



Trends in Terms of Venture Financings In Silicon Valley (Fourth Quarter 2010)

Background – We analyzed the terms of venture financings for 95 companies headquartered in Silicon Valley that reported raising money in the fourth quarter of 2010.

Overview of Fenwick & West Results

- Up rounds exceeded down rounds in 4Q10 67% to 21%, with 12% of rounds flat. That represented a significant increase in the percentage of up rounds versus down rounds from 3Q10, when up rounds exceeded down rounds 52% to 30%, with 18% of rounds flat. This was the sixth quarter in a row in which up rounds exceeded down rounds.
- The Fenwick & West Venture Capital Barometer showed an average price increase of 61% in 4Q10, up sharply from 28% in 3Q10. This was also the sixth quarter in a row in which the Barometer was positive.
- The results by industry are set forth below. In general, the software industry had the best valuation related-results in 4Q10, followed by the cleantech, hardware and internet/digital media industries, while the lifescience industry trailed.

Overview of Other Industry Data

Third party reports on the venture industry generally reported an improving venture investment and liquidity environment in 4Q10 and 2010 overall, but the environment for venture fund capital-raising continues to be difficult. Detailed results are as follows:

- **Venture Capital Investment.** Venture capitalists invested \$7.6 billion in 735 deals in the U.S. in 4Q10, a 38% increase in dollar terms from the \$5.5 billion invested in 662 deals in 3Q10, according to Dow Jones VentureSource (“VentureSource”). For all of 2010, VentureSource reported that a total of \$26.2 billion was invested in 2,799 deals, an 11% increase over dollars invested in 2009, when \$23.6 billion was invested in 2,636 deals.

The PwC/NVCA MoneyTree™ Report based on data from Thomson Reuters (the “MoneyTree™ Report”) also reported increases in venture investment, indicating that venture capital investment in the U.S. in 4Q10 increased 2%, compared to 3Q10, and 19% increase in 2010 compared to 2009.

Venture capital investment growth was driven by investments in the internet/digital media industry, and to a lesser extent the cleantech industry, while the life science and hardware industries lagged.

- **Merger and acquisition activity.** Acquisitions of U.S. venture-backed companies in 4Q10 totaled \$10.5 billion in 109 transactions, an 84% increase in dollar terms from the \$5.7 billion paid in 102 acquisitions in 3Q10, according to VentureSource. For all of 2010, VentureSource reported \$33.9

billion paid in 445 transactions, a 63% increase in dollar terms from 2009, when \$20.8 billion was paid in 381 transactions.

Similarly, the MoneyTree™ Report reported a 54% increase in the number of M&A transactions (420 in 2010 vs. 273 in 2009) and a slight increase in the average deal size.

- Initial Public Offerings. VentureSource reported 14 venture-backed IPOs in 4Q10, raising \$1.1 billion, compared to nine IPOs raising \$0.7 billion in 3Q09. For all of 2010, VentureSource reported 46 venture-backed IPOs raising \$3.4 billion, a close to six-fold increase in the number of deals from the eight venture-backed IPOs raising \$0.9 billion in 2009.

Similarly, the MoneyTree™ Report also reported a six-fold increase in the number of venture-backed IPOs in 2010, from 12 in 2009 to 72 in 2010, but noted that over half of the 32 IPOs in 4Q10 were China-based companies with U.S. venture investment.

- Venture capital fundraising. Fundraising by U.S. venture capital funds fell to \$11.6 billion in 119 funds in 2010, a 14% drop from the \$13.5 billion raised by 133 funds in 2009, according to VentureSource.

Similarly, the MoneyTree™ Report reported that venture funds raised \$12.3 billion in 2010.

Both VentureSource and MoneyTree™ Report reported the amount raised by venture capital funds was the lowest amount raised since 2003.

- Observation. As was mentioned in our 3Q10 report, venture capital funds continue to invest substantially more funds than the amount of new capital commitments they receive, a situation which is not sustainable over a prolonged period.
- Sentiment. The Silicon Valley Venture Capital Confidence Index produced by Professor Mark Cannice at the University of San Francisco reported that the confidence level of Silicon Valley venture capitalists was 3.75 on a 5 point scale, a very modest increase from the prior quarter's reading of 3.7.
- Nasdaq. Nasdaq increased 12% in 4Q10, and has increased 6% in 1Q11 through February 17, 2011.

Detailed Fenwick & West Results

Financing Round – The financings broke down according to the following rounds:

Series	Q4'10	Q3'10	Q2'10	Q1'10	Q4'09	Q3'09	Q2'09	Q1'09
A	13%	20%	18%	24%	23%	17%	8%	13%
B	26%	23%	22%	21%	22%	31%	27%	28%
C	35%	28%	28%	30%	21%	19%	35%	17%
D	14%	9%	20%	11%	17%	16%	13%	20%
E and higher	12%	20%	12%	14%	17%	17%	17%	22%

Price Change – The direction of price changes for companies receiving financing this quarter, compared to their previous round, were as follows:

Price Change	Q4'10	Q3'10	Q2'10	Q1'10	Q4'09	Q3'09	Q2'09	Q1'09
Down	21%	30%	27%	32%	30%	36%	46%	46%
Flat	12%	18%	18%	19%	23%	23%	22%	29%
Up	67%	52%	55%	49%	47%	41%	32%	25%

The percentage of down rounds by series were as follows:

Series	Q4'10	Q3'10	Q2'10	Q1'10	Q4'09	Q3'09	Q2'09	Q1'09
B	12%	20%	14%	23%	24%	19%	16%	38%
C	27%	33%	29%	45%	25%	45%	51%	50%
D	23%	30%	36%	18%	47%	56%	67%	39%
E and higher	17%	38%	33%	27%	26%	39%	67%	60%

The Fenwick & West Venture Capital Barometer™ (Magnitude of Price Change) –Set forth below is (i) for up rounds, the average per share percentage increase over the previous round, (ii) for down rounds, the average per share percentage decrease over the previous round, and (iii) the overall average per share percentage change from the previous round for all rounds taken together. Such information is broken down by series for 4Q10 and is provided on an aggregate basis for comparison purposes for the prior four quarters. In calculating the “net result” for all rounds, “flat rounds” are included. For purposes of these calculations, all financings are considered equal, and accordingly the results are not weighted for the amount raised in a financing.

Percent Change	Series B	Series C	Series D	Series E and higher	Combined total for all Series for Q4'10	Combined total for all Series for Q3'10	Combined total for all Series for Q2'10	Combined total for all Series for Q1'10	Combined total for all Series for Q4'09
Up rounds	+103%	+114%	+100%	+67%	+104%	+81%	+86%	+78%	+73%
Down rounds	-61%	-38%	-40%	-56%	-45%	-47%	-65%	-54%	-50%
Net result	+67%	+73%	+53%	+24%	+61%	+28%	+30%	+21%	+19%

Results by Industry for Price Changes and Fenwick & West Venture Capital Barometer™ – The table below sets forth the direction of price changes and Barometer results for companies receiving financing in 4Q10, compared to their previous round, by industry group. Companies receiving Series A financings are excluded as they have no previous rounds to compare.

Industry	Number of Financings	Up Rounds	Down Rounds	Flat Rounds	Barometer
Software	30	90%	7%	3%	+121%
Hardware	14	57%	36%	7%	+38%
Lifescience	14	36%	36%	28%	-5%
Internet/Digital Media	16	56%	25%	19%	+20%
Cleantech	7	72%	14%	14%	+73%
Other	2	100%	0%	0%	+74%
Total - All Industries	83	67%	21%	12%	+61%

Please note that some industries have small sample sizes that reduce the statistical validity of the results.

Liquidation Preference – Senior liquidation preferences were used in the following percentages of financings:

Q4'10	Q3'10	Q2'10	Q1'10	Q4'09	Q3'09	Q2'09	Q1'09
28%	41%	40%	38%	41%	49%	41%	45%

The percentage of senior liquidation preference by series was as follows:

Series	Q4'10	Q3'10	Q2'10	Q1'10	Q4'09	Q3'09	Q2'09	Q1'09
B	12%	32%	32%	23%	24%	38%	17%	35%
C	27%	27%	34%	42%	50%	40%	52%	38%
D	46%	60%	48%	36%	58%	63%	50%	56%
E and higher	42%	62%	53%	53%	37%	67%	53%	55%

Multiple Liquidation Preferences - The percentage of senior liquidation preferences that were multiple preferences were as follows:

Q4'10	Q3'10	Q2'10	Q1'10	Q4'09	Q3'09	Q2'09	Q1'09
13%	20%	17%	23%	19%	21%	24%	28%

Of the senior liquidation preferences that included a multiple preference, the ranges of the multiples broke down as follows:

Range of multiples	Q4'10	Q3'10	Q2'10	Q1'10	Q4'09	Q3'09	Q2'09	Q1'09
>1x – 2x	100%	85%	71%	86%	57%	89%	75%	80%
>2x – 3x	0%	0%	29%	14%	43%	11%	25%	10%
>3x	0%	15%	0%	0%	0%	0%	0%	10%

Participation in Liquidation – The percentages of financings that provided for participation were as follows:

Q4'10	Q3'10	Q2'10	Q1'10	Q4'09	Q3'09	Q2'09	Q1'09
45%	53%	35%	48%	51%	53%	49%	51%

Of the financings that had participation, the percentages that were not capped were as follows:

Q4'10	Q3'10	Q2'10	Q1'10	Q4'09	Q3'09	Q2'09	Q1'09
40%	58%	61%	54%	54%	60%	67%	60%

Cumulative Dividends – Cumulative dividends were provided for in the following percentages of financings:

Q4'10	Q3'10	Q2'10	Q1'10	Q4'09	Q3'09	Q2'09	Q1'09
5%	7%	7%	7%	4%	7%	2%	10%

Antidilution Provisions – The uses of antidilution provisions in the financings were as follows:

Type of Provision	Q4'10	Q3'10	Q2'10	Q1'10	Q4'09	Q3'09	Q2'09	Q1'09
Ratchet	3%	4%	4%	5%	6%	3%	3%	3%
Weighted Average	95%	93%	94%	94%	94%	96%	97%	97%
None	2%	3%	2%	1%	0%	1%	0%	0%

Pay-to-Play Provisions – The use of pay-to-play provisions in the financings was as follows:

Percentages of financings having pay-to-play provisions.

Q4'10	Q3'10	Q2'10	Q1'10	Q4'09	Q3'09	Q2'09	Q1'09
7%	15%	16%	7%	10%	15%	15%	14%

Note that anecdotal evidence indicates that companies are increasingly using contractual “pull up” provisions instead of charter based “pay to play” provisions. These two types of provisions have similar economic effect but are implemented differently. The above information includes some, but likely not all, pull up provisions, and accordingly may understate the use of these provisions.

The pay-to-play provisions provided for conversion of non-participating investors’ preferred stock into common stock or shadow preferred stock, in the percentages set forth below:

- Common Stock.

Q4'10	Q3'10	Q2'10	Q1'10	Q4'09	Q3'09	Q2'09	Q1'09
100%	81%	100%	86%	80%	93%	100%	73%

- Shadow Preferred Stock.

Q4'10	Q3'10	Q2'10	Q1'10	Q4'09	Q3'09	Q2'09	Q1'09
0%	19%	0%	14%	20%	7%	0%	27%

Redemption – The percentages of financings providing for mandatory redemption or redemption at the option of the venture capitalist were as follows:

Q4'10	Q3'10	Q2'10	Q1'10	Q4'09	Q3'09	Q2'09	Q1'09
19%	22%	23%	24%	21%	19%	20%	24%

Corporate Reorganizations – The percentages of post-Series A financings involving a corporate reorganization were as follows:

Q4'10	Q3'10	Q2'10	Q1'10	Q4'09	Q3'09	Q2'09	Q1'09
4%	9%	8%	14%	5%	8%	10%	10%

For additional information about this report please contact Barry Kramer at 650-335-7278; bkramer@fenwick.com or Michael Patrick at 650-335-7273; mpatrick@fenwick.com at Fenwick & West. The contents of this report are not intended, and should not be considered, as legal advice or opinion.

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