, so it means that if you feel very strongly about what you're going to provide, ask for an NDA and you'd be surprised whether they will sign it or not. Again, it depends upon how exciting your product is and how anxious they are to see it.

BEN Circumstances, how reasonable they are about the situation.

MATT I come back to when someone calls and says, "Gee, should we ask them to sign an NDA? I know it's not typical, but I feel very strongly about it." My question is why do you need to tell them the secret sauce today? Can't you tell them a bunch of other things first, find out what the level of interest is, maybe even get a term sheet or a letter of intent in place that demonstrates their commitment at least to spending time and effort looking at your business, and at that point maybe get an NDA in place and really show them what's important about your business.

BEN Right. No, that's good. Yeah, so I think that, again, a lot of things you've illustrated is, even at this early stage, whether you want to develop the right legal approach, the right framework, you won't have it all figured out as a founder.

Your business will evolve, you will evolve as a business person and the circumstance is nobody can predict exactly how... you might think I have a great product and maybe it just takes off like a rocket ship, maybe it takes a little while, maybe it sputters for a while and then it takes off. Maybe it doesn't go anywhere. We all have our guesses and hunches, but we don't know exactly the twists and turns and none of us can predict that, oh, in exactly 5.2 years, you will have the opportunity to sell to this private equity firm.

We're all doing our best, but, again, I think there's this idea of if you're a first-time or less-experienced founder, there are some things you can do where you begin to act like a more experienced founder. Right?

MATT Yeah.

BEN You're learning, you're studying, you're reading all the resources that are available for free online and all this kind of stuff. You're learning that you reach out to the right mentors, you're learning what questions to ask along the way, so that it gives you this framework for thinking about your business, so that you are sending all these positive signals to partners, investors, like oh, this person, this man or woman, really has their act together. Right? That only is going to open more doors for you, whether it's with retailers and partners and co-packers or if it's with investors or even some day, acquirers.

MATT Yeah. I think that that's important and that comes, by the way, just to sort of another plug for us is align yourself with a good attorney or a law firm relatively early on, find a good accountant, so when you're then talking to people and they say, "Well, what have you done in terms of corporate structure," I say, "Oh, gee, I've been working with Egan Nelson for quite a while and they've kept me on the up and up," and say, "Okay, good, that makes me feel better. That's not concern of mine that we have to at least worry about." They'll eventually do due diligence and confirm it, but at least it gives you some credibility. I'll say it, it's not really because of us, per se, it's that you've shown the initiative and discipline to go get good professional help early in the process. That makes those partners, investors, feel better about your business, that you've got your house in order.

BEN It gives them great confidence that you're taking this seriously because this is real money.

MATT Right.

BEN Right? You may be young or old or middle aged, it doesn't matter, but investors want to know, are you taking this really seriously? You have a good attorney, a good accountant, a good banking relationship, you've surrounded yourself with people who understand this space and understand what you're trying to do. You've developed that relationship early on that tees you up, that puts you in a situation where as you grow, you'll be at the ready and you can begin to reach out to these people and say, "Okay, now we have this really cool opportunity. Let's talk about that."

Rather than, "Hi, my name's Ben. We've never met each other. Let's see, where to begin?"

MATT Exactly.

BEN Right? Again, that's kind of that savvy founder who's really, for me, when I see somebody like that, I go, oh, they're really thinking differently about their company. This person, it increases your optimism for how things are going to go for them.

MATT Exactly. Yeah, I think that's a good point.

BEN That's great. Well, I just want to thank you, Matt Bair, for you've given us a lot of great nuggets to process and chew on and there's obviously so much more that we could dig into here.

MATT Sure.

BEN I mean, as across the entire legal industry, every one of these little silos we could have spent hours and hours on, but I think it's really valuable and useful for people who aren't attorneys or maybe this is a new world to them, to begin to familiarize themselves with the language and some of the decisions that they're going to need to make at various stages along the way. Again, one of our objectives here at Barcode is to begin to provide that framework for thinking about your business. Not necessarily, we're not giving people all the answers. We're just saying here are the options. Here's the menu of options in front of you, so you need to dig into this menu and figure out, oh, okay, now I understand there's not an infinite number of legal entities.

There's a set and they each come with their pluses and minuses that may apply to you and may not apply to you. You think, "Okay, what's best for me and for what we're trying to build here?"

MATT Yeah. Well, it's been a pleasure to be here. Thanks for inviting me.

BEN Absolutely. I want to just remind our viewers and listeners that you can certainly find out much more about this topic and all the other conversations that we have had and will continue to have at BarcodeStartup.com where you can find this episode in its video format, in a variety of podcasting platforms, as well as in a text-based format, so we're really providing it for you regardless of how you best process this information. We want to make it easy and available to you. Thanks again for joining us and we look forward to seeing you next time.