Private Company Financings Report

Cooley Godward LLP

SEPTEMBER 2006

Executive summary on private company financings through the second quarter of 2006.

The overall investment climate for privately-held startups held steady in the second quarter of 2006, continuing the level of activity that was seen in the first quarter. According to our report, covering 73 venture capital transactions that closed in each of the first and second quarters, company valuations tapered off in early-stage transactions and declined in later stage transactions. Up-round financings, transactions in which the valuation of a company increased relative to the prior round of financing, were at historically high levels, accounting for 85% of all deals in the first and second quarters. The report also found that entrepreneurs continue to strike good deals with investors, as the vast majority of transactions carried a 1x liquidation preference, and a very small percentage contained full ratchet antidilution provisions. For the second quarter, early-stage financings (Series A and B) were an increasing percentage of the deal volume, accounting for 73% of all deals. The report also shows a slight reduction in the amount of money raised on average, likely attributable to the increased percentage of early stage deals.

» See page 2 for our detailed breakdown.

This quarterly report provides a summary of data from the previous six quarters, reflecting Cooley Godward's experience in venture capital financing terms and trends. Information is taken from transactions in which Cooley Godward served as counsel to either the issuing company or the investors.

QUARTERLY FOCUS

Dilution: How Expensive is Venture Capital?

Having compiled data on almost 500 financing transactions over the past two years, we thought it would be interesting to periodically take a closer look at specific trends. One question that entrepreneurs frequently ask is, "How much of the company will I have to give up in a venture financing?" After removing recapitalizations and other unusual transactions that might skew the results, we looked at the median percentage of a company sold in various rounds of financing, reflecting the amount of dilution incurred by existing stockholders after each round. The chart below details our findings.

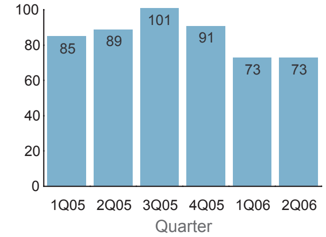
SERIES	A	B	C	LATER
NUMBER DEALS	154	148	65	67
MEDIAN % SOLD	42.9%	37.1%	25.2%	20.9%

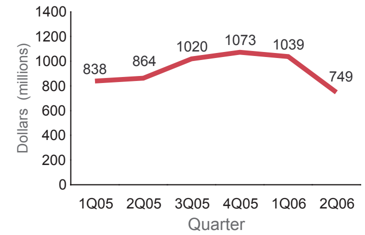
While our data shows a relatively steady increase in valuations over the last two years (with the notable exception of Q1 2006), what has not been clear is whether that resulted in entrepreneurs and early investors retaining more ownership of the company. What the Series A data showed us is that the old "Rule of Three"— a third for the founders, a third for the investors and a third for the option pool — is a thing of the past. If there is a new rule of thumb, it would probably be more like "40-40-20"– 40% for the founders, 40% for the investors and 20% for the option pool.

To better understand the dilution of ownership in Series A financing, we sorted the data based on the date of the closing as well as the size of the financing. . While we did not see any variance in the data when sorted by time period, when sorting by the amount of money raised we found that for those Series A deals where $5 million or more was raised (69 deals), the median dilution was 50%. For those raising below $5 million, the median dilution was only 40% (85 deals).

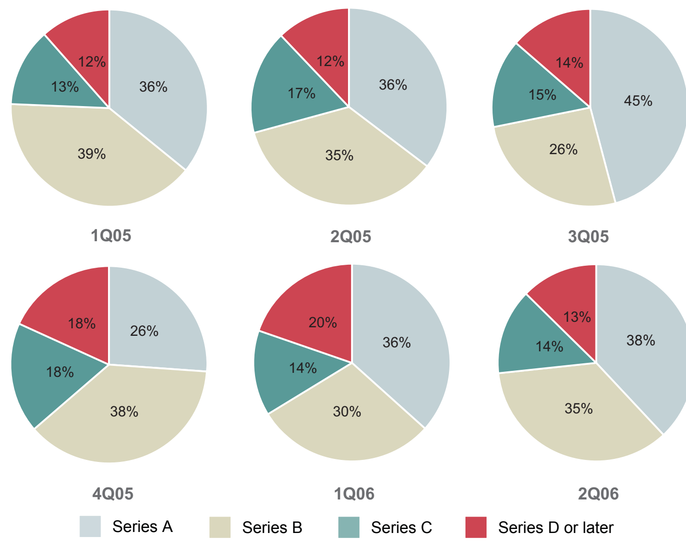
We also looked closely at the Series B data, because it was something of a surprise that the median dilution was still very high at 37%. After sorting the data by time, we found there is a clear downward trend in Series B dilution, with median dilution of 39% two years ago moving down to 34% in the first half of 2006. After sorting the data by the amount raised, the trend was as expected: for deals where $10 million or more was raised, the median dilution was 39%; while for deals where less than $10 million was raised, the median dilution was only 33%.

NUMBER OF DEALS CLOSED—By Quarter. The number of closed transactions in the second quarter, 73, was the same as the first quarter. For the first half of 2006 the total number of closed transactions is down from the same period last year. **AGGREGATE AMOUNT INVESTED (millions $)—By Quarter.** The aggregate amount of money invested fell in the second quarter to $749 million. This drop follows an extended upward trend, and is likely attributable to the increase in the percentage of early stage deals.

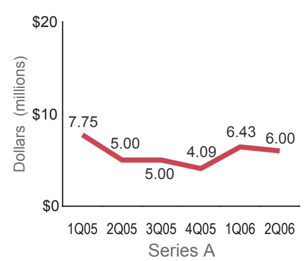


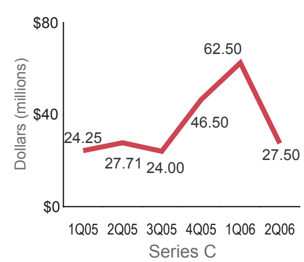


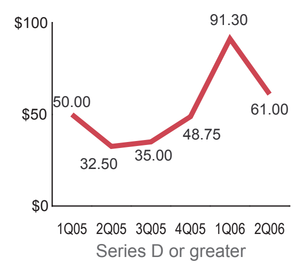
DEAL BREAKDOWN—By Series. The deal breakdown by series showed an increase in Series A and Series B deals in the second quarter relative to the first quarter of 2006 and the fourth quarter of 2005.



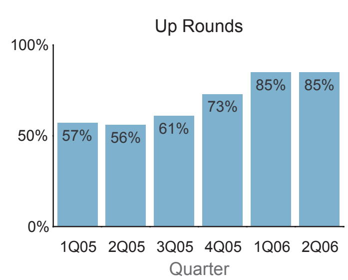
MEDIAN PRE-MONEY VALUATION (millions $)—By Series. Pre-money valuations across all stages of funding were down in the second quarter of 2006 following several quarters of increases. The declines were particularly steep in the later stages of funding, Series C and D.

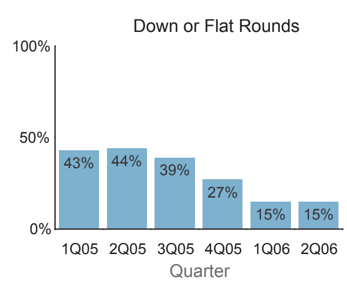




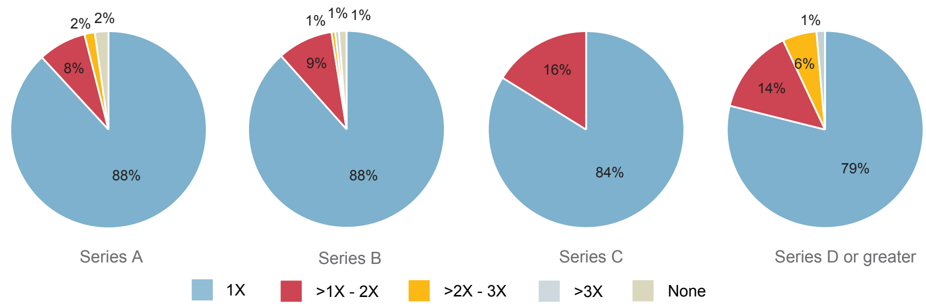


PERCENTAGE OF UP ROUNDS vs. DOWN OR FLAT ROUNDS. The percentage of up-round financings in the second quarter was flat compared to the first quarter, but they remain at historically high levels, showing that existing companies continue to build value for their investors.

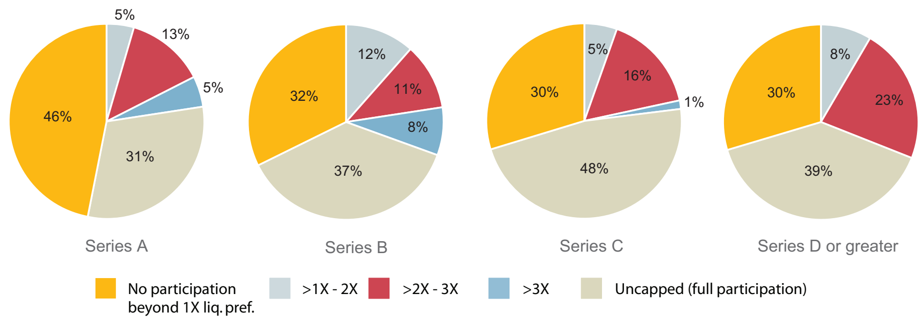




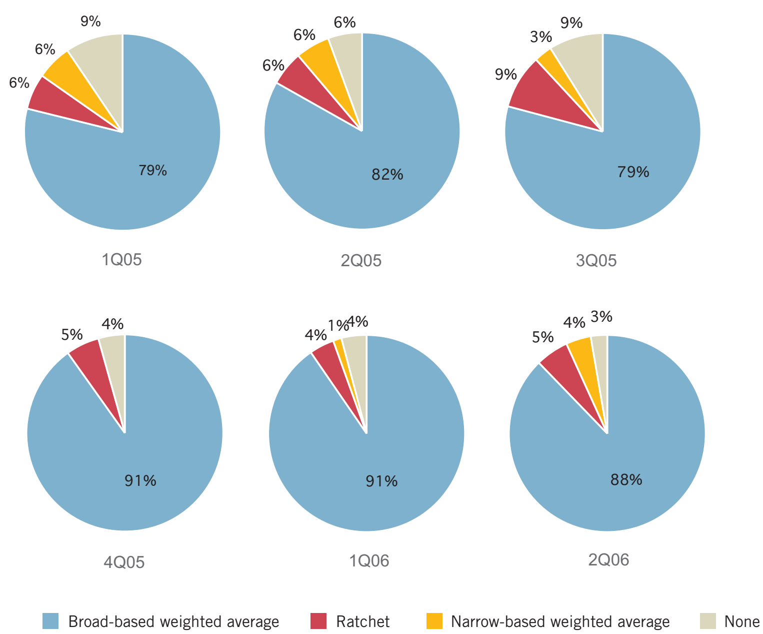
LIQUIDATION PREFERENCES—By Series. The vast majority of all transactions continued to contain a 1X liquidation preference across all stages of financings.



PREFERRED STOCK PARTICIPATION—By Series. The following shows the prevalence of various participation caps at all stages of financing. Early stage Series A financings showed a greater percentage of non-participating preferred terms, demonstrating the relatively strong startup market.



ANTIDILUTION—By Quarter. The following shows the usage of different types of antidilution provisions in each of the last six quarters, with the vast majority remaining broad-based weighted average.



ABOUT COOLEY In 1959, Cooley Godward formed the first institutional venture capital limited partnership in the western United States. Since then we have been at the vanguard of private company financings, both as a representative of hundreds of venture capital and private equity partnerships and as counsel to companies and entrepreneurs raising money from the venture capital community. Industry sectors include all areas common to venture capital financings, including communications, computer hardware and networking, consumer electronics, general retail, Internet, life sciences, semiconductors, and software.

ABOUT THIS REPORT Cooley represented either the company or an investor in each of the transactions covered in this report. *For more information regarding this report, please contact the Cooley attorneys listed below.*

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