



COUNSEL TO GREAT COMPANIES

The Art of the Venture Capital Term Sheet

UCLA First Fridays

September 7, 2018

Presented by:

George Colindres, Senior Counsel
gcolindres@perkinscoie.com

Perkins Coie LLP

Presentation Overview

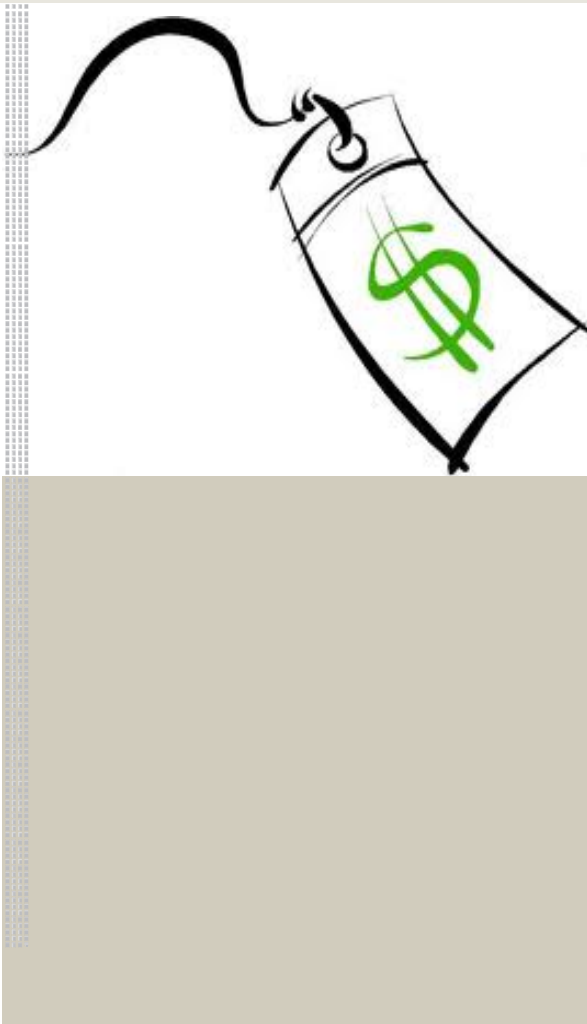
- Term Sheet Provisions
- Q&A
- The Financing Process (if we have time)

Term Sheet Provisions

OVERVIEW

- Price and Valuation
- Liquidation Preference
- Anti-Dilution: Full Ratchet vs. Weighted Average
- Board Composition
- Drag-Along Rights
- Protective Covenants
- Information and Registration Rights
- Participation Rights
- Rights of First Refusal and Co-Sale

Term Sheet Provisions



PRICE AND VALUATION

- Pre-Money and Post-Money Valuations
- Based on “Fully-Diluted” Capitalization
- Treatment of Stock Option Reserve

Example Capital Structure

Series A Financing

Founders	4,000,000 Shares	40%
Option Pool	2,000,000 Shares	20%
Series A Preferred Stock	4,000,000 Shares	40%
<hr/>		
“Fully-Diluted”	10,000,000 Shares	

- “Pre-Money” is \$3,000,000, so
Series A Price = $\$3.0\text{MM} / 6.0\text{MM} = \0.50 per Share
- \$2,000,000 Investment (at \$0.50) = 4,000,000 Shares
- “Post-Money” is \$5,000,000
- Called a “2 on 3” Round

Example Capital Structure - Continued

Series B Financing

Founders	4,000,000 Shares	18.2%
Old Option Pool	2,000,000 Shares	9.1%
Series A Preferred Stock	4,000,000 Shares	18.2%
Option Pool Increase	2,000,000 Shares	9.1%
Series B Preferred Stock	10,000,000 Shares	45.5%
<hr/>		
“Fully-Diluted”	22,000,000 Shares	

- “Pre-Money” is \$12,000,000, so . . .
- Series B Price = $\$12.0\text{MM} / 12.0\text{MM} = \1.00 per Share
- \$10,000,000 Investment (at \$1.00) = 10,000,000 Shares
- “Post-Money” is \$22,000,000
- “10 on 12” Round

Term Sheet Provisions



***Defined:** Right of Preferred Stock to Receive a Preferential Payout Relative to Other Stockholders Upon a Liquidation or Sale of the Company.*

LIQUIDATION PREFERENCE

- Multiples (1x, 2x) Before Payment to Junior Classes
- “Participating” vs. “Non-Participating”
- “Senior” vs. “Pari Passu”

Term Sheet Provisions

Examples of Liquidation Preference

Founders	4,000,000 Shares	18.2%
Old Option Pool	2,000,000 Shares	9.1%
Series A Preferred Stock	4,000,000 Shares	18.2%
Option Pool Increase	2,000,000 Shares	9.1%
Series B Preferred Stock	10,000,000 Shares	45.5%
<hr/> "Fully-Diluted"		22,000,000 Shares

Participating Preferred/Series B Senior to Series A

Sale \$20 Million

Series B → First \$10MM

Series A → Next \$2MM

All Shares → Split \$8MM (\$0.364/Share)

Non-Participating Preferred/Series B Senior to Series A

Series B → First \$10MM (\$1.00 > \$0.909)

Series A/Founders/Options → Split \$10MM (\$0.83/Share)

(Series A Does Not Convert Because \$0.83 > \$0.50)

Term Sheet Provisions

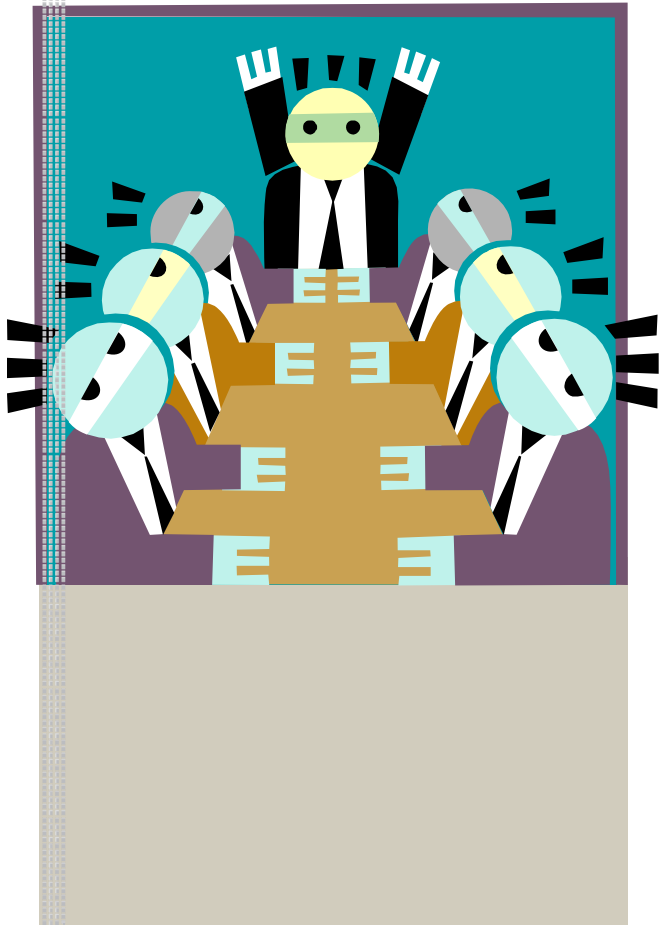


***Defined:** Adjustment to the Conversion Ratio of Preferred Stock into Common Stock Applied Upon the Subsequent Sale of Stock at a Lower Price than Current Round*

ANTI-DILUTION

- Applies to “Down Rounds” Only
- “Full-Ratchet” vs. “Weighted Average”
- “Broad-based” vs. “Narrow-based”
- Exclusions and Carveouts

Term Sheet Provisions



COMPOSITION OF BOARD OF DIRECTORS

- Size of Board
- Mechanics of Stockholder Voting
- Control Issues
- Voting Agreement

Term Sheet Provisions



***Defined:** Right to Force Other Stockholders to Agree to a Sale of the Company*

DRAG ALONG RIGHTS

- Enforceability Issues
- Compromises
- Minimum Sales Prices

Term Sheet Provisions



***Defined:** Right to Prevent the Company from Taking Certain Actions Without Approval of the Investors*

PROTECTIVE COVENANTS

- Future Financings
- Changes in Rights, Preferences and Privileges
- Company Sale
- Board Composition
- Stock Option Plan Reserves
- Material Transactions

Term Sheet Provisions



*Defined: Right to
Receive Information*

INFORMATION RIGHTS

- Information Rights
- Observation Rights
- Inspection Rights

Term Sheet Provisions



***Defined:** Rights to Cause the Company to Register the Shares Held by Investors with the SEC for Re-Sale to the Public*

REGISTRATION RIGHTS

- “Demand” Registration Rights
- “Piggyback” Registration Rights
- “S-3” Registration Rights

Term Sheet Provisions



***Defined:** Right of the Investors to Purchase a Pro Rata Share of Future Financings*

PARTICIPATION RIGHTS

- Sometimes Limited to “Major Investors”
- Calculation of “Pro Rata Share”
- Carveouts and Exclusions
- Waiver of Rights

Term Sheet Provisions



Defined: *Right of Investors to Purchase Shares to be Sold by a Company “Founder” or to Sell Shares in lieu of the Founder*

RIGHTS OF FIRST REFUSAL AND CO-SALE

- Inhibits Founder Liquidity/Secondary Sales
- Carveouts and Exclusions
- Cumbersome Process

Term Sheet Provisions



OTHER ISSUES

- Drafting Control
- Pre-Closing Covenants (Diligence Issues)
- Post-Closing Covenants
- Legal Opinions
- Due Diligence and Legal Expenses
- Tranches based on Milestones

The Financing Process

Step One:

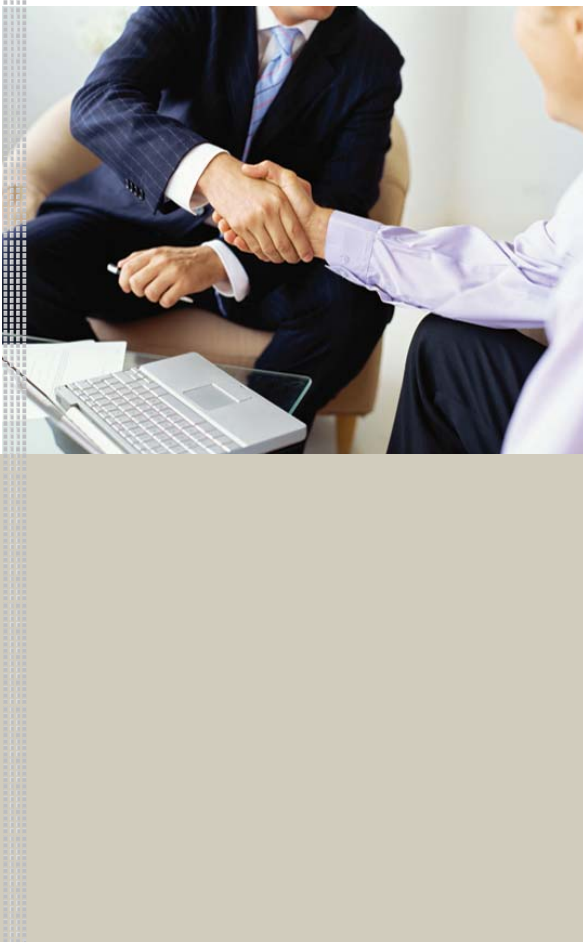


PREPARATION

- Forming and Organizing a Corporation
- Management Team
- Board of Directors
- Board of Advisors
- Assigning the Intellectual Property
- “Clean” is Better than “Complex”

The Financing Process

Step Three:



SHOPPING THE COMPANY

- Due Diligence on Potential Investors
- Creating a “Buzz”
- Identifying a Lead Investor
- Forming a Syndicate

The Financing Process

Step Four:

BUSINESS DUE DILIGENCE

- Defending the Business Model
- Educating the Investor
- Key References
- Management Diligence



The Financing Process

Step Five:



TERM SHEET

- Valuation
- Key Terms
- Understand Which Terms are Negotiable
- Spend the Time to Get the Terms Right

The Financing Process

Step Six:



LEGAL DUE DILIGENCE

- Capital Structure
- Stock and Option Vesting
- Employment and Consulting Agreements
- Key Contracts
- Intellectual Property

The Financing Process

Step Seven:



DEAL DOCUMENTS

- Preferred Stock Purchase Agreement
- Certificate of Incorporation
- Investor Rights Agreement
- Voting Agreement
- Right of First Refusal and Co-Sale Agreement
- Legal Opinion
- Ancillary Documents

The Financing Process

Step Eight:



THE CLOSING

- Collecting Signatures
- Addressing Diligence Concerns and Issues
- Show Me the Money

The Financing Process

Step Nine:



AFTER THE CLOSING

- Closing Documents and Certificates
- Schedule First Board Meeting
- Meet Milestones
- Periodic Investor Updates

Georges Colindres

Senior Counsel



LOS ANGELES, CA

+1.310.788.3280

SAN DIEGO, CA

1.858.720.5739

GColindres@perkinscoie.com

Full Bio Available at
www.perkinscoie.com/GColindres/

George Colindres is senior counsel with the Corporate practice and Emerging Companies & Venture Capital practice in the firm's Los Angeles and San Diego offices.

He acts as outside general counsel for clients in a diverse array of industries, including social networking, e-commerce, online advertising, online gaming, software, hardware, telecommunications, medical devices, biotechnology, pharmaceuticals and real estate. His work for these clients includes:

- Corporate governance, including entity formation and capital structuring and equity incentive plan matters
- Commercial and licensing agreements, including drafting and negotiating confidentiality/nondisclosure, clinical trial, distribution, development, manufacturing, VAR and OEM 2nd co-marketing agreements, terms of service/use and privacy policies
- Employment and compensation matters
- Preferred Stock and other equity financings
- Convertible promissory note (bridge) financings
- Venture debt financings and other secured transactions
- M&A transactions
- Public offerings

George also represents venture capital firms, private equity firms, real estate funds, strategic investors, angels and angel groups and other investors in connection with fund formation, governance matters, making investments and M&A transactions.

Emerging Companies & Venture Capital

Practice Spotlight



We regularly represent venture-backed and public company issuers in a wide variety of capital raising activities throughout the world. In the past year, we handled more than 500 financings for venture-backed and emerging growth companies.

OVERVIEW

Perkins Coie's Emerging Companies & Venture Capital group offers a wide breadth of experience in corporate and transactional matters. We have the depth and breadth of expertise and resources to scale with companies as they grow and to help them succeed over the long term. We take a pragmatic and solution-oriented approach, both in deals such as equity financings and other strategic transactions, and in our outside general counsel role, and we know how to get things done while striking the right balance between advocacy and compromise.

NOTEWORTHY PARTNERSHIP



We are trusted thought leaders. For years, lawyers in our practice have been members of the NVCA Model Legal Documents Working Group.

We not only helped develop model financing documents, but also served on the NVCA steering committee to develop model H.R. documents and codes of conduct for both the venture investors and the portfolio companies they invest in. We hope these policies are adopted throughout the industry, sending a strong message that sexual harassment and inappropriate behavior has no place in the venture eco-system.

Emerging Companies & Venture Capital

Practice Spotlight

With one of the nation's largest and most active technology-oriented business practices, we have unmatched experience in handling complex corporate finance, intellectual property, technology transfer and other business issues on behalf of innovative startups and investors.

70+
ECVC ATTORNEYS



IN THE PAST TWO YEARS, WE HAVE ENGAGED
1,000+
STARTUP AND
INVESTOR CLIENTS



IN THE PAST YEAR ALONE, WE HAVE HANDLED
500+
STARTUP AND
INVESTOR FINANCINGS



AND HAVE HELPED THOSE CLIENTS WITH
3,500+ NEW
MATTERS

INTELLECTUAL PROPERTY	TECHNOLOGY LICENSING	PRIVACY & SECURITY
--------------------------	-------------------------	-----------------------



STARTUP COUNSEL FOCUS AREAS

- Formations and founder issues
- Independent contractor issues
- Privacy and security issues
- Crisis management
- Venture capital fund formation
- Venture capital litigation
- Dispute counseling
- Venture debt
- Corporate finance
- Initial public offerings
- General business counseling
- Intellectual property protection
- Corporate governance and advisor counseling
- Commercial contracts
- Mergers & Acquisitions
- Employee issues
- Licensing and technology

Public Companies: Corporate Venture Capital

Practice Spotlight

Our Emerging Companies & Venture Capital attorneys represent many of Perkins's Coies public, Fortune 1000 company clients in their investments in venture-backed companies. Our bi-coastal, integrated team, which handles a wide range of domestic and international fund formations and financings, is a natural choice for many of the world's largest and most established corporations. Working together, we have handled thousands of financings, and our representation of emerging growth companies, venture capital funds and public companies provides us with broad and deep experience negotiating and closing financing transactions quickly and efficiently. A few of our corporate venture capital clients include:



CLIENT SPOTLIGHT: FROM STARTUP TO IPO TO M&A TO FUND FORMATION TO CORPORATE VENTURE CAPITAL



We have represented Amazon from its early days as a startup and served as counsel in its initial public offering. We continue to represent Amazon in numerous matters today. One example of our corporate venture capital work is our representation of Amazon in its formation of the Alexa Fund in 2015, and in its more than 30 investments in voice recognition startups. Amazon is investing in these startups to develop apps that will use the Alexa/Echo platform.

Public Companies: Corporate Venture Capital

Practice Spotlight

McKESSON

- Represented McKesson Ventures in its Series B Preferred Stock investment in a digital healthcare startup.

 **Microsoft**

- Represented Microsoft Corporation in its investments in Foursquare Labs, Inc. and more than 25 other emerging growth companies.

BLUCORA

- Represented Blucora, Inc. in its preferred equity strategic investment in Series C Preferred Units in ValueAppeal.

First Data.

- Represented First Data Corporation in its preferred equity investments in Mineral Tree and Booker Software.

*Confidential
Client*

- Represented a confidential online retailer in its Series A investment in a food delivery company.

 **LATTICE**
SEMICONDUCTOR.

- Represented Lattice Semiconductor Corporation in a Series A Preferred Stock investment in Tactual Labs Co.

Emerging Companies & Venture Capital

Practice Spotlight

REGISTERED INVESTMENT COMPANIES

We have extensive experience representing registered investment companies, including open-end funds and closed-end funds, as well as BDCs. We routinely represent funds, their investment advisers or their independent board members. We also have the kind of contacts at the SEC and in the investment management industry that allow us to practice at the cutting edge of current developments. One hopes it will never be useful, but each of us has had substantial experience with SEC examinations and, unfortunately, with SEC enforcement cases involving participants in the investment management industry.

Perkins Coie lawyers advise major fund complexes in a variety of matters such as:

- Fund formation and registration
- Regulatory compliance
- Risk management
- Corporate governance
- Fund mergers and acquisitions
- Obtaining exemptive orders, no-action letters and other relief from regulatory agencies
- Negotiating and structuring investments
- Alternative investment strategy compliance

FUND CLIENTS

- Family offices
- Open-end and closed-end funds of all sizes
- Investment advisers
- Independent trustees
- Private equity funds
- Funds of hedge funds
- Offshore subsidiaries
- Borrowing facilities
- Derivatives
- Venture capital funds
- Hedge funds
- Real estate funds
- Search funds
- Distressed funds

Emerging Companies & Venture Capital

Key Differentiators



COLLABORATIVE TEAM

We have a deep and strong command of the corporate aspects and needs of startups and investors and, because of our depth and breadth, are able to engage specialists in key areas such as privacy and security and IP, at a moment's notice.



TRUSTED COUNSEL

Our lawyers inspire deep confidence in clients that any deal we handle will result in efficient legal project management without any issue being overlooked. Clients appreciate and trust our impeccable judgment and intellectual approach.



INDUSTRY FOCUS

We represent VC funds and high-growth, VC-backed companies in fast-moving industry sectors and know that seasoned capabilities, coupled with a deep understanding of the inner-workings of our clients' businesses, constitutes the basis for valuable service.



THOUGHT LEADERSHIP

We have one of the nation's largest and most active technology-oriented business practices with an in-depth focus on emerging technologies, such as wearables, Internet of Things, blockchain technology, unmanned vehicles and virtual reality.

Corporate Practice Bench and Reputation

Practice Spotlight

300+

Corporate Lawyers

150+

M&A Lawyers

50+

Capital Markets
Lawyers

50+

Startups & Venture
Capital Lawyers



Ranked Nationally for
Corporate and M&A Law
Int'l Financial Law Review (2018)



Recommended by Legal500
for Mergers & Acquisitions
Legal500 (2018)



Ranked Tier 1 for Corporate Law,
Venture Capital, and Securities Law
U.S. News—Best Lawyers® (2018)



Ranked Nationally for
Startups & Venture Capital Law
Chambers USA (2018)



Named the Go-To BigLaw Firm
for Silicon Valley Entrepreneurs
JD Journal (2017)



Named a Top 4 Law Firm in Silicon
Valley by Tech Entrepreneurs
Inc. Magazine (2016)



Named a "Leader" Among
Tech-savvy Law Firms
BTI Brand Elite (2016)



Named a Top 20 Corporate Law
Firm in the United States
NYSE Governance Services (2015)

Emerging Companies & Venture Capital

Representative Investor Clients



ANDREESSEN
HOROWITZ



KICKSTARTER



SEQUOIA CAPITAL



Emerging Companies & Venture Capital

Representative Investment Counsel Experience



Benhamou Global Ventures, LLC
Investment in IntelliVision



Bensussen Deutsch &
Associates, Inc.
*Growth Equity Investment
and Recognition by
American Capital Ltd.*



DiNapoli Capital Partners
*Refinancing of
Hotel Teatro, Denver*



Endeavour Capital
Investment in Zoom+

EnhancedCapital

Enhanced Credit Supported
Loan Fund, LP
Investment in BluSky



First Data Corporation
*Preferred Stock Investment in
Booker Software, Inc.*



Javelin Venture Partners
Investment in 3Scale, Inc.



Madrona Venture Group
*Madrona Venture Group, LLC
Preferred Stock Investment in
Envelop VR*



Microsoft Corporation
*Series D Investment in
InsideSales.com*



Pylon Capital LLC
Sale to Bright Market, LLC

Second Avenue Partners

Second Avenue Partners
Investment in Gemshare, Inc.



Simple Finance Technology
Preferred Stock Financing



Voyager Capital
*Preferred Stock Investment
in Patent Navigation, Inc.*



Vulcan Capital Growth Equity LLC
Investment in TrueCar, Inc.



WestRiver Management, LLC
*Formation of WestRiver Equity
Partners, LLC*

Emerging Companies & Venture Capital

Representative Investment Fund Clients

amazon alexa

ANDREESSEN
HOROWITZ

BCV
BENHAMOU GLOBAL VENTURES

edisonpartners

ENDEAVOUR

ENERGY
FOUNDRY

entangled.ventures

EW Essex Woodlands

INNOVATION
ENDEAVORS

JAVELIN
VENTURE PARTNERS

JMC INVESTMENT

Lightspeed

Liquid 2
Ventures

LU+

MADRONA
VENTURE GROUP

NEWGEN
CAPITAL

NEXTfrontier
CAPITAL

S2G
VENTURES

SEQUOIA

SVAngel

start
engine

Triangle Peak
PARTNERS

THE VENTURE REALITY FUND

voyager
CAPITAL

VULCAN
Capital

Emerging Companies & Venture Capital

Ongoing Initiatives and Key Resources

Angel Network

PERKINS COIE ANGEL NETWORK

We created the Perkins Coie Angel Network to help our seed-stage clients get access to a broad angel community. Our proprietary network allows us to efficiently profile active angel investors seeking startup deal flow. We leverage those profiles to connect our startup clients with angels and seed investors who meet their investment criteria.

Le[a]d Better

LE[A]DBETTER

We know that capital is the primary catalyst for business growth. To help women business leaders maximize their company's capital, we are offering qualifying startups that have at least one woman in a senior leadership role a 15% discount off of our standard hourly rates for certain legal services for a limited period of time. We also provide opportunities for leaders to learn and network with startup ecosystem luminaries to help drive business growth.

Startup Percolator

STARTUPPERCOLATOR.COM

In 2012, we launched Startup Percolator, a user-friendly interactive website that enables entrepreneurs to generate the legal documents needed to form a Delaware "C" corporation, free of charge. Startup Percolator also includes a blog with rich, dynamic content and helpful tips to guide companies through the start-up process.

Emerging Companies & Venture Capital

Ongoing Initiatives and Key Resources

AT PERKINS COIE, WE ARE BUILDING THE NEXT-GENERATION TOOLS AND SERVICES TO HELP OUR STARTUP CLIENTS EXPERIENCE GROWTH AS THEY BUILD GREAT COMPANIES.

Our Startup & Investor Services team combines decades of experience with the power of Perkins Coie's network to provide entrepreneurs the resources required to navigate the ever-changing landscape.

VC DEAL FUNNEL

CAPITAL IS NOT ONE-SIZE-FIT-ALL

Our team works to prepare our clients for the process of raising capital and helps them target the right investors. Our goal is to create win-win relationships for our clients and investors.

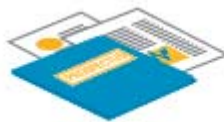


SYSTEMATIC APPROACH TO RAISING CAPITAL

We work with the client before their plan is sent to investors to optimize their fundraising potential. Our group advises clients on these key components:



Business Planning



Pitch Materials



Financing Strategies



Investor Targeting

Emerging Companies & Venture Capital

Le[a]dBetter Program - Supporting Gender Equality in Business Leadership



Women entrepreneurs are majority owners of an estimated 10 million businesses, or, as currently reported by the U.S. Small Business Administration, 36% of all businesses in the United States. Yet, in the U.S., of the 1,186 companies that received Series A funding in 2015, just 6.6% - 79 companies - included a woman on the founding team. - PitchBook

To help make gender equality in business leadership a reality, Perkins Coie proudly launches Le[a]dBetter, an innovative program that supports startups that have women in senior executive roles. Inspired by the Lilly Ledbetter Fair Pay Act of 2009, legislation drafted in response to the Lilly Ledbetter gender wage gap lawsuit, Le[a]dBetter is an innovative educational, networking and alternative fee arrangement program designed to offer support to companies in the startup ecosystem that demonstrate inclusion and business leadership diversity in their executive suite.

We are offering qualifying startups that have at least one woman in a senior leadership role a 15% discount off of our standard hourly rates for certain legal services for a limited period of time. We also offer investors who invest in startups with at least one woman in a senior leadership role a 15% discount off of our hour rates.

To round out the Le[a]dBetter program, we are also providing participants with access to:

- educational seminars developed to help women executives further enhance their leadership and business skills; and
- ongoing opportunities to network with other business leaders.

To learn more, visit www.perkinscoie.com.

