

**Included in this Issue**

- A Market Perspective
- Selected New England “Series B” and Later Round Transactions
- Terms of New England Series B and Later Rounds
- The Activity Level Summary

This edition of EEC Perspectives focuses on “Series B” and later round financings. We hope it will be an informative companion to last month’s publication devoted to Series A financings. This EEC Perspective presents data and analysis on the number and size of transactions in the New England region and, with respect to numbers of transactions, nationally. It also reports and provides analysis on certain key terms of the New England transactions. Based on our sampling, the first quarter of 2008 was a good time to do a Series B or later financing.

For this issue of EEC Perspectives, we have asked Foster Hinshaw of Dataupia Corporation to comment on later rounds. Foster points out, among other things, that, the general downturn in the economy leads VCs to favor early stage investments. 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](mailto:info@foleyhoag.com). Also, please visit our web site, [emergingenterprisecenter.com](http://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

Foster Hinshaw, Founder and CEO, Dataupia Corporation

### ***“B” Rounds -- Opportunity in “Gloom and Doom”***

In 2002, during the valley of the tech bubble burst, one of the most respected VC's in the tech community said to me:

“It's all about survival, survival, survival – I don't know if we will ever recover”.

Notwithstanding, the resiliency of our tech community proved its intrinsic value to the economy and there were some nice IPO's and exits from companies that were incubating during the bubble years (including FAST, EqualLogic and Netezza).

Today the news is similar: (a) zero IPOs in Q2 2008; (b) the financial sector is in a major, albeit predictably cyclical, reset; and worse (c) another 1970's style energy crisis is on us.

Almost as predictably, VC capital favors earlier rounds. This is for two reasons: (1) anticipated exit prices have decreased reflecting that IPO's set the market price, even for acquisitions; and (2) time-to-exit has now extended by at least one year and hence has lowered anticipated ROI's. These disproportionately affect later rounds rather than “A” rounds. For instance, “D” rounds which traditionally are 12 to 18 months until exit are now anticipating at least 18 to 24 months until exit. Even “C” and “B” rounds are adversely affected in favor of “A” rounds.

The challenges for the emerging company in our current “gloom and doom” are to:

- Have compelling value for its customers to fight a bad economy (such as tools to competitively attract end customers)
- Prove itself to be counter-cyclical or at least economically resilient (such as lower cost solutions for fundamental infrastructure)
- Have high competitive differentiation to be the leader in its category

The exciting part for “B” round entrepreneurs is that the next couple of years is the time to build traction and momentum so that you are positioned for an excellent exit as the economy inevitably recovers and needs exciting new technologies.

## Selected New England “Series B” and Later Round Transactions

### First 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
Aveksa, Inc.	Series B	\$0.6935	18,959,184	\$13,148,194.10	45,000,000	42.13%	\$18,059,305.89	\$31,207,500.00	Up
Contour Semiconductor, Inc.	Series B	\$1.0268	16,016,922	\$16,446,175.51	41,000,000	39.07%	\$25,652,624.49	\$42,098,800.00	Up
CoreStreet, Ltd.	Series B	\$1.64025971	6,238,120	\$10,232,136.90	35,000,000	17.82%	\$47,176,952.95	\$57,409,089.85	Up
Everyscape, Inc.	Series B	\$1.25802	5,705,844	\$7,178,065.87	13,500,000	42.27%	\$9,805,204.13	\$16,983,270.00	Up
Eyegate Pharmaceuticals, Inc.	Series C	\$1.747797	8,605,118	\$15,039,999.43	40,000,000	21.51%	\$54,871,880.57	\$69,911,880.00	Up
Noble Peak Vision Corp.	Series B	\$1.972387	6,084,000	\$12,000,002.51	23,500,000	25.89%	\$34,351,091.99	\$46,351,094.50	Up
PointCare Technologies, Inc.	Series C	\$13.3488	500,000	\$6,674,400	1,800,000	27.78%	\$17,353,440	\$24,027,840	Unknown
QD Vision, Inc.	Series C	\$1.28538	12,058,805	\$15,500,146.77	32,000,000	37.68%	\$25,632,013.23	\$41,132,160.00	Up
Reveal Imaging Technologies, Inc.	Series C	\$2.769	2,889,393	\$8,000,729.22	35,000,000	8.26%	\$88,914,270.78	\$96,915,000.00	Up
Vlingo Corporation	Series B	\$2.33	8,600,152	\$20,038,354.16	30,000,000	28.67%	\$49,861,645.84	\$69,900,000.00	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.*

We can prepare a similar analysis across any group of transactions that our clients are interested in. For example, we could prepare 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.

**COMMENTARY:**  
**Bill Kolb, Foley Hoag Partner**

“The information in the table is encouraging for both entrepreneurs and investors. Most significantly, the new financings are predominantly “up” rounds, suggesting that investors are bullish on the company’s prospects and are willing to invest at a higher valuation. Also noteworthy is the amount invested. Each financing reported in the table is a substantial commitment, ranging from \$6 million to \$20 million of new money. This indicates that the funds are being used to grow the business, as opposed to merely maintaining current operations.

The information seems to run counter to the general perception that the overall economy is shaky and that many businesses are contracting. However, from our own practice and experience, we continue to see many interested investors with ample funds eager to finance promising businesses. Whether the positive trends of the first quarter of 2008 will continue for the remainder of the year remains to be seen, but the information supports the conclusion that even in uncertain economic times, there are opportunities for strong companies to obtain significant funding on attractive terms.”

## Terms of New England Series B and Later Rounds<sup>1</sup>

	Q1	
	Yes	No
Based on NVCA Form <sup>2</sup>	6	4
Dividends		
Cumulative accruing <sup>3</sup>	5	5
1x Liquidation Preference <sup>4</sup>		
With full participation	1	
With capped participation	3	
Non-participating	4	
Greater than 1x Liquidation Preference		
With full participation		
With capped participation		
Non-participating		
Redemption	9	
Antidilution <sup>5</sup>		
Fully broad based	1	
Broad based	6	
Narrow based		
Full ratchet	3	
Pay to Play Provision	3	

### COMMENTARY: Bob Warren, Foley Hoag Lawyer

“You will notice that almost every deal we looked at for this issue of EEC Perspectives included redemption rights for the preferred stock being sold. For the most part, redemption rights are pretty innocuous. VC’s “need” them because they want a pathway to get out of their investment if an exit hasn’t occurred prior to the end of the life of the fund, but as a practical matter, these rights are rarely used or even threatened. That being said, redemption rights do cause headaches for the accountants. In fact, for two separate IPO clients I have seen comments and confusion from the SEC staff on the correct accounting treatment for redeemable preferred stock. One issue is whether or not redeemable preferred stock should be treated as equity or debt (or something in between) on the face of the balance sheet. For the most common form of venture capital preferred stock (optional redeemable preferred), the correct answer might be a treatment that is in between equity and debt (see SFAS 133). For CFOs of later stage venture backed companies with an eye on the public markets, my advice is to make sure you have a handle on the “effective interest method” and the accretion of redeemable preferred stock. The answers aren’t always straightforward.”

We can prepare a similar analysis across any group of transactions that our clients are interested in. For example we could prepare 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.

<sup>1</sup> Determined from a review of publicly available Certificate of Incorporation filings.

<sup>2</sup> Certificate of Incorporation appears to have been based substantially on the NVCA form.

<sup>3</sup> Dividend rates ranged from 6% to 8% during the first quarter of 2008.

<sup>4</sup> 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.

<sup>5</sup> “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 on the previous page 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.

## The Activity Level Summary

### New England Series B and Later Round Transactions by Industry\*

Industry	2007				2008	Total 2007	Total 2008
	Q1	Q2	Q3	Q4	Q1		
Biopharma	4	7	9	13	5	33	5
Medical Device	3	10	3	4	5	20	5
Alternative Energy	1	0	3	1	1	5	1
Software	12	24	12	23	14	71	14
Communications	5	5	5	2	1	17	1
Other	9	7	14	9	13	39	13
Total	34	53	43	52	39	182	39

\* Source: Dow Jones VentureOne

### National Series B and Later Round Transactions by Industry\*

Industry	2007				2008	Total 2007	Total 2008
	Q1	Q2	Q3	Q4	Q1		
Biopharma	46	50	37	61	33	194	33
Medical Device	41	49	32	39	44	161	44
Alternative Energy	5	18	14	8	10	45	10
Software	91	132	102	111	111	436	111
Communications	36	28	41	28	28	133	28
Other	98	132	127	140	154	497	154
Total	317	409	353	387	380	1466	380

\* Source: Dow Jones VentureOne

### Size of New England 2008 Year to Date Series B and Later Round Transactions by 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	2	0	1	1	1
Medical Devices	3	2	0	0	0
Alternative Energy	0	0	0	0	1
Software	6	2	3	0	3
Communications	0	1	0	0	0
Other	7	3	2	0	1
Total	18	8	6	1	6

\* Source: Dow Jones VentureOne

**COMMENTARY:**  
**Matt Eckert, Foley Hoag Lawyer**

“Contrary to the data for Series A financings that we reported in the previous issue of EEC Perspectives, the numbers of transactions that closed in the first quarter of 2008, both in New England and nationally, were up slightly from the first quarter of 2007. While random variation may account for the difference, the data may also indicate that venture financing activity in Series A rounds is more sensitive to short-term or cyclical changes in general economic conditions than that of subsequent rounds. The investment decision in later-round financings is often rather different than that in a Series A, and the timing of later rounds (particularly for existing investors) is dictated largely by the capital needs of the company rather than evaluation of a business plan. Perhaps the old marketing maxim that it is easier to retain existing customers than acquire new ones applies to venture capitalists as well. This can be an important consideration when evaluating whether to proceed with a Series A round on the term sheet in hand or hold out for a more favorable offer that may or may not come along.”

*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.*

If you have any questions about this quarterly review 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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