



# Expert Insight - Are You Investment Ready?

In our latest expert insight piece, Nathan Guest, Corporate Partner, Technology & Life Sciences (Head of Technology) at VWV, guides us through what every start-up should know about seeking investment.

## Are You Investment Ready?

Start-ups, scale-ups and the people they employ significantly drive innovation in the UK life sciences sector. Their developments in science and technology however, will not survive the journey to successful commercialisation without proper funding.

Early stage funding typically comes in two forms - grant funding and equity funding. However, grant funding often requires some level of match funding, so equity fundraising is on the critical path for the majority of start-ups and scale-ups we work with. Fundraising processes are challenging and distracting enough - heading into one without being properly prepared rarely ends well.

Here, we focus on 'investment readiness' from a legal perspective. A company seeking to raise money will also need to spend considerable time preparing a slide deck and/or business plan, financial projections and a persuasive pitch.

## Why Should a Company Consider Undertaking an 'Investment Readiness' Process?

Before a venture capital investor commits itself to a funding deal, it will generally carry out due diligence investigations to satisfy itself that there are no material issues which could impair or prevent the business plan from being fulfilled

- or which might suggest that the valuation is too high. The investor, or their lawyers, will expect management/founders to respond to a due diligence questionnaire and to provide access to specific documents that support their responses, such documents to be accessed via a data site. How extensive those questions are will depend on the nature and stage of the business as well as who is asking the questions, for instance institutional investors will typically ask many more questions than angel investors will. Key questions you should be asking yourself are: Do you own what you think you own? Are you regulatorily compliant? Who is working in the business and on what terms? Life sciences investors will be as demanding on these legal points as they are on your R&D and commercial plans, so you need to be prepared.

The due diligence process can take a lot of time which will inevitably have an impact on the founders' ability and capacity to do their day job. To limit the distraction that the investor due diligence exercise can cause, we advise that companies who are seeking to raise growth capital undertake an 'investment readiness' legal audit in advance of investor discussions so that any 'issues' can be remedied prior to investor due diligence. This is particularly important for companies seeking to raise an institutional round of investment.



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Carrying out a legal investment readiness audit will require founders/management to spend time compiling key documentation so that it is organised and in readily available form ahead of the investment negotiations and investor due diligence. This is time well spent as it will:

- give the company and its lawyers the opportunity to identify and, hopefully, rectify any issues that might otherwise weaken the company's bargaining position, including on valuation, or even cause the deal to abort and therefore saving on potential wasted costs
- give the company greater confidence that there are no 'skeletons' in the company's closet or potential investor 'deal breakers'
- mean that the company can respond quicker to the investor's own due diligence enquiries later in the process (freeing up management time to focus on the business itself and the inevitably time-consuming discussions with the investor(s) and/or their lead advisers)

#### **How to Get Investment Ready - The 'Investment Readiness' Process**

Our 'investment readiness' process involves working through a questionnaire on the legal areas that an investor will focus on and is a similar exercise to the investor due diligence process. The areas which we would typically focus on would include:

- Intellectual property - This is usually one of the most important areas for life sciences companies and one where the most complications can arise - particularly for spin-outs. If the founders were working for a university when the initial idea arose and was developed, who owns the resulting intellectual property? If it is the university, has it been validly assigned or licensed in? Who will own any improvements? How will 'know how' be addressed? Is confidential information adequately protected so that the company does not lose rights to patents and know-how? These questions are even more complex if there are academic founders who remain employed by the university but are engaged as consultants to the company. Other areas that can enhance value are applying to register the brand and securing relevant domain names.
- Contracts - If key personnel are acting under consultancy agreements, then the terms of these need to be carefully reviewed. Unless there is a written agreement that confirms otherwise, IP

developed by a consultant or contractor is very likely to be owned by them. It is imperative that the arrangements are properly documented to show that the company owns or will own the IP (although, as referenced above, there will be other considerations if the consultant is an academic).

- Post-revenue - If the company is already generating revenue, an investor will also want to know that the company's relationships with important customers are properly documented. If you already have a product or service going to market, are the terms and conditions properly protecting your rights and information?
- Employment - If the company has employees, the investor will want to see evidence that they have been properly engaged and statutory requirements have been met. Founders of life sciences companies will often have been working on an informal basis without a full employment contract, and so, pre-investment is a good time to get these arrangements on a clear documented legal footing. This also links to IP protection, as a well-drafted employment contract, which will make sure that anything created or developed by the employee during the period of the employment would belong to the company.
- Shareholdings, structure and constitution - Who owns the shares in the company? An investor will review the company's statutory books, to ensure that they are consistent with the Companies House filings, and they will also want to review the articles of association and any shareholders' agreement or investment agreement to check whether any existing investors can block a new investment. If you have set up share options or other equity incentive schemes for key employees (or wish to do so) then this should be reviewed, before implementation, to ensure they work and do not give rise to avoidable income tax charges.
- Data protection - An investor will need to be satisfied, particularly where the company deals with personal data, that the correct legal safeguards are in place as regards the use, storage and sharing of data. A life sciences company will often be dealing with medical data, which is subject to even more stringent controls, and so ensuring compliance is crucial.

- Financial promotions - There is significant UK legislation that governs how companies in the UK may lawfully raise investment, whether that investment is coming from investors based in the UK or overseas. Similarly, a company raising investment from investors based overseas should also be aware of the financial promotions legislation in that jurisdiction, before issuing a slide deck or investment prospectus (however named) to investors based in that jurisdiction. You will need to take legal advice on the steps that need to be taken to avoid or mitigate the risk of inadvertently committing a civil and criminal offence by getting this wrong.
- *National Security & Investment Act 2021 (NSIA)* - Early consideration should be given as to whether the proposed investment (and/or related transactions) is caught by the NSIA, which came fully into force in January 2022. The NSIA provides a mechanism for the UK Government (acting through BEIS) to scrutinise and, if deemed necessary, intervene if BEIS considers that the investment could harm the UK's national security. The NSIA identifies 17 sensitive areas of the economy which includes 'synthetic biology', 'artificial intelligence' and 'critical suppliers to Government,' so it is very broad in its application. The NSIA stipulates that certain investments (and other acquisitions) in these sensitive sectors will need to be notified to BEIS and cleared in advance of completion, which could have a material impact on the investment timetable. Also, the licensing of sensitive IP to a company, while not mandatorily notifiable, is often self-reported in order to immunise the deal from subsequent review (BEIS has up to five years to review a completed transaction). Sometimes, however, this triggers an intervention (the July 2022 order blocking the University of Manchester from licensing vision-sensing technology to a Chinese company reportedly arose in response to a voluntary notification). There are also civil and criminal sanctions for failure to comply with this legislation.

### **What Can VWV Offer Your Start-Up?**

When it comes to raising capital, being 'investment ready' can make a huge difference to the ease at which the investment proceeds, the time the deal will take to conclude and will provide founders with the best protection against the investor chipping away at the valuation.

At VWV we have a team of specialist lawyers dedicated to supporting start-ups, spin-outs and other emerging technology and life sciences companies that are created to develop and commercialise innovative technologies and scientific developments. If you would like to discuss what legal investment readiness might mean for you, please contact Nathan Guest.

### **Nathan Guest - Corporate Partner, Technology & Life Sciences (Head of Technology) - VWV**

Nathan is a Corporate Lawyer with more than 20 years' experience of advising clients on private equity, venture capital, M&A and management buy out transactions. Although he acts for UK and international corporates and some institutional investors, the vast majority of his and his team's clients are technology and life sciences start-ups (including university 'spin-outs'), scale-ups and other high-growth technology and life sciences companies. Nathan has co-founded and led several 'lawyer-in-residence' programmes for UK tech and life sciences incubators and has sat on numerous advisory boards during his career. Nathan leads a team of c.50 specialist lawyers who focus on helping these emerging tech and life sciences clients to navigate the many potential legal pitfalls and impediments to scaling their business. In particular, Nathan has considerable experience of advising clients on angel and institutional venture capital fundraising deals, including corporate venturing deals, and in preparing for them. Having a significant network of contacts, Nathan is also happy to provide assistance with introducing clients and contacts to other businesses, professional advisers and key contacts who may be able to help them - whether in connection with an actual or potential transaction or ongoing commercial matters.

**For more information, please contact Nathan Guest on 0117 314 5289 or at [nguest@vww.co.uk](mailto:nguest@vww.co.uk)**