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Investor Issues for Later Stage Investments

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Deal Trends

- Continued emphasis on experienced founders/management teams that can execute in a rapidly changing market.
- Valuations decreasing in all sectors, especially for later stage companies with limited revenue traction.
- Recapitalization transactions will increase as later stage companies are forced to restructure.

Deal Trends

- Increased interest in international deals and founding teams with international backgrounds and experience
- Down rounds are common and early stage investors are more likely to negotiate existing venture terms in later rounds of financing
- Imposing Pay to Play provisions is very common

Deal Trends

- Redemption rights are increasingly common
- Cumulative dividends are increasingly common

Current Deal Terms

- Liquidation Preferences Frequently 2x in later rounds
 - 3x is less common later rounds still tend to track existing preferences with pari passu treatment in many cases although this is changing as need for cash gives new investors greater leverage
 - Priority for later rounds increasingly common

Current Deal Terms

- Participation
 - Only relevant in a trade sale
 - Frequently Fully-Participating
 - 3x cap on participation is often negotiated, caps are less common in the current market
 - Preferred Stock is always fully convertible

Current Deal Terms

- Anti-Dilution Protection
 - Increased incidence of down-rounds
 - Broadly-based Weighted Average formula has become standard
 - More emphasis on Anti-Dilution and obtaining waivers in the negotiation process for down round

Current Deal Terms

- Control Rights
 - Board Seats reserved to Preferred Stock
 - Board Seat reserved for the CEO, not Common Stock
 - Veto rights, particularly series votes, are important for later stage investors where insiders have a majority of the shares

Current Deal Terms

- Control Rights
 - Can create specific Board approval rights for later round Board representative for next round or sale event

Current Deal Terms

- Veto Rights
 - Major Question is Class v. Series Veto
 - Typical Vetos include:
 - Alteration of Preferred Rights
 - Change in authorized Preferred Shares
 - Authorization of a senior or pari passu series
 - Redemption of stock
 - Asset sales or acquisitions
 - Dissolution, liquidation or bankruptcy

Current Deal Terms

- Drag Along Rights
 - What percentage of shares can force a drag-along?
 - Requires individual contractual obligations of shareholders'
 - What conditions (e.g. valuation) apply to the right?
 - Difficulty of valuation is often an issue.

Current Deal Terms

- Drag Along Rights
 - Drag-Along Rights are now market; can create carve out based upon deal size to protect minority investors

Current Deal Terms

- Other Terms
 - Increased use of shareholder approvals for management decisions and operational issues.
 - Valuation adjustments increasingly common for later stage companies with unrealistic revenue projections.