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The Next Round and Down Rounds

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Preparing for the Next Round

- Capital formation is a continuous process
- Subsequent to closing a round, begin to think about positioning for next round
- Time between rounds vary depending on investment environment and company progress

Considerations for the "Next Round"

- Milestones/objectives requisite to next round
- Existing investors, new investors or a combination
- Short term cash needs
- Proposed valuation/dilution
- Series A/B 'balance'
- Board seats, charter and investment agreement amendments

The Dreaded "Down Round"

- 2003 Nasdaq fell from 5200 to 1600
- Valuations dropped 95%
- Follow on financings severely impacted
- Down rounds, cram downs, involuntary recaps, and the 'death spiral preferred'
- Litigation occurred due to significant dilution and restrictive covenants

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Market Changes Brought Relief

- Upside performance adjustments
- Carve outs for management/option pools
- Warrants for angels who remained active
- Bonus pools for the management team
- Pay-to-play provisions

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Summary

- It’s never too early to begin thinking about positioning the company for its next round of capital
- Consider investor groups, valuation, additional restrictions, short term bridges
- Down rounds (now) reflect poor performance versus market factors
- Market changes have lessened the negative impact of down rounds