STARTUPS IN THE UK
STARTING AND SCALING UP

In part one of a two-part series, Jamie Moore, Kristy Hart, Nicola Whiteley, Anna Humphrey, Faraaz Samadi, Natasha Ahmed and Kelly Hagedorn of Orrick explain the key issues and complexities that UK startups must navigate.

Setting up and scaling a company can be an exhilarating yet arduous journey. Individual entrepreneurs and business founders who want to commercialise their latest idea must navigate the complexities of launching and growing a successful company. Challenges will inevitably arise at each stage of a startup's lifecycle but, in many cases, laying the right foundations at the start can help to smooth the way for the later stages of growth.

This feature article, the first in a two-part series, explores what founders need to think about in the early stages of growth. From setting up a private limited company to safeguarding intellectual property (IP), key areas such as building and incentivising teams, and the complexities of data protection and key compliance matters.

Part two of the series will focus on the next phase of growth and explore the key issues surrounding raising finance, cybersecurity considerations, how to steer a company through financial difficulties, comply with directors' duties and more.

SETTING UP A PRIVATE LIMITED COMPANY

Incorporating a startup can be a complex and stressful process. Unfortunately, errors are relatively common and can lead to future problems when they are discovered as part of the due diligence on a later funding round or an exit. There are several key issues that founders should consider when incorporating a private limited company, to ensure that the startup is well set up and ready to hit the ground running.

Co-founder equity split

One of the most common reasons why business ventures fail is due to disagreements between the founders regarding the split of the equity. Incorporating a startup early can form the basis of these discussions and allow the founders to address these problems head on to ensure that they are aligned on equity split from the beginning. Many co-founders look to have these discussions in the context of putting in place a founder agreement; however, it is worth noting that the founder agreement will be superseded by the shareholders' agreement on the first priced round and is therefore often not time well spent at incorporation.

Adopt articles of association

All registered companies must adopt articles of association, unless they opt for

© 2023 Thomson Reuters (Professional) UK Limited. This article first appeared in the August 2023 issue of PLC Magazine.

the model articles under the Companies Act 2006 (2006 Act) to apply. The articles of association will contain provisions concerning decision making, the rights attaching to a share class, and how directors exercise their powers. Although model articles are sufficient for an early-stage company, it is important to consider whether incorporating the startup with a set of articles that deviate from model articles can better ensure that the business has a strong constitutional foundation.

For example, when a startup is in its early stages, it may not have the financial backing to fully remunerate its employees with high salaries. By incorporating and including provisions in the articles of the company in relation to share options, it is possible to reward employees with the promise of a greater stake in the future growth of the company (*see "Incentivising the team" below*).

Directors and persons with significant control

A private limited company must have at least one director who is a living individual, over the age of 16, although additional corporate directors are permitted (*section 155(1), 2006 Act*). Keeping the board of directors lean at the outset can help the business to remain agile and make decisions quickly to match the fast-paced growth and development of a startup and also leave room for the board of directors to grow as new investors come onboard.

A person with significant control (PSC) is a person that either holds more than 25% of the issued shares, 25% of the voting rights, or the power to remove the majority of the board of directors from the company, or otherwise has the right to exercise significant influence on a company's decision making. A company is obliged to identify any PSCs when incorporating the startup (*section 12A, 2006 Act*) and keep and maintain a register of PSCs throughout its lifecycle (*Part 21A and Schedule 1A, 2006 Act*).

Where the company being incorporated is a wholly owned subsidiary of a foreign parent entity, such as a UK subsidiary of a US parent company, there are additional requirements to determine the ultimate PSC which will need to be considered.

Allot subscriber shares

Subscriber shares are the shares that are issued and allotted to the initial subscribers of a newly incorporated company. If the company is to have a share capital, it must issue and allot at least one share to each of its subscribers. In order to retain some flexibility as a startup grows and takes on new investment, and to avoid having to sub-divide the shares in the near future, it can be helpful to incorporate the company with more shares of a smaller nominal value, such as 1,000 ordinary shares of £0.001 or even 100,000 ordinary shares of £0.00001.

Companies House matters

It is a common misconception that registering a company name at Companies House will protect that name under trade mark law and stop others from using it. In fact, trade marks in the UK are administered by the Intellectual Property Office (IPO) and must be filed for separately (*see "Protecting the ideas" below*). The company's trading name and the legally registered company name may be different. On incorporation, it is good practice to check the Companies House name availability checker and the IPO trademark database.

Most Companies House filings are now made electronically, which means that there is no longer a requirement to submit paper filings. Incorporating the company, making most filings relating to share capital (for allotments, sub-divisions and re-classification of shares), notifying a PSC, and filing the annual confirmation statements can all be done through the Companies House portal (*www.gov.uk/guidance/filing-your-companies-house-information-online*).

Companies House has also introduced a service that allows businesses to upload documents online that previously required paper filing, such as the articles of association and shareholders' written resolutions. It is a legal requirement to file any special resolutions passed by shareholders, but that is often missed (*section 29, 2006 Act*). It is recommended that founders should take the approach of filing all shareholders' written resolutions unless there is a particular sensitive reason not to file an ordinary resolution.

Update and maintain company registers

It is important to prepare and maintain statutory company registers. In a financing round or on an exit, these are the first documents that advisers will ask for. Every UK incorporated private limited company is required to maintain certain statutory company registers, either at its registered office, at a single alternative inspection location (SAIL) address or at Companies House. The registers, otherwise known as the statutory books, comprise the:

- Register of members.
- Register of directors.
- Register of directors' usual residential addresses.
- Register of secretaries.
- Register of PSCs.

BUILDING THE TEAM

When setting up and growing a company, one of the first priorities is hiring the first employees and building the core team; making good choices at this stage is a prerequisite for long-term strategic growth. There are also numerous practical processes to set up in order to be an employer (*see box "Practical considerations for a new business"*).

Correctly classify the staff

In the UK, there are three employment status categories: employee, worker and self-employed consultant. The category that a person fits into depends on specific facts and circumstances rather than how the parties decide to document the relationship (*Uber BV and others v Aslam and others [2021] UKSC 5; see News brief "The Supreme Court and Uber: taxi for the gig economy?", www.practicallaw.com/w-030-2571*). The relevant facts include the amount of control that the company has over the individual, whether the individual is free to work or provide services to others, whether the individual has a right of substitution, and whether the individual is obliged to accept work and the company is obliged to provide it.

This is significant because it will affect the staff member's access to certain legal rights such as paid holiday, sick pay, payment of minimum wage, protection from termination and controls on working time. There are also differences in tax treatment and if an individual is incorrectly classified as a consultant when they are, in reality, an employee or worker, then the company may be liable for income tax (PAYE) and

© 2023 Thomson Reuters (Professional) UK Limited. This article first appeared in the August 2023 issue of PLC Magazine.

Practical considerations for a new business

In practice, the first steps in setting up a workforce are to:

- Set up a UK bank account from which to pay salaries or other benefits to the workforce.
- Deduct employment taxes at source. It is not necessary to operate a payroll in-house; external payroll providers can be instructed to operate the payroll.
- Register with HM Revenue & Customs to ensure that employment and other taxes are paid (*www.gov.uk/register-employer*).

As UK employees are subject to the protection of the retained EU law version of the General Data Protection Regulation (*679/2016/EU*) and the Data Protection Act 2018, it is likely that an employer will process data in relation to those individuals (*see "Compliance matters" in the main text*). As such, a startup business will need to register with the Information Commissioner's Office (ICO) and pay a registration fee, unless it is exempt. The ICO website has a registration self-assessment tool to determine whether a new business needs to pay a data protection fee to the ICO, and if so, the ability to register with the ICO online (*https://ico.org.uk/for-organisations/data-protection-fee/self-assessment/*).

All employers in the UK are also required to obtain employers' liability insurance. This insurance protects the company in respect of liability to its employees for injuries or illness.

National Insurance contributions (NICs) in respect of that employee, including interest and a potential fine (*see feature article "Off-payroll working: under an umbrella?", www.practicallaw.com/w-035-2317*).

Statutory particulars of employment must be provided to employees on or before their start date; these are usually provided in the form of a more detailed employment contract. All employees, including founders, should be asked to sign employment contracts or service agreements at the earliest opportunity, to ensure that the company is adequately protected.

Insured benefits and pensions

The insured benefits that may typically be provided to a senior employee are:

- Health and dental insurance.
- Life assurance.
- Permanent health insurance and long-term disability insurance.

If benefits are not set up at the outset, appropriate wording can still be included in any employment agreements that will allow for them to be put in place in the future without creating any obligation on the company. This will ensure that the protective conditions for the company are in place regardless.

Automatic enrolment legislation set out in the Pensions Act 2008 requires that a business must enrol qualifying employees in a qualifying workplace pension scheme automatically (*see feature article "Pensions auto-enrolment: issues in practice", www.practicallaw.com/2-527-5427*). The requirement can be postponed for up to three months from the employee's start date.

Employee entitlements and rights

Employees in the UK:

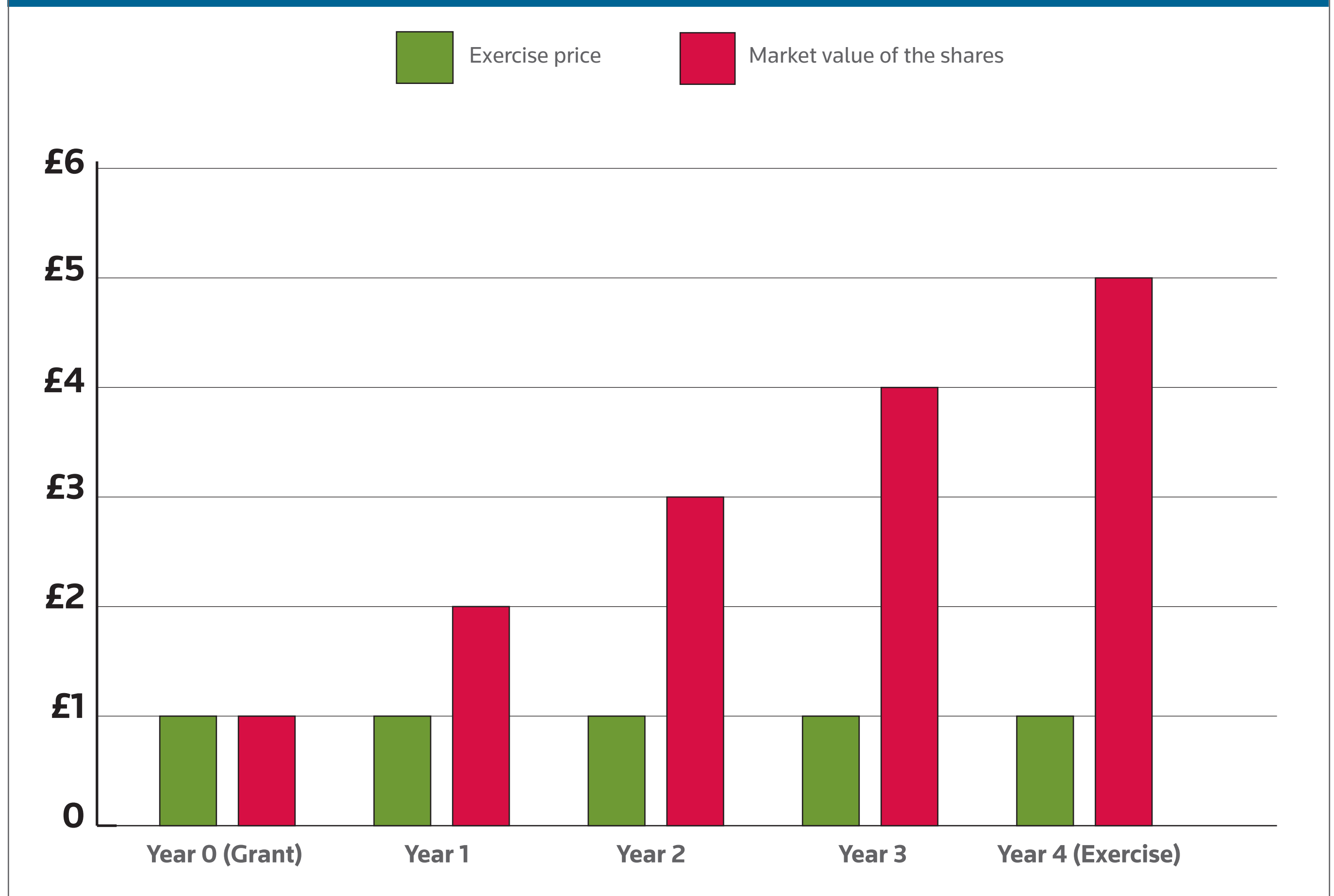
- Are entitled to a minimum of 5.6 weeks (28 days) of holiday each year, which can include public holidays (*regulations 13 and 13A, Working Time Regulations 1998 (SI 1998/1833)*) (WTR).
- Must be paid at least the minimum wage. Different rates apply to different age groups and the rates are updated annually (*National Minimum Wage Act 1998*).
- Are not permitted to work more than an average of 48 hours per week and are entitled to minimum rest breaks, which an employer must monitor or an employee must opt out of (*regulations 4, 10, 11 and 12, WTR*).
- Automatically have certain key rights for which there is no minimum service requirement and which therefore are essential for founders to be aware of. Two examples of these are:

  - employees are protected from discrimination on the basis of the nine protected characteristics during recruitment and throughout employment. The protected characteristics are age, disability, gender reassignment, marriage and civil partnership, pregnancy and maternity, race, religion or belief, sex and sexual orientation (*section 4, Equality Act 2010*); and
  - employees are protected from being dismissed or suffering detriment if they blow the whistle; for example, if they disclose any breach of a legal obligation or health and safety obligation on the employer's part (*Employment Rights Act 1996*) (ERA).

After two years' service, employees will then also accrue unfair dismissal rights (*section 108(1), ERA*). An employee can bring an unfair dismissal claim if their dismissal does not fall under one of the five fair reasons; that is, capability or qualifications, conduct, redundancy, breach of a statutory duty or restriction, or some other substantial reason (*section 98, ERA*). An employee can also bring an unfair dismissal claim if the employer failed to follow the prescribed steps in relation to the dismissal and the employer cannot show that they have acted reasonably.

Co-founders and first employees

There is a temptation for co-founders to put in place founder agreements to govern their relationship and what happens to those all-important founder shares if a co-founder were to leave the company. However, these agreements are often replaced by the full shareholders' agreement and articles of association put in place during the first priced round of financing. Putting a founder agreement in place might therefore not be worth the time and costs required.



In the current competitive market for talent, equity also becomes an important question in respect of the first employees of a new business (*see "Incentivising the team" below*). A valuable employee may require a stake in the business as well as their employment rights.

Protecting IP and confidential information

It is best practice to have written agreements in place for founders and employees that, among other things, make specific provision for the transfer of IP from them to the company and to protect the company's confidential information. Under English law, there is a presumption of ownership on the creation of IP from employees to their employers, but this is not the case for contractors and freelancers. A company's IP is often its most valuable asset, and investors will be very interested in these provisions (*see "Protecting the ideas" below*).

An employee is also subject to an implied duty of confidentiality during their employment, but including express provisions in their service or employment agreement can also help to ensure that all relevant confidential information is protected and that this protection continues after their employment has ended.

Post-termination restrictions

The service or employment agreement should include post-termination restrictions, also known as restrictive covenants, which help to protect the business and its confidential information for a defined period after their relationship with the company has ended. Investors will generally expect these to be in place for founders. These can encompass, for example, non-compete, non-solicitation of employees and business, and non-dealing restrictions. Without these restrictions, the founder or employee would be free to set up business in competition with the company or recruit the company's employees immediately after leaving employment.

However, in order to be enforceable, these restrictions must be carefully drafted and tailored to an individual's position and be no more restrictive than is necessary to protect the company's legitimate business interests (*see feature article "Employee restrictive covenants: enforcement, challenge and trends", www.practicallaw.com/w-024-8474*). If post-termination restrictions are not included from the outset, it can be more difficult to introduce them at a later date and separate consideration would need to be given to the individual in order for the covenants to be enforceable.

INCENTIVISING THE TEAM

Most early-stage companies are not in a position to compete with the salaries that are offered by large corporates to attract and retain employees. By providing an opportunity to benefit in any increase in the company's valuation through share option grants, options can play a crucial role in offering attractive compensation packages and aligning the interests of employees and shareholders.

Shares or options

A share option is a contractual right, not an obligation, to purchase a company's shares, subject to certain conditions and

© 2023 Thomson Reuters (Professional) UK Limited. This article first appeared in the August 2023 issue of PLC Magazine.

at a pre-determined price, known as the exercise price or strike price. Unlike the issue and allotment of shares, on the grant of an option, an optionholder does not become a shareholder in the company. The optionholder only becomes a shareholder if they choose to exercise their options. Where shares are issued to an employee, they suffer an upfront tax charge if the price that they pay to purchase the shares (if anything) is not at least the market value of the shares at that time, whereas an option is not taxed at the time of grant; instead the tax charge crystallises in the future.

Given that the optionholder is allowed to exercise their option only in certain circumstances and is not obliged to purchase the underlying shares, share options are a very flexible incentive (*see box "Potential gain on exercise of options"*).

Who to grant options to

Options are generally granted to employees and executive directors but can also be granted to non-executive directors, consultants, advisers, employers of record employees, and third parties contracting through personal service companies, subject to relevant local laws and the type of share option scheme chosen (*see below*).

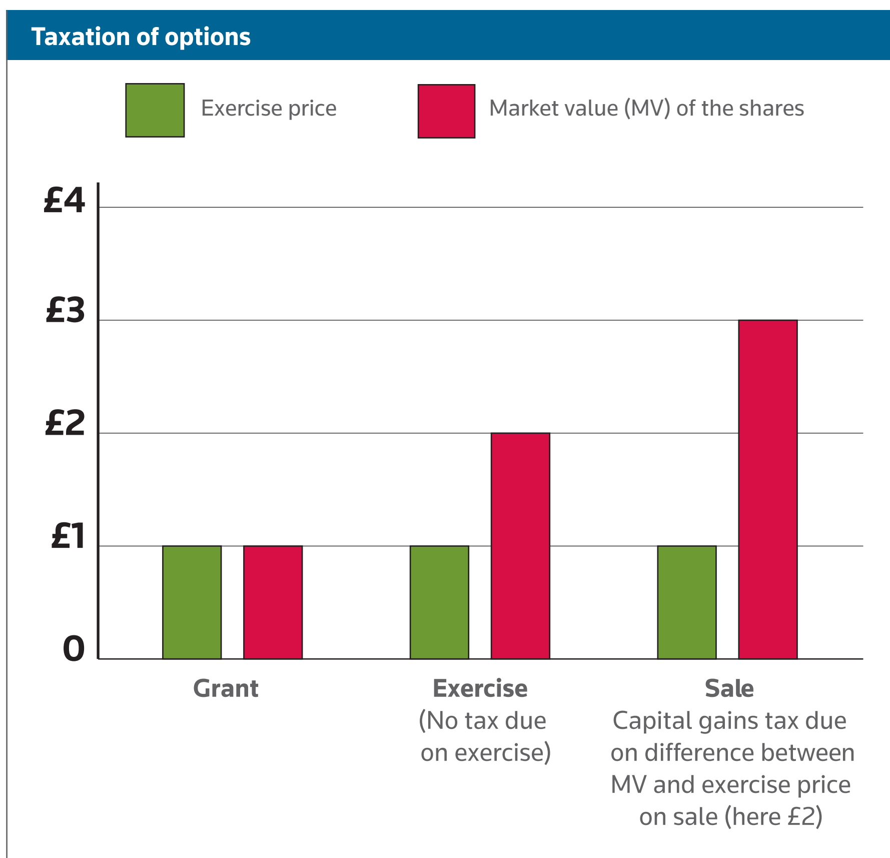
In the UK it is increasingly common to grant options to all employees of venture-backed businesses, not just the executives. Founders will need to think carefully about who will be able to benefit from the share option scheme; for example, to make the most of the scheme, the business should avoid granting options to ex-employees. The scheme should also be fair, and the grants awarded according to objective and transparent criteria.

Enterprise Management Incentive options

Enterprise Management Incentive (EMI) options are a tax-efficient and flexible way to grant options, provided that certain detailed requirements are met as to:

- The company granting the options.
- The employees being granted the options.
- The terms of the options.
- The shares under option.

Taxation of options



Eligible employees may be granted EMI options up to the value of £250,000. The company must, among other requirements, be independent, carry on a qualifying trade, not have gross assets exceeding £30 million (the gross assets test), and have fewer than 250 full-time equivalent employees. It is common for later-stage startups to breach the gross assets test once they have gone through further rounds of funding due to investment monies being reflected on their balance sheets. Founders need to keep an eye on this as their business grows.

HM Revenue & Customs (HMRC) must also be notified of EMI option grants within 92 days, and evidence of this retained by the company, and an EMI annual return must be submitted yearly (*see Briefing "EMI options: are problems remediable?", www.practicallaw.com/w-038-9590*).

Company share option plans

Company share option plans (CSOPs) are a tax-advantaged share option plan which a startup business might use if the company does not meet the EMI requirements. It is common for startups at later stages to make use of CSOPs. Eligible employees may hold up to £60,000 of unexercised CSOP options, which was increased from £30,000 in April 2023 (*see News brief "Company Share Option Plans: getting a facelift?", www.practicallaw.com/w-037-3496*).

However, as with EMI options, certain conditions need to be met. For example, the company must be independent, and options must be granted with an exercise price that is equal to the market value of the shares on the date of grant.

Non-tax advantaged schemes

These types of option plans are much more flexible than CSOPs or EMI, allowing founders to grant non-tax favoured share options in circumstances where the company is unable to satisfy the requirements for a CSOP or an EMI scheme. These plans are potentially easier to implement and operate than tax-advantaged schemes but do not provide the same generous taxation benefits. It is very common for startups to use non-tax advantaged options for their non-executives, advisers and consultants, as EMI and CSOP options can only be granted to employees.

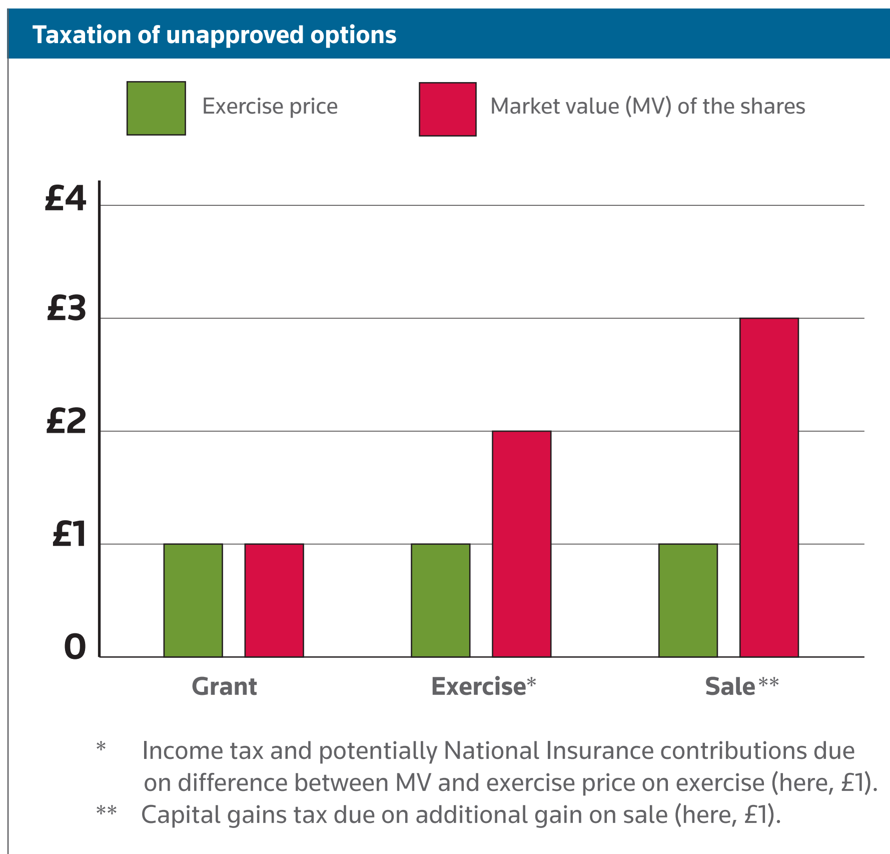
Consider the tax implications

Firstly, if all requirements continue to be met, employees are taxed on EMI and CSOP options at the point of sale of the shares that are received on exercise of the option. This is in contrast to employees who have

© 2023 Thomson Reuters (Professional) UK Limited. This article first appeared in the August 2023 issue of PLC Magazine.

been granted non-tax advantaged options, who are taxed both at the point of exercise of the option and at the point of sale of the shares.

Secondly, optionholders who sell shares that were acquired on the exercise of EMI and CSOP options are subject to capital gains tax on gains made on the shares (currently at 20% for higher and additional rate taxpayers, but gains on shares acquired on the exercise of EMI options held for at least two years can qualify for business asset disposal relief (BADR) without needing to meet certain of the usual BADR requirements, which can reduce the rate to 10% on the first £1 million of lifetime gains), whereas optionholders holding non-tax advantaged options are subject to income tax and potentially NICs on any difference between the exercise price and the value of the shares at the point of exercise, and capital gains tax on any gain made on the shares at the point of sale of the shares. Given the company's potential PAYE obligations to account to HMRC for any income tax and NICs, appropriate indemnities should be included in the share option scheme to ensure that the company can recover these liabilities from the optionholder (*see boxes "Taxation of options" and "Taxation of unapproved options"*).



Vesting schedules

A vesting schedule provides that an optionholder earns options over an increasing number of shares either:

- At set times, known as time-based vesting.
- On the satisfaction of certain performance conditions, known as performance-based vesting.

The greater the number of options that are vested, the greater the number of shares the employee would be entitled to if the employee was able to exercise the option and receive shares, if the option was exercisable.

The vesting schedule assists with employee retention as it rewards optionholders to remain with a company. Without a vesting schedule, an optionholder would be entitled to all their options at the point of grant. It is market standard in the UK and US for venture-backed startups to apply time-based vesting over a four-year period, where no options vest during the first year (known as the cliff), and thereafter linear vesting occurs monthly over the next three years. However, some companies opt for back-loaded vesting schedules.

Even though an option is vested, it also needs to be exercisable before the employee can exercise the option and receive the shares. While it is common for share option schemes to provide for options to be exercisable as they vest, some share option schemes provide for options to be exercisable only on an exit event, which is typically defined as an initial public offering, a sale, or a liquidation event such as a funding round or secondary sale. These are known as exit-only share schemes.

Good and bad leavers

Leaver provisions govern what happens to an optionholder's options when they leave a company, in particular through good and bad leaver definitions and how vested and unvested options are treated for each type of leaver.

UK market practice is leaning towards a good leaver being anyone who leaves other than for cause, such as gross misconduct or fraud, which follows the US market position. A bad leaver's unvested and vested options will generally lapse; that is, the right to purchase shares is extinguished. Good leavers are typically allowed to exercise any options that are already vested within a certain time period (usually 90 days), and their unvested options lapse.

Change of control

On a change of control, such as the sale of a company, optionholders might be permitted to exercise their vested options immediately before the transaction so that the shares may be sold to the potential buyer or, depending on the transaction structure, swap their options in the target company for options in the buyer company, known as an option rollover.

Companies may also accelerate vesting in connection with a change of control, so that an optionholder's previously unvested options will vest and become exercisable.

Documentation

A share plan sets out the overarching terms and conditions under which the share options are granted. An option agreement is then entered into for each grant and records the number of shares subject to the option and the exercise price. This set-up allows for the terms of the option grants to be personalised.

© 2023 Thomson Reuters (Professional) UK Limited. This article first appeared in the August 2023 issue of PLC Magazine.

Where EMI or CSOP options are being granted, startups should obtain a valuation for the shares that will be under option, which can be agreed with HMRC.

PROTECTING THE IDEAS

Beyond its people, a company's IP is often its most valuable asset, especially for companies in the technology sector. Ensuring that the startup owns the rights in its IP and is taking the appropriate steps to protect its IP rights is crucial.

Ownership of the work product

While the general position under English law is that IP rights created by an employee in the course of their employment automatically vest in the company, putting in place a written, standalone IP assignment agreement increases clarity and lowers the risk of future disputes around IP ownership (*see "Protecting IP and confidential information" above*).

The general rule applying to employees does not apply to third-party contractors and freelancers. IP that is created by third parties will belong to those third parties unless it is properly assigned to the company under a written agreement. A startup should therefore enter into a contractor agreement that contains appropriate IP assignment provisions with any third-party contractors that the company engages to develop its IP.

To the extent that any IP was created for the company before their entry into such contract, an IP assignment agreement should be considered to ensure that any such IP is also formally assigned to the company.

Record keeping

It is important to keep records of drawings and drafts that provide evidence of the development of the business's IP. These records should ideally be signed, dated and marked confidential. If a dispute ever arose and the company needed to enforce its rights against someone using the same or similar IP, these records could be useful in resolving the dispute. If the startup wants to register its registrable IP, comprehensive records are also helpful when preparing the IP registration application.

Trade marks

Trade marks or brands are the signs used by companies to distinguish their goods or services, such as names, logos, slogans and designs. This branding can be protected by trade mark registration in the UK and can be renewed indefinitely in ten-year increments. Registering trade marks grants a company monopoly rights over them in the territories in which they are registered for the goods and services covered by the registration, provided that such trade marks are actively used.

Registering trade marks also makes it easier to take enforcement action against third parties that attempt to copy or use marks that are very similar to a startup's trade marks. A trade mark can be licensed or assigned by its owner and is therefore a valuable commercial asset. Although a company might still be able to bring claims in respect of unregistered trade mark rights, this relies on the common law doctrine of passing off, and can be a long, difficult and, potentially, expensive process.

Copyright

Software, among other creative works, may be protected by copyright. Unlike registered trade mark rights, in the UK copyright protection arises automatically when a qualifying work is first created. Copyright protection gives the owner the right to prevent others from copying and unjustifiably profiting from an original work for a term of up to 70 years from the death of its author. It may be possible to use the copyright work of others under licence, but it is important to understand the terms of the relevant licence.

Some licences provide that if a user combines open source software (OSS) with proprietary (closed source) software to create a new product, the user is then compelled to distribute that new product on the same terms, usually for free. So, it is vital that a startup business understands the licence terms of any OSS that it uses.

International IP protection

If a startup is trading abroad or intending to do so in the future, it will want to consider obtaining IP protection in those jurisdictions. This will help to protect its IP as the business continues to expand globally and will be something investors will be keeping a keen eye on.

Using non-disclosure agreements

Non-disclosure agreements (NDAs) are contracts that impose contractual confidentiality obligations on the parties to ensure that the information exchanged between them remains confidential (*see feature article "Drafting confidentiality agreements: the DNA of an NDA", www.practicallaw.com/9-536-5387*). Using NDAs

Other company policies

Although the following policies are not legally required, it can be useful for the company to implement them and they can provide protection for the company in key areas. Most companies choose to introduce the following as a minimum as they grow:

- Equal opportunities policy.
- Family leave policies, particularly where the company offers enhanced pay for family leave.
- Whistleblowing policy, if this is not mandatory for the sector in which the startup operates.
- Flexible or remote working policy.
- IT and communications policy.
- Anti-corruption and bribery policy.
- Modern slavery statement.
- Environmental, social and governance policy.

© 2023 Thomson Reuters (Professional) UK Limited. This article first appeared in the August 2023 issue of PLC Magazine.

can be an effective way to protect against a company's confidential information, including IP, such as trade secrets and proprietary source code, from being leaked or shared with competitors.

NDAs can be used at various stages of a company's growth, including with third parties to which the startup gives access to new products and designs in the research and development stage of product development. NDAs can also be put in place before in-depth discussions commence with potential customers and suppliers and with potential investors during fundraising.

Protect IP in contracts

Contracts with customers and suppliers should contain provisions that relate to IP ownership and appropriately scoped licences.

Customers. Robust provisions are required in contracts with customers that make use of IP owned by the business so that the business can retain control and ownership over its IP. The terms should clearly set out the extent of the licence that is granted to the customer, including whether it is exclusive or non-exclusive, royalty-free or subject to payment of a royalty fee, sub-licensable, transferable, or limited in time or geographically.

Suppliers. If a startup uses the IP of another company, this should be formalised through a written licence or an IP assignment. The unauthorised use of IP rights of a third party may risk infringement action by the third-party owner against a startup.

COMPLIANCE MATTERS

While focusing on many of the key operational aspects in the early stages of growing a startup, it can be easy to forget the importance of compliance. Two core areas where compliance is increasingly important from the outset are data protection and employment.

Data mapping

From the very beginning, it is important to consider whether the startup will be collecting any personal data. This will help to determine the extent of the business's data protection obligations. For example, if the company is data-driven and intends to collect large amounts of personal data or particularly sensitive data, the extent of the privacy compliance obligations and liability exposure will be greater than if the use of personal data is confined to holding only employee personal data. Conducting a data mapping exercise will therefore set the right foundation for a good compliance programme and help the founders to understand their legal obligations and the risks that the business faces.

Legal basis for processing

The retained EU law version of the General Data Protection Regulation (*679/2016/EU*) (UK GDPR) requires companies to have a valid legal basis for any processing of personal data. There are six available legal bases:

- Obtaining the individual's consent.
- Complying with a legal obligation.
- Performing a contract.
- Protecting the vital interests of an individual.
- For a public task.

Related information

This article is at practicallaw.com/w-040-1311

Other links from uk.practicallaw.com/

Topics	
Company formation and constitution	topic/2-103-1146
Compliance: data protection	topic/1-616-6178
Confidentiality	topic/7-103-1304
CSOP/SAYE/SIPs	topic/6-319-0952
Directors	topic/7-200-0622
EMI options	topic/9-318-9952
Employee data and monitoring	topic/5-200-0623
Share capital: structure, allotment and transfers	topic/9-103-1157

Practice notes	
Allotment and issue of shares	5-422-4150
Auto-enrolment: overview	4-500-1097
Contracts: business and trade name FAQs	w-016-2750
Copyright: subsistence	9-583-8805
CSOPs, EMI, SAYE options, and SIPs: a comparison	2-205-7140
Data mapping and GDPR recordkeeping obligations	w-037-6224
Data retention policies (UK)	w-014-7851
EMI share option plans: overview	7-578-1466
Employment status (1): employee, worker or self-employed?	6-200-4244
Intellectual property issues relating to employees and consultants (UK)	5-200-2151
Legal protection of software	7-202-4703
Protecting confidential information: overview	8-384-4456
PSC register: identifying people with significant control	9-624-0527

Previous articles	
Off-payroll working: under an umbrella? (2022)	w-035-2317
Employee inventor compensation: a multi-jurisdictional perspective (2022)	w-035-2039
Employee restrictive covenants: enforcement, challenge and trends (2020)	w-024-8474
Acquihire deals: buying technology in the 21st century (2018)	w-015-5729
Employee share plans: the lie of the land (2017)	w-009-5578
Pensions auto-enrolment: issues in practice (2013)	2-527-5427
Drafting confidentiality agreements: the DNA of an NDA (2012)	9-536-5387

For subscription enquiries to Practical Law web materials please call +44 0345 600 9355

© 2023 Thomson Reuters (Professional) UK Limited. This article first appeared in the August 2023 issue of PLC Magazine.

- For the legitimate interests of an organisation.

For a company to legally process any personal data, it must have established which legal basis it intends to rely on before collecting that personal data. Each legal basis has different requirements that must be satisfied, therefore, this analysis should be factored in at the start before processing any personal data.

Website privacy and cookies

The UK GDPR requires companies to provide certain information to individuals whenever they collect and process personal data. This is typically done by way of a privacy notice. Where the startup has created a website that collects personal data from site users, a UK GDPR-compliant privacy notice must be displayed on its website.

Where a company website uses cookies, the general rule is that it must inform users that cookies are being used, explain what the cookies are doing and why, and obtain the user's consent to store a cookie on their device. The best way to achieve this is through having a compliant cookie policy and implementing a means by which individuals can consent to the use of cookies when they visit the website.

Generally, the first place that a regulator or individual will look for information about a company's privacy practices are the disclosures on the company website. The external-facing privacy notices should therefore be prioritised in the early stages of a startup's privacy compliance journey as they are likely to be subjected to a higher level of scrutiny.

Internal privacy compliance

Companies that process personal data are required to implement and maintain certain privacy compliance documents, policies and procedures. For example, companies must have a record of processing activities in place that details the company's processing of personal data. If the startup has employees, an employee privacy notice will also be required. The extent of the privacy compliance documents, policies and procedures will largely depend on the nature and scope of the startup's business operations; there is no "one-size-fits-all", so it is important for founders to seek advice early to understand what the compliance roadmap will look like.

International data transfers

There are strict rules governing the transfer of personal data internationally. If the startup idea involves personal data being transferred outside of the UK to a country that is not deemed to have an equivalent level of data protection, the company will need to implement additional safeguards, such as standard contractual clauses and any necessary supplementary security measures, such as encryption, access controls etc.

At the time of writing, the following are viewed as providing adequate data protection from a UK perspective: the EEA, Gibraltar, Andorra, Argentina, Faroe Islands, Guernsey, Isle of Man, Israel, Jersey, New Zealand, South Korea, Switzerland and Uruguay, and partially as regards Canada and Japan. As part of the data-mapping process, founders need to consider how and where data will be moved to in order to determine whether the data will need safeguarding.

Employee handbook and company policies

There are a handful of mandatory employment policies that should be adopted at the relevant stage.

Disciplinary and grievance procedures. The company should seek to align its disciplinary and grievance procedures with those set out by Acas (*www.acas.org.uk/templates-for-employers*). If a claim, such as one for unfair dismissal, is successfully brought against the company in an employment tribunal, a failure to comply with the steps set out by Acas can result in an uplift of 25% of any award that is made. Disciplinary and grievance procedures should be marked non-contractual and sit separately from the employment contract.

Health and safety policy. Companies with five or more employees are required to have in place a written health and safety policy.

Whistleblowing policy. Certain regulated and listed companies are required to have a whistleblowing policy.

While not mandatory, certain additional policies can be beneficial for the company as they ensure that both the employer and employees are clear about what is expected of them. Putting these in place also helps to maintain consistency across the business and manage legal risk (*see box "Other company policies"*).

Depending on the business of the company and its size, further policies can also be introduced. These policies can be collated in an employee handbook, and can include a sickness and absence policy, holiday policy and expense policy. Company policies should explicitly state that they are non-contractual in order to give the startup more flexibility to amend and update them as the business grows.

General compliance

There are a number of other key employment-related compliance issues that a startup should keep in mind to ensure that employee matters are being managed in a compliant manner, including the following:

- Ensure that all employees have the right to work in the UK.
- Provide all employees with a written statement of the main terms and conditions of employment before employment begins.
- Automatically enrol eligible employees into a qualifying pension scheme and make the minimum employer and employee contributions.
- Comply with the rest breaks, holiday entitlements and maximum weekly working time limit set out in the WTR and, if necessary, keep adequate records in relation to the same.
- Pay employees the national living or minimum wage for all of their working time.
- Consider any sector-specific regulatory compliance issues in respect of their employees.

Jamie Moore, Nicola Whiteley, Anna Humphrey, Faraaz Samadi, Natasha Ahmed and Kelly Hagedorn are partners, and Kristy Hart is an associate, at Orrick.

This article is based on Orrick's Founder Series, which is available at www.orrick.com/en/Insights/Orricks-Founder-Series.

© 2023 Thomson Reuters (Professional) UK Limited. This article first appeared in the August 2023 issue of PLC Magazine.