



FENWICK & WEST LLP  
A LIMITED LIABILITY PARTNERSHIP

## FENWICK & WEST LLP

### Trends in Terms of Venture Financings In the San Francisco Bay Area (First Quarter 2006)

- **Background** – We analyzed the terms of venture financings for 101 technology companies headquartered in the San Francisco Bay Area that reported raising money in the first quarter of 2006.
- **Overview**

The results of the 1Q06 survey showed a continuation of the strong positive trend in venture valuations. The highlights of the quarter were as follows:

- Up rounds exceeded down rounds for the ninth quarter in a row, and by the largest margin since our survey began (74% up vs. 15% down, with 11% flat).
- The Fenwick & West Venture Capital Barometer showed a 64% average price increase for companies receiving venture capital in 1Q06 compared to such companies' previous financing round. This was also the largest increase since the survey began.

Other U.S. venture industry related results for the quarter included the following:

- The amount invested by venture capitalists in the U.S. in 1Q06 was approximately \$6 billion, an improvement over \$5.1 billion in 1Q05, and on par with the last 3 quarters of 2005.(1)
- Acquisitions of venture-backed companies in the U.S. in 1Q06 totaled \$7.5 billion in 92 transactions. This was flat with \$7.5 billion in 93 transactions in 1Q05, and with 2005 on the whole, but is a significant improvement over \$4.8 billion in 86 deals in 4Q05. (1)
- There were 13 IPOs of venture-backed companies in the U.S. in 1Q06, of which 8 were healthcare companies. This was an improvement over the 8 IPOs in 1Q05, and generally flat with the last half of 2005. (1)
- Nasdaq was up 6% in 1Q05, but is down 7% in 2Q06 to date.

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

Series	Q1'06	Q4'05	Q3'05	Q2'05	Q1'05	Q4 '04	Q3 '04	Q2 '04
A	11%	22%	18%	15%	24%	18%	14%	17%
B	40%	35%	31%	26%	29%	24%	29%	28%
C	17%	17%	23%	27%	16%	28%	20%	25%
D	15%	11%	15%	21%	22%	18%	20%	15%
E and higher	17%	15%	13%	11%	9%	12%	17%	15%

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

Price Change	Q1'06	Q4'05	Q3'05	Q2'05	Q1'05	Q4 '04	Q3 '04	Q2 '04
Down	15%	19%	25%	31%	31%	28%	32%	21%
Flat	11%	12%	15%	4%	10%	12%	15%	12%
Up	74%	69%	60%	65%	59%	60%	53%	67%

The percentage of down rounds by series were as follows:

Series	Q1'06	Q4'05	Q3'05	Q2'05	Q1'05	Q4 '04	Q3 '04	Q2 '04
B	12%	10%	16%	12%	19%	24%	12%	16%
C	12%	5%	35%	32%	36%	25%	32%	25%
D	27%	46%	33%	37%	30%	28%	52%	18%
E and higher	12%	35%	23%	60%	62%	42%	42%	29%

**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 Q1'06 and is provided on an aggregate basis for comparison purposes for the prior five 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 we have not weighted the results for the amount raised in a financing.

Q1'06

Percent Change	Series B	Series C	Series D	Series E and higher	Combined total for all Series for Q1'06	Combined total for all Series for Q4'05	Combined total for all Series for Q3'05	Combined total for all Series for Q2'05	Combined total for all Series for Q1'05	Combined total for all Series for Q4 '04
Up rounds	+120%	+74%	+80%	+65%	+95%	+81%	+88%	+83%	+66%	+84%
Down rounds	-38%	-47%	-50%	-77%	-49%	-56%	-60%	-43%	-49%	-54%
Net result	+89%	+56%	+35%	+37%	+64%	+45%	+38%	+41%	+24%	+36%

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

Q1'06	Q4'05	Q3'05	Q2'05	Q1'05	Q4 '04	Q3 '04	Q2 '04
40%	41%	57%	46%	50%	46%	54%	56%

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

Series	Q1'06	Q4'05	Q3'05	Q2'05	Q1'05	Q4 '04	Q3 '04	Q2 '04
B	29%	22%	42%	25%	38%	32%	33%	45%
C	47%	40%	48%	40%	57%	39%	59%	50%
D	60%	69%	87%	68%	55%	72%	61%	59%
E and higher	41%	65%	77%	70%	62%	50%	74%	82%

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

Q1'06	Q4'05	Q3'05	Q2'05	Q1'05	Q4 '04	Q3 '04	Q2 '04
14%	24%	30%	22%	12%	24%	31%	25%

Of the senior liquidation preferences, the ranges of the multiples broke down as follows:

Range of multiples	Q1'06	Q4'05	Q3'05	Q2'05	Q1'05	Q4 '04	Q3 '04	Q2 '04
>1x- 2x	80%	67%	93%	88%	100%	89%	75%	84%
>2x – 3x	20%	33%	7%	0%	0%	0%	6%	8%
> 3x	0%	0%	0%	12%	0%	11%	19%	8%

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

Q1'06	Q4'05	Q3'05	Q2'05	Q1'05	Q4 '04	Q3 '04	Q2 '04
65%	64%	70%	71%	73%	60%	74%	64%

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

Q1'06	Q4'05	Q3'05	Q2'05	Q1'05	Q4 '04	Q3 '04	Q2 '04
55	50%	54%	60%	51%	60%	63%	47%

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

Q1'06	Q4'05	Q3'05	Q2'05	Q1'05	Q4 '04	Q3 '04	Q2 '04
3%	4%	3%	4%	9%	9%	9%	6%

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

Type of Provision	Q1'06	Q4'05	Q3'05	Q2'05	Q1'05	Q4 '04	Q3 '04	Q2 '04
Ratchet	4%	9%	7%	8%	9%	9%	14%	9%
Weighted Average	92%	85%	92%	88%	87%	85%	85%	87%
None	4%	6%	1%	4%	4%	6%	1%	4%

- **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.

Q1'06	Q4'05	Q3'05	Q2'05	Q1'05	Q4 '04	Q3 '04	Q2 '04
11%	16%	8%	16%	17%	12%	16%	20%

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.

Q1'06	Q4'05	Q3'05	Q2'05	Q1'05	Q4 '04	Q3 '04	Q2 '04
73%	89%	88%	87%	93%	75%	72%	77%

- Shadow Preferred Stock.

Q1'06	Q4'05	Q3'05	Q2'05	Q1'05	Q4 '04	Q3 '04	Q2 '04
27%	11%	12%	13%	7%	25%	28%	23%

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

Q1'06	Q4'05	Q3'05	Q2'05	Q1'05	Q4 '04	Q3 '04	Q2 '04
27%	31%	32%	29%	30%	28%	30%	28%

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

Q1'06	Q4'05	Q3'05	Q2'05	Q1'05	Q4 '04	Q3 '04	Q2 '04
9%	11%	17%	15%	13%	8%	20%	12%

For additional information about this report please contact Barry Kramer at 650-335-7278; [bkramer@fenwick.com](mailto:bkramer@fenwick.com) or Michael Patrick at 650-335-7273; [mpatrick@fenwick.com](mailto:mpatrick@fenwick.com) at Fenwick & West. To be placed on an email list for future editions of this survey please go to [www.fenwick.com/vctrends.htm](http://www.fenwick.com/vctrends.htm). The contents of this report are not intended, and should not be considered, as legal advice or opinion.

<sup>1</sup> Information in this paragraph obtained from Dow Jones VentureSource.