MATRIX SOLICITORS

DECELERATING YOUR STARTUP

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The Tech industry is booming! New startups are born everyday and funding deals are announced with signature pictorials of founders and team members clad in t-shirts emblazoned with the name of the startup and jeans. But as with all businesses, tech startups also fail; even the ones that have raised millions of dollars; an example is Protonn, an American startup, which shut down less than a year after it had raised $9 Million in seed funding.[1] According to the 2020 Better Africa Report authored by GreenTec Capital Africa Foundation and Wee Tracker, the average failure rate for African startups was 54.2 percent, while Nigeria had a startup failure rate of 61%. [2]

With failure on the table as a possibility, founders must have this at the back of their minds when they are negotiating investment agreements; and take as much care in managing risk and relationships in decelerating as they do in starting up or accelerating. It is possible to fail and still tidy up the business without being scathed, but this is only achievable if the startup has the right advisors to midwife the deceleration process. To sound a note of warning, hiring competent advisors at the deceleration stage will probably not redress prior significant management missteps or poor record keeping – so, it is prudent to manage the business right (perhaps with the help of qualified third-parties) every step of the way.

Depending on the urgency of the situation, deceleration may need to happen overnight, though this is not ideal as the state of the startup's health should be constantly monitored or over a period of time during which the shutting down process can be phased; whatever the circumstance, the following should be done.

1. **Dispassionately assess the situation**. Many times, because founders are so invested in the business, it is near impossible to assess the situation dispassionately, even with hard evidence in full view; as such, it is better to speak to someone (including professionals and in certain cases, investors) that is not only neutral but understands your startup, the industry and the situation of your business. If the conclusion is reached that the business cannot profitably continue, then it's time to shut things down, responsibly.

2. **Assess assets, receivables, financial liabilities and exposure**. If the startup has a strong finance/valuation team, this exercise can be done inhouse, otherwise, hire an external professional/team. At the end of this exercise, the founders should know every single asset, including licenses and intangible assets, that they own and their value, the quantum of their receivables (if any) as well as their financial liabilities.

3. **Assess the legal options and risk**. Every single relationship and agreement tied to the startup must be thoroughly reviewed and exit options explored. Competent legal advisors should be able to advise on the best exit strategy for each agreement and foretell to a reasonable extent, the litigation/dispute resolution risks that attend each exit option.

4. **Talk to your investors**. Founders must carry their investors along in both the up and down times. Where the reason for shutting down is lack of funds to advance the startup's business, investors may be willing to provide further funding. However, when shutting down becomes inevitable, founders must have a full

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[1] https://inc42.com/buzz/protonn-shuts-down-less-than-a-year-after-9-mn-seed-funding/ (accessed 9th March 2022)

[2] https://greentec-foundation.org/report/better-africa-report/ (accessed 9th March 2022)

picture of the situation and present it in clear and simple terms to investors. Founders must be able to demonstrate that they have explored all reasonable options before reaching the conclusion that the business cannot profitably continue. If the founders have negotiated a bad investment agreement, this is where things may go sideways, quickly. In all, a savvy investor that has lost money in a failed start-up is likely to invest with the same founder in future, if the founder has managed the business, as a going concern, and the shutting down process well. Also note, that even in shutting down, there are sale options – consider those options and present them to your investors so that a joint decision can be made.

5. **Talk to your employees**. The employees of a startup are probably the most important stakeholders because without talent, you cannot build a viable tech business. Founders should let employees know on time, if possible, give additional notice beyond what is stipulated in their contracts to ensure that they have enough time to plan their future. Terminate contracts appropriately and make necessary payments (e.g. redundancy pay); the last thing any founder wants is having labour-related litigation post shut down.

6. **Determine what can and needs to be sold**. During deceleration, there will be physical, digital and intellectual property to be sold. The sale and transfer of all assets must be properly documented, and the appropriate authorities should be notified, where applicable.

7. **Decide what to do with the business**. If the business is being acquired by a third-party, the acquisition must be properly structured and documented. If the business is being shutdown completely, the entity should be wound-up in compliance with Nigerian law and the tax and other regulatory authorities should be notified of the dissolution of the entity.

8. **Notify your regulators and industry partners**. Apart from the Corporate Affairs Commission and the Federal and state tax authorities, startups that are in highly regulated industries, such as the banking and finance industries, must notify financial regulators that they are closing shop. For startups that are in highly interconnected industries, it is important to notify industry partners that are connected to the startup of its closure.

9. **Notify your customers**. Customers should be notified and long running contracts, terminated in compliance with agreed terms. Where refunds are due, they should be made promptly.

Deceleration can be quite difficult for founders who are emotionally and financially invested in their business, but it is easier to decelerate before the business degenerates into bankruptcy, especially when third-parties have invested in the business.

Should you have further questions, please contact:

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