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This is the third edition of *EEC Perspectives* to focus on “Series B” and later round financings. This *EEC Perspectives* presents data and analysis on the number and size of transactions in the New England region and, with respect to numbers of transactions, nationally for the first nine months of 2008. It also reports and provides analysis on certain key terms of the New England transactions.

For this issue of *EEC Perspectives*, we have asked **Justin J. Perreault** of **Commonwealth Capital Ventures** to comment on later rounds. Justin points out, among other things, that in our current economic times an early stage company raising a Series B-round financing faces additional challenges. We plan to bring you other points of view in future issues of *EEC Perspectives*.

We hope you will find this information useful in your financing efforts. In addition, we would like to hear from you if you have transactions or comments that might be interesting to others. Do not hesitate to send one of us at the EEC an email at info@foleyhoag.com. Also, please visit our Web site emergingenterprisecenter.com and plan on attending some of the many networking and educational events we hold at the EEC. We hope you will find the EEC a valuable resource as you start and grow your company.



David A. Broadwin

A Market Perspective

Justin J. Perreault, General Partner, Commonwealth Capital Ventures

We are currently experiencing the most unsettled economic times in recent memory. Against this backdrop, an early stage company raising a series B-round financing faces additional challenges. A B-round financing can be tricky even in normal times. Often a company at this stage has made substantial progress in product development, building its team, and understanding its target market. Yet at the same time, it is common for a B-round company to have modest or no revenue, so important questions of market acceptance and likely revenue ramp are still highly uncertain.

With this in mind, here are a few thoughts for entrepreneurs embarking on a B-round financing in the current environment:

It's only a financing round.

Often entrepreneurs regard B round pricing and terms as a grade for all the hard work and progress they've made. Naturally, based on these criteria many think they've earned an "A" in the form of a large valuation increase. Yet other criteria come into play in B-round pricing, many of which are completely exogenous to the startup. For example the economic backdrop, overall pricing environment for venture-backed companies, and VC's appetites to do B-rounds versus A or later-stage rounds all fluctuate. In most cases, the pricing offered for B-round financings by VCs is generally a reasonable measure of a company's value. If you want to raise a B-round, don't take the price personally. View it for what it is, the price of additional equity capital at a single moment in time.

Flat is the new up-round.

At the moment many VCs are more inwardly focused than usual, working with their existing portfolio companies to respond to the rapidly changing business environment. Many are simply not focused on making new investments. This will certainly change in short order as things settle down. There is definitely ample venture capital on the sidelines to fund exciting new ideas. But for the moment, you might consider doing an A-round extension with your existing VCs. It is quick, simple, and allows you to get back to building your business as fast as possible. Consider raising less money as an A-round extension and postpone investing the time and effort of a full-blown B-round process until the climate is more receptive.

The B-round is one step in a long journey.

Most venture-backed companies require several rounds of funding before reaching profitability and by that time the B-round terms and pricing will be irrelevant. What matters more is picking a VC firm that will work with you, your team, and other investors over the entire cycle of your company's development. You want to pick a partner that can help you to succeed and whose attitude is to ensure that along the way there is a fair distribution of rewards for everyone involved. Take the long term view and choose your partner wisely to maximize your long term outcome.

In summary, the important thing to keep in mind is that the main objective of the B-round is to secure the capital and partners who can help you grow your business to the next level. While it's a challenging time now, this too shall pass, and the long term opportunity for entrepreneurs with innovative new ideas to build great new companies is as strong as ever.

Selected New England “Series B” and Later Round Transactions

Third Quarter 2008

Implied Pre-Money and Post-Money Valuation

Company	Most recent round of preferred stock	Original issue price of most recent round of preferred stock	Number of authorized shares of preferred stock in most recent round	Value of preferred stock authorized in most recent round	Number of authorized shares of common stock	Most recent round of preferred stock as a percentage of authorized common stock	Implied pre-money valuation	Implied post-money valuation	Up or Down Round
GameLogic, Inc.	C	\$0.2081	48,045,935	\$9,998,359.07	140,587,338	34.18%	\$19,257,865.96	\$29,256,225.04	Up
Expressor Software Corporation	B	\$1.756	5,694,760	\$9,999,998.56	19,000,000	29.97%	\$23,364,001.44	\$33,364,000.00	Up
Carbonite, Inc.	C	\$18.23	1,206,802	\$22,000,000.46	6,250,000	19.31%	\$91,937,499.54	\$113,937,500.00	Up
innoPad, Inc.	B	\$1.2	2,500,000	\$3,000,000.00	14,000,000	17.86%	\$13,800,000.00	\$16,800,000.00	Up
Ambient Devices, Inc.	AA	\$0.454	11,222,712	\$5,095,111.25	16,475,662	68.12%	\$2,384,839.30	\$7,479,950.55	Up
Blueshift Technologies, Inc.	B-2	\$1.35	5,377,393	\$7,259,480.55	37,746,319	14.25%	\$43,698,050.10	\$50,957,530.65	Up
PatientKeeper, Inc.	F	\$2.17	3,555,000	\$7,714,350.00	60,000,000	5.93%	\$122,485,650.00	\$130,200,000.00	Up

This analysis is inherently imprecise and is based on a number of general assumptions which may or may not be accurate. However, in a typical situation we believe it will yield an approximation of the valuation placed on the company at the time of financing, and therefore may be of interest to our readers

COMMENTARY:

David Pierson, Foley Hoag Partner

As was the case for the Q2 2008 later-stage deals featured in the December 2008 issue of EEC Perspectives, the Q3 2008 later-stage deals in the table above present a mixed picture. Significantly, the level of financing activity in Q3 2008 was down materially compared to Q2 2008 (7 reported transactions in Q3 versus 15 reported transactions in Q2). As was the case in Q2, the size of the reported transactions varied widely, as did the percentage of the financed companies sold and the implied pre- and post-money valuations, and once again some but not all of these differences can be accounted for by the stage of the financing round in question. Perhaps the most encouraging aspect of the reported Q3 data is that despite the worsening economic outlook, financing transactions continued to get done and all of the reported transactions were up-rounds. This tends to support the notion that even in these difficult economic times, promising companies should be able to find investors that are willing to fund their growth. Those that do best will be the ones that have trimmed their expenses and cash burn rates sufficiently to enable them to be patient in their search for new money and that have managements and existing investor syndicates that are willing to be flexible on terms for the next round.

We can prepare a similar analysis across any group of transactions that our clients are interested in. For example, we could prepare an analysis for a group of competitive companies so you can see what the implied valuations of your competitors are. If you would like additional information on this service, please contact your lawyer at Foley Hoag or one of our Emerging Enterprise Center lawyers listed at the end of this publication.

Terms of New England “Series B” and Later Rounds¹

	Q1		Q2		Q3		Q4
Based on NVCA Form ²	Yes 6	No 4	Yes 10	No 5	Yes 7	No 0	
Dividends							
Cumulative accruing ³	Yes 5	No 5	Yes 7	No 8	Yes 3	No 4	
1x Liquidation Preference⁴							
With full participation	1		2		0		
With capped participation	3		3		4		
Non-participating	4		8		3		
Greater than 1x Liquidation Preference							
With full participation	0		0		0		
With capped participation	0		2		0		
Non-participating	0		0		0		
Redemption	9		11		7		
Antidilution⁵							
Fully broad-based	1		3		0		
Broad-based	6		10		6		
Narrow-based	0		1		0		
Full ratchet	3		1		1		
Pay to Play Provision	3		3		3		

¹ Determined from a review of publicly available Certificate of Incorporation filings.

² Certificate of Incorporation appears to have been based substantially on the NVCA form.

³ Dividend rates ranged from 6% to 8% during the third quarter of 2008.

⁴ Two of the transactions involved liquidation preferences which are not typical in these type of transactions and therefore were not included in the above chart.

⁵ “Fully broad-based”, “broad-based” and “narrow-based” all refer to a weighted average conversion rate adjustment formula. “Narrow-based” means that the formula includes outstanding equity on an as-converted basis, but not options or warrants. “Broad-based” adds to the narrow-based formula outstanding options and warrants on an as-exercised basis, but does not include ungranted options. “Fully broad-based” adds to the broad-based formula options that may be issued in the future pursuant to a plan approved by the Board of Directors. “Full ratchet” means that the conversion rate adjusts to the lowest price at which the issuer sells or is deemed to sell (as in the case of a sale of convertible securities) any shares of common stock.

The table above summarizes publicly available information about various terms included in the Certificates of Incorporation for “Series B” and later-round financings for companies headquartered in New England. For the purposes of this table we have focused solely on transactions that appeared to us, from the public filings, to be identifiable as “Series B” and later-round financings. We have excluded transactions that appeared to us to involve considerations and concerns different from those applicable in a typical “Series B” or later round, such as might occur, for example in the case of a recapitalization. For this reason, the set of transactions described above is somewhat different from the set of transactions described in the later tables. We have selected terms to report on that we believe will be of particular interest to entrepreneurs. Each of these terms is linked to a description of that term in our Web site. Information included in the table above is based on information made publicly available by participants in the relevant transactions and therefore is not comprehensive.

COMMENTARY:
Bruce Kinn, Foley Hoag Partner

It is interesting that, at least within this sample, there was no major shift in price-related terms, such as full ratchets or greater liquidation preferences, when Q3 deals are compared to deals occurring earlier in the year. Although the number of deals and the prevalence of up-rounds in the Q3 sample suggest caution in drawing conclusions too broadly, this observation is consistent with our experience during the period, with investors more likely to address their pricing concerns through direct price negotiation than through other related terms. A second observation from the data is the uniform acceptance of redemption provisions, apparently in response to the persistent slowdown in IPOs and other exits last year.

It is important to place the 2008 Q3 data that is presented here against a backdrop of public markets and a national economy that were at that time under stress but not yet in rout. We expect that the pricing and price-related terms for 2008 Q4 data, when available, will provide a more negative picture.

We can prepare a similar analysis across any group of transactions that our clients are interested in. For example we could prepare an analysis by industry so you can see what terms are prevalent in your industry. If you would like additional information on this service, please contact your lawyer at Foley Hoag or one of our Emerging Enterprise Center lawyers listed at the end of this publication.

The Activity Level Summary

New England "Series B" and Later Round Transactions by Industry*

Industry	2007				2008				9 Months ended September 30, 2007	9 Months ended September 30, 2008
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4		
Biopharma	4	7	9	13	5	6	11		20	22
Medical Device	3	10	3	4	5	5	6		16	16
Alternative Energy	1	0	3	1	1	3	0		4	4
Software	12	24	12	23	14	13	10		48	37
Communications	5	5	5	2	1	2	2		15	5
Other	9	7	14	9	13	11	14		30	38
Total	34	53	43	52	39	40	43		133	122

* Source: Dow Jones VentureOne

National "Series B" and Later Round Transactions by Industry*

Industry	2007				2008				9 Months ended September 30, 2007	9 Months ended September 30, 2008
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4		
Biopharma	46	50	37	61	33	41	44		133	118
Medical Device	41	49	32	39	44	44	42		122	130
Alternative Energy	5	18	14	8	10	16	18		37	44
Software	91	132	102	111	111	117	89		325	317
Communications	36	28	41	28	28	25	29		105	82
Other	98	132	127	140	154	128	129		357	411
Total	317	409	353	387	380	371	351		1079	1102

* Source: Dow Jones VentureOne

Size of New England 2008 Year to Date “Series B” and Later Round Transactions by Industry*

Industry	\$5 million or less	Above \$5 million up to \$10 million	Above \$10 million up to \$15 million	Above \$15 million up to \$20 million	Above \$20 million
Biopharma	3	2	5	2	9
Medical Device	5	6	2	2	1
Alternative Energy	1	1	0	0	2
Software	11	9	8	0	7
Communications	2	2	0	0	1
Other	19	10	5	0	2
Total	41	30	20	4	22

* Source: Dow Jones VentureOne

The tables above summarize publicly available information about the number and size of second round financings for companies headquartered in New England and nationally by industry. The data included in the tables is derived from Venture Source, a publication of Dow Jones Venture One. Venture Source categorizes transactions as “seed round” “first round,” “second round” and so on. Upon examination of each transaction, it is not always clear why a particular transaction was put in a particular category, however, for the purposes of these tables we have used the categories as defined by VentureSource. Information included in the tables below is based on information made publicly available by participants in the relevant transactions and therefore is not comprehensive.

COMMENTARY:
Amanda Vendig, Foley Hoag Lawyer

Both nationally and in New England the number of deals being done in the biopharma, medical device and alternative energy industries have remained consistent with their 2007 levels. Unfortunately the same cannot be said of deals being done in the software and communications industries which have seen drops of 20% or more in the number of deals as compared to this time last year. We have seen this same trend for Series A financings, where the biopharma, medical device and alternative energy sectors have held up well in the current economic downturn but the software and communications sectors have been hit much harder.

If you have any questions about this publication or about the EEC and how we can help your entrepreneurial venture, please feel free to contact any of the following lawyers:

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