

The Capital Network

Negotiation and Valuation

January 27, 2010

LEGAL INSIGHT. BUSINESS INSTINCT.

Valuation

- Art or Science?
- Supply and Demand (i.e., companies vs. dollars)
- Macro Economic Factors
- Qualitative and Quantitative Factors

Glossary

- Pre-Money Value = Assumed value of enterprise before capital is invested
- Post-Money Value = Pre-money value plus invested capital
- Seed Money = Initial capital invested in company
- Series A, B, C, etc. = Rounds of preferred stock investment

Glossary

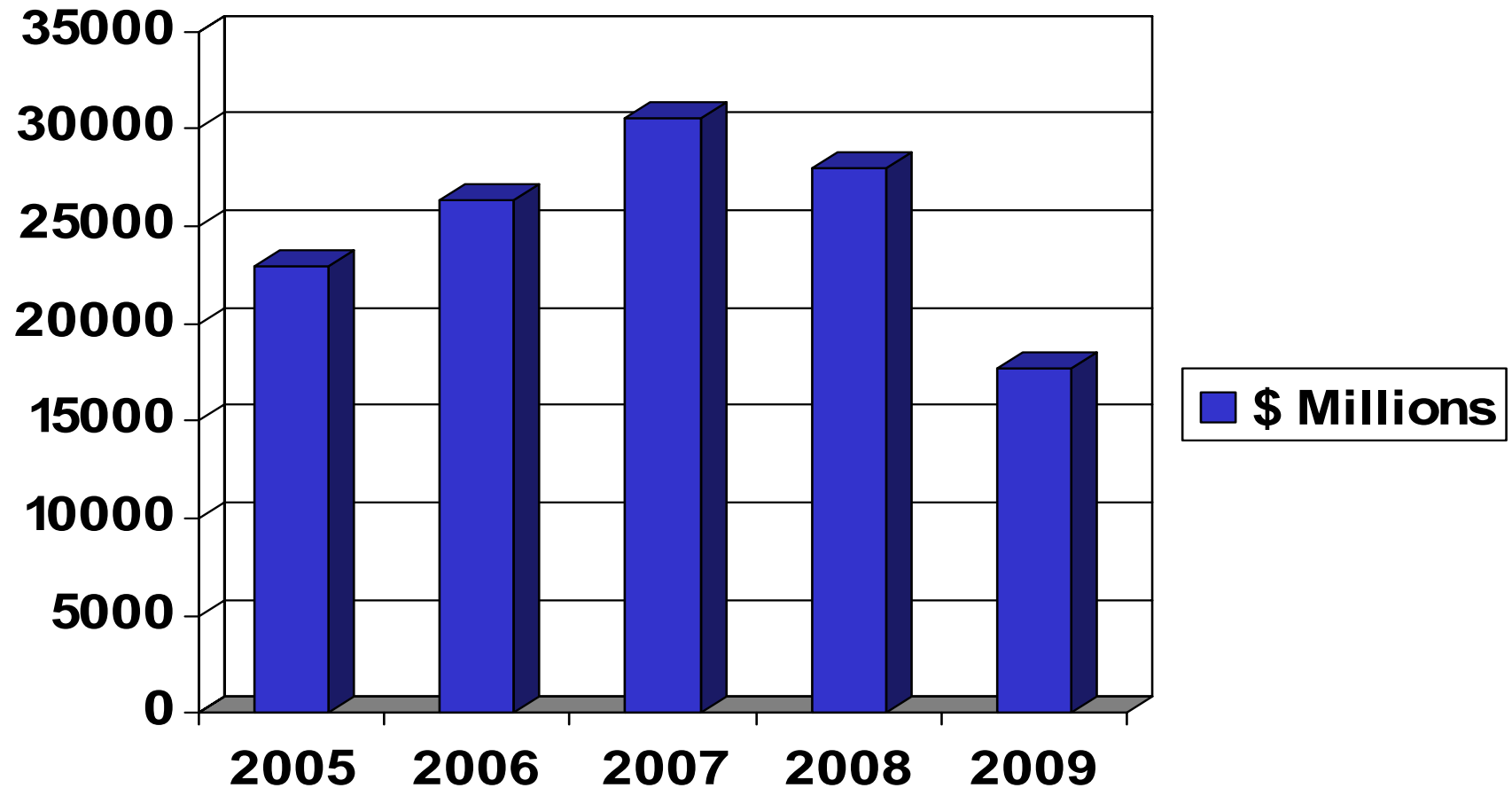
- $\text{Price Per Share} = \text{Pre-Money Value} / \text{Pre-Money Shares}$
- Fully Diluted shares = Shares outstanding assuming conversion/exercise of all options, warrants and other convertible securities (typically including the Option Pool)
- Option Pool = Need to determine how this is treated for purposes of calculating number of fully diluted shares

Valuation by Stage

Financing	Company Stage (Examples)	Data	Risk Uncertainty	Median Pre-Money Value (MM)*	% Change from 2008*
Seed	Incorporation; early development	Soft data: value proposition; team experience; etc.	Extremely high	\$2.3	(13.1%)
First Round (Series A)	Development	Soft and hard data: concept validation; technology validation; time to market; execution risk	Very high	\$5.8	(12.1%)
Second Round (Series B)	Shipping Product	More hard data: preliminary revenue; market reaction; competitive landscape	High	\$15.3	(24.2%)
Later Stage (Series C and beyond)	Shipping Product/Market Expansion	Hard data, yet lingering young company uncertainty; predictive revenue(?)	Moderate to lower	\$35.7	(54.1%)

* Source: VentureSource Valuation Statistics through 3Q09

Historical Landscape - Total US Venture Deals



Source: Pricewaterhouse Coopers/NVCA MoneyTree Report

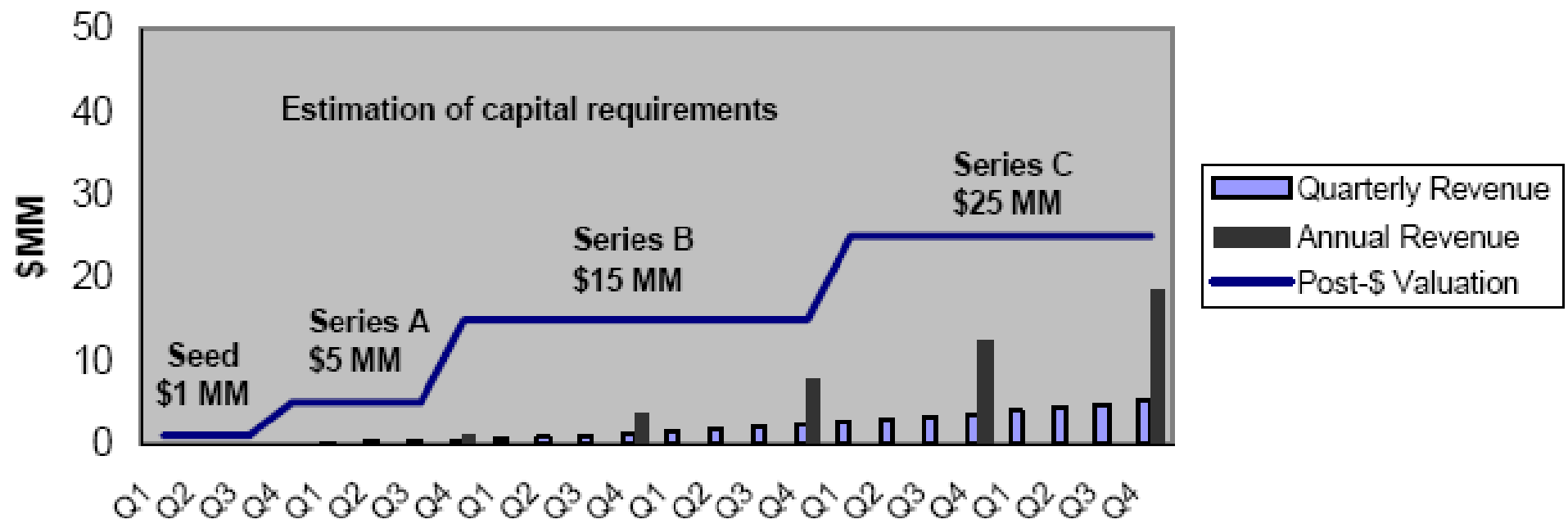
Note this does not include “angel investments”. Per Center for Venture Research, Angel investment dollars were down 27% for the first half of 2009 vs. same period of 2008, and investment mix shifted 19% from seed stage to mid-stage.

Also note this has not been adjusted for inflation,. Per US Bureau of Labor Statistics, \$100 in 2005 had the same buying power as \$109.85 in 2009.

BINGHAM

Staged Financing Strategy

Long-term Financing Strategy



VALUATION

MAGIC, METHOD OR MADNESS??

REAL ISSUE - GROWING THE PIE

VALUATION - HOW TO AGREE

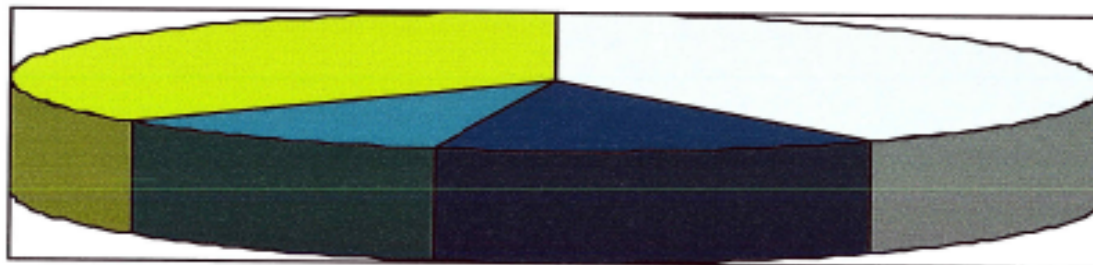


□ founders
■ employees

- Remember it's the area of the pie slice not the %
- All parties agree ... focus on building value



□ founders
■ employees
■ angels



□ founders
■ employees
■ angels
■ VCs

VALUATION - QUANTITATIVE

- Based on Sales
- Based on Net Income
- Discounted Cash Flow
- Discounted Future Earnings
- Net Worth or Book Value
- Real Options, Black Sholes, Etc.

VALUATION - QUALITATIVE

- Market Driven Methods
- Key Assets
- Financing History
- Size and growth of Market
- Rate of Return Required by Investor

VALUATION - QUALITATIVE

- Market Driven Methods
 - Review of “comparable” deals
 - Valuation of deals recently completed in a similar space
 - Competitive landscape

VALUATION - QUALITATIVE

- Key Assets of The Company
 - Management - Knowledge & Experience
 - Intellectual Property - Defensibility
 - Accuracy of Financials & Time to Profitability
 - Milestones achieved and missed
 - Product, Revenue, Customers

Valuation in the extremely early stage is all about relationships - growing team, advisors, board, customers etc.,

VALUATION - QUALITATIVE

- Financing History
 - How Much Funding to Date
 - What Are Future Funding Needs
 - Last Round Post-Money Valuation
 - When Was The Last Round Completed
 - Is The Stock Option Pool Sufficient

VALUATION - QUALITATIVE

- Size and Growth of Market
 - Current Size and Targeted Market
 - Not the total available market
 - Anticipated growth rate (CAGR)

VALUATION - QUANTITATIVE

- Return Rate Required By Investor
 - 10x to 20x?
 - Time Frame - 3-5-7 Years?
 - Valuation can be “determined” by working in reverse from a “likely exit valuation”

VALUATION - THE END GAME

- Investor Interest and Competition (real or perceived)
- Overall Climate
- What can the VC sell to his/her partners
- What are the dynamics among the syndicate?
- What are the Company's alternative options?

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Hartford
Hong Kong
London
Los Angeles
New York
Orange County
San Francisco
Santa Monica
Silicon Valley
Tokyo
Walnut Creek
Washington

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