

Podcast title: Adventures in Entrepreneurship Law

Episode: What kind of contracts do startups need?

Podcast guest: Jaakko Lindgren, Partner, Dottir Attorneys at Law.

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Transcription notes:

N1: Narrator 1

N2: Narrator 2

Host 1: Kalle Airo

Host 2: Petra Hietanen-Kunwald

Episode guest: Jaakko Lindgren

Other information about the text:

[text] = a sound or not transcribed parts are written with square brackets e.g. [laughs] or [interview paused due to a phone call]

[recording starts]

N1: Aalto university podcast.

[Intro music]

N2: In the adventures in entrepreneurship law podcast series. Petra Hietanen-Kunwald, and Kalle Airo from Aalto university, explore business law from an entrepreneurial point-of-view with expert guests. In some episodes, their co-host is Moritz Scherleitner. The podcast content is meant for education, and is not intended to constitute legal advice.

What kind of contracts do start-ups need? Commercial contracts in a nutshell. Our guest is Jaakko Lindgren. Partner, Dottir attorneys at law. Entrepreneurship law with Petra and Kalle. Many start-ups have an unclear idea about contracts. And how to use them. In this episode Petra and Kalle discuss with Jaakko Lindgren, what start-ups should look for in commercial contracts. They will also talk about the difference between a contract and a memorandum of understanding. The magic of reading. And the significance of written contracts. We also learn what terms should be avoided to stay out of trouble. And how important it is to understand what you own.

Kalle Airo: So entrepreneurs have two kinds of products. First of all, the product that the company is selling to customers. And then the company itself. And you need contracts for both of these products. Today we will concentrate on the commercial contracts that you typically do with the product that you are actually selling. And we are discussing this with Jaakko Lindgren. So welcome to the show.

Petra Hietanen-Kunwald: Welcome.

Kalle: Okay so Jaakko, you are relatively well-known for most Finnish people who follow the start-up scene. But who are you?

Jaakko Lindgren: I am an attorney. And I am one of the founders of the Dottir law firm. I am practicing law in Finland. I have a background in the big law firms. And big listed IT firms. And also in the start-up scene. I have been, in some way, involved in the start-up scene for more than ten years. Like early days of the Aalto start-up movement and so on. I know quite well Finnish start-up scene. And everything what has happened in the Otaniemi. This is my background shortly.

Kalle: So why is entrepreneurship important to you?

Jaakko: It is a good story. I started my career in the big law firm. Then I worked many years in the big listed firm in Finland. Then my friends started to found different kind of start-ups. But I worked those days in the big law firm, and I think that those guys could have so cool firms, and the firms are cool, I must do something myself. And then I found a couple of crazy lawyers in different law firms, and then we found together Dottir almost seven years ago. It is like one of the biggest things in my life. Like a good story in my personal life and working life. I like it. Because you are so many hours in the office, and you must like what you do. And if you have your own firm, it's part of you and you like it. I guess this is the reason. And this is some kind of a justification for my career.

Petra: We are talking today about commercial agreements, how start-ups can sell their products. So first of all, what is a commercial agreement? What is an agreement?

Jaakko: How I say it in an easy way. It is a binding legal document. It could be oral, but it's not very good. Because in Finland, and maybe in some other countries also, agreements could be oral ones, a couple of guys talking about it. But my first advice in every single firm is that they need all agreements in written form. Then you can read those agreements, and check which are the obligations. And what are the rights of the parties in the agreement? And a commercial agreement is a base of every single company. They can buy and sell products and services. When they do some buying or selling, they need an agreement in a written form.

Kalle: Okay so you mentioned written contracts. And oral contracts. Are there other ways how you can actually enter into this binding agreement?

Jaakko: I guess it is good to make a difference between negotiation phase and then agreement phase. You must understand always which type of contract is binding, and which is not. And if you have some kind of memorandum of understanding, or later of intent, or some other contract. Or some kind of pilot contract or something like that, you must always focus on which terms are binding and which are not. When you draft the contract, when you negotiate the contract. And after negotiation and signing, you must understand which clauses in the agreement are binding. And binding meaning that you must fulfill those requirements in those clauses in the future. And you must fulfill those clauses in some time frame, one year, or maybe ten years, or signs that you terminate the whole contract. This is the big issue. And we have a quite strong culture in Finland that we trust each other. It's a very good thing. But at the same time you must be in the difference between binding contract, and only some kind of trust between parties. If you have those clauses in binding

form in your contract, then you can trust that you can fulfill those clauses, or other party will fulfill those clauses. And it is a part of the how you build your own firm. In the starting phase, you have a lot of this kind of pilot agreements or memorandums of understanding. And phase by phase, in the end you have more like a binding agreements and the real business. And in the starting phase, you have this kind of testing or piloting agreement, and so on.

Petra: Maybe we can come back to this terminology. So we have a letter of understanding, memorandum of understanding, letter of intent, binding agreements. So how do I know, as an entrepreneur... First of all, you could tell the difference between those two. And then tell us how entrepreneurs know whether this is a memorandum of understanding, not binding. Or if this is already an agreement that is binding. How do they know?

Jaakko: I guess that in the real life, every single founder must understand... To read is the first phase. To read the agreement. If you read the agreement, then you understand is this agreement binding or not binding. Or which part of this agreement is binding and not. Because in Finland, in a practical life, I have seen letter of intent, which is fully binding agreement. Then I have seen memorandum of understanding, which is full binding. Then I see quite often letter of intent, or memorandum of understanding which are not binding. They are only some kind of speech of parties.

Petra: So you can not on the basis of the title of the agreement, you cannot conclude whether this is binding or not?

Jaakko: Yes.

Petra: So if you only want to have a general memorandum, it would be wise for instance to write there that this is not yet binding. But we will later on agree on the binding terms. Something like this. Just to make it clear.

Jaakko: Yes.

Petra: This is very important to understand. And on the other way around, there can be agreements that are so vague, that you don't have an agreement, even though you think there is an agreement.

Jaakko: Yes. But I guess that the good starting point in start-up firms, that they will read the agreements. They don't sign agreements without reading. I guess that this is the some kind of very key topic, because I have seen so many firms, which have a lot of agreements, but they don't have a real understanding of those, what kind of agreements they have. Because when they are young firms, and big corporations call them for example, they will sign everything without thinking. Because they think this could be a good thing for the whole firm. But they don't have the full picture, what kind of agreement they sign. And I guess that this reading is one very important point.

Kalle: So basically you are saying that you should have one person, who actually reads contracts and understands the big picture, how the contracts are linked to each other.

Jaakko: Yes. I have seen many kind of start-up teams. We have very good teams, and then we have very good technical teams, which are not very good commercial-wise. But some kind of key issue, that every single start-up team must have one person in team, with focusing boring, legal stuff. And boring administrative stuff. This person must read agreements, and understand agreements. And also the same person must have an archive system of all agreements. For example typical start-up needs venture money. And before you can get the venture money, you need a DD phase. And you must show and disclose all the agreements. And if you have a very good guy in the team in the early days of the firm, then your administration looks very good at very early stages. And it is good in the starting point of the firm.

Kalle: So what kind of commercial agreements do start-ups typically have? And are there some kind of commercial agreements that they don't have but they should have?

Jaakko: This is interesting question. I guess you must follow the money. Because if you follow where they use the money, and where the money comes. There you find the agreements. And typical start-ups have different agreements relating what kind of service they need, space they need, like rent or something. And then agreements relating their employees or if they rent some employees, or using this kind of services. Of course those are important, but the most important, you must focus in your firm. When you have a product or service, you have very good agreement how you sell your service or product. And you need those kind of agreements in the right place. That you understand how you're gonna make money with your service or product. And you need an agreement in commercial-wise very early days. Like the typical, if I look at the Otaniemi area nowadays. Of course there are different kind of firms, but quite typical in Otaniemi firms are, they are product firms relating to the cloud computing or AI or something like that. Those firms need terms of service, or frame agreement, or something like that, with their clients. I guess those are the main points. But if I look at the new firm, and try to figure out what kind of agreements they have, then I follow the money. I check that which are the money flows. There you can find the agreements. Or if you don't, then you have a problem.

Kalle: So basically you need to own what you are selling. And have a contract that lets you actually invoice what you are selling.

Jaakko: Yes. This is true.

Petra: That is very good advice. How does it work when you buy services? Because sometimes you need to buy services. Or have a cooperation with others.

Jaakko: Yes. I guess that in the early phase, every single firm needs to buy some services. But you must buy services in a way that you can terminate quite easily those services. You couldn't take ten years rent agreement. You couldn't take ten years IT service agreement. Because you don't know what will happen in the next year. And when you are focusing in buying some services in a start-up, you must have the capabilities and right to terminate those agreements. Because in the start-up world, you couldn't understand what will happen

next year or the year after that. Because typical, those firms in the early days, they develop with a very fast growth.

Petra: Everything can change then.

Jaakko: Yes, very rapidly.

Petra: Agreements, they are often very long, they can also be very short. What are the most important terms that you always should have in agreements?

Jaakko: I guess that the common understanding between the parties. They must have an understanding on what is the focus and what is the scope of agreement. This is the first thing. Both parties in the agreement must understand the scope of the agreement in the same way. Then, timetable, or delivery table, or using time. This is second important thing. Then pricing. Both parties understand the same way the pricing. If parties have similar understanding of scope of agreement, time table and pricing, then you have quite a good situation. Then when we focus in the start-ups, terminations. Because typical human being thinks that it's very cool to sign the agreements. And then take a class of champagne or something like that. We are happy that we signed the agreement. But in the lawyer, the most important thing is understand of life cycle of agreement. How you can terminate the agreement. Because if you don't have a clear termination clauses, then some day you have a total mess in your table with your agreement.

Petra: What about liability clauses?

Jaakko: Of course, they are important. But I guess that the lawyer focusing a lot of time and effort in liability clauses. But in real life, of course liability clause could be a problem. But in 95 percent of the litigation and arbitration regarding commercial agreements, they are focusing on different terms than liability in their agreement. Because typical parties have different understanding end result of the agreement. And then liability or arbitration start. But of course, there are also other important clauses. But in the start-up firm level, you must have a focusing that you understand those scope timetable and pricing very clearly. And after that, you can consult the lawyer, or something like that. And the lawyer can put the boilerplate stuff in your agreement.

Petra: So before signing an agreement, what should an entrepreneur look for?

Jaakko: I guess that if the basics are in good shape, like scope, time table, pricing and so on. Then the founder must focus on two clauses. Exclusivity. No exclusivity clauses in commercial agreements in start-ups. Because if you try to develop bigger firm and grow. Then if you have an exclusivity clause that you can make a business, for example in Finland only with the one pulp and paper company. You couldn't develop a lot your business, if you have this kind of exclusivity clause. This is one topic. Of course in some cases, if you have an exclusivity clause with the only one year, or in one factory, or something like that. If there are some limitations. Then you could have exclusivity clauses in the agreement.

Petra: Question from the audience. What is an exclusivity clause?

Jaakko: In a simple way, you could make a business only with this partner. If you are in the software firm, and you make an agreement with one pulp and paper firm. Then you can make software business only with this firm. And if you are a product company, and make exclusivity agreement with the one manufacturing firm, then you can use only one manufacturing firm. And it could destroy your firm's value. Because investors, they look in the growing firms, but if you have an agreement... Say that this firm can make business only with this one firm, then you have a problem.

Kalle: And you might actually run, or it used to run in this kind of problems, where a start-up would make, let's say in the German market there would be some that I want exclusive rights to sell your product. And there is no minimum price. And they just don't do anything. They get you out of the German markets by you signing the exclusivity.

Jaakko: Yes. And it is a problem. A second important thing is termination. You must always understand when we can terminate this agreement. And when other party can terminate the agreement. You must always think what is the life cycle of this agreement. You could be happy in signing agreement nowadays, when most of the signing agreement is in DocuSign, but ten years ago it's always written signing. And it was a big thing in many firms. People focusing in the signing agreements. But clever founder focusing also on the life cycle of the agreement.

Kalle: So how can and should an entrepreneur manage risk with agreements?

Jaakko: I guess that, I have seen so many years in the start-up in Finland. My first advice, read the agreements. You must understand what you sign. It is the first thing. Second thing, no oral agreements, only written form agreements. This might sound stupid because we trust each other in Finland. But in the business life, and when you build the firm, you must have written agreements with your sub-contractors, employees, manufacturing, and so on. Written agreements. And then, one person in team who is focusing in agreements very early days. Then use the legal services when you need it. Also in the early days. Or have one founder who has some legal background. But again, it's not maybe clever because lawyer founder maybe have so much to do in the very early days, because a company has a very limited number of agreements in the early days. But maybe you can think that you use some legal services or have one founder in your team which has some understanding of the legal stuff. Those are the high level ways to manage the agreements risks.

Kalle: So what kind of terms should you avoid in commercial agreements?

Jaakko: Of course there are many of them. But if I look at the typical problems in Finland and start-up scene in general in the Nordics. IPR rights. You must have a clear understanding after signing agreement, who owns the IPR rights. For example typical case in the start-up world, you have a product firm, and then you use the sub-contractor. Which is coding something in your product. Then lawyer looks at the agreement. And the ownership of IPR rights is unclear. Then we have a problem. Because in Finland, and in Otaniemi, and also in the Nordics, many firms are software firms nowadays. And there the most valuable thing is IPR rights of the product. And if you have a problem in your core, for example if you couldn't

understand who owns IPR rights of your product, then we have a huge problem in the future. I guess that focusing IPR clauses in the agreement, both parties must have similar understanding who owns the IPR rights after this agreement.

Kalle: Thank you for sharing your insights and advice so far. But what are the key takeaways you want the viewers to remember out of this discussion?

Jaakko: I guess that every firm must focus in their service or product. Service and product are most important thing in the firm. Because if they have good product or service, then they have good clients also. And then firm is successful. Commercial agreements is not rocket science. But you need one person in your team, who is focusing on agreements.

Kalle: Thank you.

Petra: Thanks a lot. It was very interesting.

[recording ends]