Fenwick
FENWICK & WEST LLP

Trends in Terms of Venture Financings
In Silicon Valley
(Third Quarter 2011)

Background – We analyzed the terms of venture financings for 113 companies headquartered in Silicon Valley that reported raising money in the third quarter of 2011.

Overview of Fenwick & West Results

- Up rounds exceeded down rounds in 3Q11 70% to 15%, with 15% of rounds flat. This was an increase from 2Q11 when up rounds exceeded down rounds 61% to 25%, with 14% of rounds flat. Series B rounds were exceptionally strong, comprising 38% of the relevant rounds (Series A rounds aren't included as there is no prior round for comparison purposes), and 89% of the Series B rounds were up rounds. This was the ninth quarter in a row in which up rounds exceeded down rounds.

- The Fenwick & West Venture Capital Barometer™ showed an average price increase of 69% in 3Q11, a slight decrease from the 71% increase registered in 2Q11. However, we note that one internet/digital media company had a 1,500% up round, and that if such round was excluded the Barometer would have been 54%. This was also the ninth quarter in a row in which the Barometer was positive.

- Interpretive Comment Regarding the Barometer. When interpreting the Barometer results please bear in mind that the results reflect the average price increase of companies raising money this quarter compared to their prior round of financing, which was in general 12-18 months prior. Given that venture capitalists (and their investors) generally look for at least a 20% IRR to justify the risk that they are taking, and that by definition we are not taking into account those companies that were unable to raise a new financing (and that likely resulted in a loss to investors), a Barometer increase in the 30-40% range should be considered normal.

- The results by industry are set forth below. In general internet/digital media was the clear valuation leader, followed by software, cleantech and hardware, with life science continuing to lag.

Overview of Other Industry Data.

After 2Q11 there was reason to believe that the venture environment was improving, but the results were more mixed in 3Q11. While the amount invested by venture capitalists in 3Q11 was healthy, the amount raised by venture capitalists was significantly off the pace set in the first half of the year. As a result, venture capitalists are continuing to invest significantly more than they raise, an unsustainable situation (and one that perhaps provides increased opportunities for angels and corporate investors). IPOs also decreased significantly in 3Q11, although M&A activity was up. The internet/digital media industry continued to lead, while life science continued to lag.

Detailed results from third-party publications are as follows:

- **Venture Capital Investment.** Venture capitalists (including corporation-affiliated venture groups) invested $8.4 billion in 765 deals in the U.S. in 3Q11, a 5% increase in dollars over the $8.0 billion invested in 776 deals reported for 2Q11 in July 2011, according to Dow Jones Venture Source ("VentureSource"). The largest Silicon Valley investments in 3Q11 were Twitter and Bloom Energy, which were also two of the three largest nationwide. Northern California received 38% of all U.S. venture investment in 3Q11.

  The PwC/NVCA MoneyTree™ Report based on data from Thomson Reuters (the "MoneyTree Report") reported slightly different results – that venture capitalists invested $7.0 billion in 876 deals in 3Q11, a 7% decrease in dollars over the $7.5 billion invested in 966 deals reported in July 2011 for 2Q11. Investments in software companies were at their highest quarterly level since 4Q01, at $2.0 billion; investments in internet companies fell to $1.6 billion after the ten year high of $2.4 billion reported in 2Q11, and life science and cleantech investments fell 18% and 13% respectively from 2Q11.

  Overall, venture capital investment in 2011 is on track to exceed the amount invested in 2010 according to both VentureSource and the MoneyTree Report.

- **Merger and Acquisition Activity.** Acquisitions (including buyouts) of U.S. venture-backed companies in 3Q11 totaled $13 billion in 122 deals, a 33% increase in dollar terms from the $9.8 billion paid in 100 deals reported in July 2011 for 2Q11, according to Dow Jones. The information and enterprise technology sectors had the most acquisitions, and the acquisition of PopCap Games by Electronic Arts for $750 million was the largest acquisition of the quarter.

  Thomson Reuters and the National Venture Capital Association ("Thomson/NVCA") also reported an increase in M&A transactions, from 79 in 2Q11 (as reported in July 2011) to 101 in 3Q11.

- **Initial Public Offerings.** Dow Jones reported that 10 U.S. venture-backed companies went public in 3Q11, raising $0.5 billion, a significant decrease from the 14 IPOs raising $1.7 billion in 2Q11. Perhaps of greater concern is that six of the IPOs occurred in July, with only four in the latter two months of the quarter, and half of the 10 companies went public on non-U.S. exchanges (one each on AIM, Australia and Tokyo, two on Taiwan). By comparison, all 25 companies going public in the first half of 2011 went public on U.S. exchanges.

Similarly, Thomson/NVCA reported that only five U.S. venture-backed companies went public in the U.S. in 3Q11 (they do not include offerings on foreign exchanges), raising $0.4 billion, a substantial decrease from the 22 IPOs raising $5.5 billion reported in 2Q11. This was the lowest IPO level in seven quarters. Of the five IPOs, four of the companies were based in the U.S. and one in China, and four were IT-focused and one was life science-focused. The largest of the IPOs was China-based Tudou, raising $0.2 billion.

At the end of 3Q11, 64 U.S. venture-backed companies were in registration to go public, an increase from 46 in registration at the end of 2Q11.

- **Venture Capital Fundraising.** Dow Jones reported that U.S. venture capital funds raised $2.2 billion in 3Q11, a significant decline from the $8.1 billion raised in the first half of 2011. 2011 is on track to be the fourth year in a row in which venture capital fundraising will be less than investments made by venture capitalists, and by over $30 billion in the aggregate.

  Similarly, Thomson/NVCA reported that U.S. venture capital funds raised $1.7 billion in 3Q11, a substantial dollar decrease from the $2.7 billion reported raised by 37 funds in 2Q11.

- **Venture Capital Returns.** According to the Cambridge Associates U.S. Venture Capital Index®, U.S. venture capital funds achieved a 26% return for the 12-month period ending 2Q11, less than the Nasdaq return of 31% (not including any dividends) during that period. Note that this information is reported with a one quarter lag.

- **Sentiment.** The Silicon Valley Venture Capitalist Confidence Index® produced by Professor Mark Cannice at the University of San Francisco reported that the confidence level of Silicon Valley venture capitalists was 3.41 on a 5 point scale, a decrease from the 3.66 result reported for 2Q11, and the second quarter of decrease in a row. Venture capitalists expressed concerns due to the macro economic environment, the uncertain exit environment, high company valuations and regulatory burdens. The divergence between the internet/digital media industry, which has performed well, and the lagging life science industry, was also noted.

- **Nasdaq.** Nasdaq decreased 13% in 3Q11, but has increased 10% in 4Q11 through November 14, 2011.

Detailed Fenwick & West Results

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

Series	Q3'11	Q2'11	Q1'11	Q4'10	Q3'10	Q2'10	Q1'10	Q4'09
A	18%	19%	18%	13%	20%	18%	24%	23%
B	31%	25%	24%	26%	23%	22%	21%	22%
C	19%	26%	24%	35%	28%	28%	30%	21%
D	14%	15%	20%	14%	9%	20%	11%	17%
E and higher	18%	15%	14%	12%	20%	12%	14%	17%

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

Price Change	Q3'11	Q2'11	Q1'11	Q4'10	Q3'10	Q2'10	Q1'10	Q4'09
Down	15%	25%	16%	21%	30%	27%	32%	30%
Flat	15%	14%	17%	12%	18%	18%	19%	23%
Up	70%	61%	67%	67%	52%	55%	49%	47%

The percentage of down rounds by series were as follows:

Series	Q3'11	Q2'11	Q1'11	Q4'10	Q3'10	Q2'10	Q1'10	Q4'09
B	6%	17%	10%	12%	20%	14%	23%	24%
C	19%	27%	17%	27%	33%	29%	45%	25%
D	25%	28%	25%	23%	30%	36%	18%	47%
E and higher	19%	33%	12%	17%	38%	33%	27%	26%

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 3Q11 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 Q3'11	Combined total for all Series for Q2'11	Combined total for all Series for Q1'11	Combined total for all Series for Q4'10	Combined total for all Series for Q3'10
Up rounds	+139%	+103%	+99%	+60%	+112%	+138%	+91%	+104%	+81%
Down rounds	-37%	-79%	-48%	-72%	-62%	-51%	-56%	-45%	-47%
Net result	+121%	+44%	+56%	+18%	+69%	+71%	+52%	+61%	+28%

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 3Q11, 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	44	75%	14%	11%	+71%
Hardware	8	63%	12%	25%	+34%
Lifescience	18	50%	22%	28%	+4%
Internet/Digital Media	11	73%	18%	9%	+201%*
Cleantech	9	78%	11%	11%	+41%
Other	3	100%	0%	0%	+115%
Total - All Industries	93	70%	15%	15%	+69

Please note that some industries have small sample sizes that reduce the statistical validity of the results.
*Please also note that one internet/digital media had a 1,500% up round. If this were excluded the Barometer result for the internet/digital media industry would have been 73%.

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

Q3'11	Q2'11	Q1'11	Q4'10	Q3'10	Q2'10	Q1'10	Q4'09
31%	37%	43%	28%	41%	40%	38%	41%

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

Series	Q3'11	Q2'11	Q1'11	Q4'10	Q3'10	Q2'10	Q1'10	Q4'09
B	20%	31%	24%	12%	32%	32%	23%	24%
C	57%	37%	47%	27%	27%	34%	42%	50%
D	19%	39%	42%	46%	60%	48%	36%	58%
E and higher	33%	44%	71%	42%	62%	53%	53%	37%

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

Q3'11	Q2'11	Q1'11	Q4'10	Q3'10	Q2'10	Q1'10	Q4'09
21%	29%	14%	13%	20%	17%	23%	19%

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

Range of multiples	Q3'11	Q2'11	Q1'11	Q4'10	Q3'10	Q2'10	Q1'10	Q4'09
>1x – 2x	100%	62%	83%	100%	85%	71%	86%	57%
>2x – 3x	0%	25%	0%	0%	0%	29%	14%	43%
>3x	0%	13%	17%	0%	15%	0%	0%	0%

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

Q3'11	Q2'11	Q1'11	Q4'10	Q3'10	Q2'10	Q1'10	Q4'09
39%	38%	43%	45%	53%	35%	48%	51%

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

Q3'11	Q2'11	Q1'11	Q4'10	Q3'10	Q2'10	Q1'10	Q4'09
32%	64%	60%	40%	58%	61%	54%	54%

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

Q3'11	Q2'11	Q1'11	Q4'10	Q3'10	Q2'10	Q1'10	Q4'09
6%	6%	8%	5%	7%	7%	7%	4%

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

Type of Provision	Q3'11	Q2'11	Q1'11	Q4'10	Q3'10	Q2'10	Q1'10	Q4'09
Ratchet	2%	5%	5%	3%	4%	4%	5%	6%
Weighted Average	97%	92%	92%	95%	93%	94%	94%	94%
None	1%	3%	3%	2%	3%	2%	1%	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.

Q3'11	Q2'11	Q1'11	Q4'10	Q3'10	Q2'10	Q1'10	Q4'09
6%	14%	5%	7%	15%	16%	7%	10%

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.

Q3'11	Q2'11	Q1'11	Q4'10	Q3'10	Q2'10	Q1'10	Q4'09
100%	100%	83%	100%	81%	100%	86%	80%

- Shadow Preferred Stock.

Q3'11	Q2'11	Q1'11	Q4'10	Q3'10	Q2'10	Q1'10	Q4'09
0%	0%	17%	0%	19%	0%	14%	20%

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

Q3'11	Q2'11	Q1'11	Q4'10	Q3'10	Q2'10	Q1'10	Q4'09
21%	19%	20%	19%	22%	23%	24%	21%

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

Q3'11	Q2'11	Q1'11	Q4'10	Q3'10	Q2'10	Q1'10	Q4'09
2%	5%	7%	4%	9%	8%	14%	5%

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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