



TERM SHEET
BATTLE
LONDON
-2012-

TERM SHEET BATTLE



AN IMPROVISED MOCK NEGOTIATION OF A SERIES A FINANCING

THE CAST

Jens Lapinski

Jason Ball

Tina Baker

Brad Furber

THE CHARACTERS

Jens - Co-Founder & CEO, Gaming Solutions IQ, Inc.

Jason - General Partner of Ravenous Ventures IV, L.P.

Tina- Partner, Schwartz & Shields LLP

Brad – Referee



SETTING THE STAGE/BACKGROUND

Gaming Solutions IQ, Inc. ("GSIQ") was co-founded by three European entrepreneurs, Jens (a UK citizen), Simon (a Dutch citizen) and Lone (a Danish citizen) in October, 2010. GSIQ is creating a collection of localized cross-platform portals that form the core of an online and mobile game community, and provides solutions to advertisers and publishers to target, connect with and acquire users and customers among such gaming audiences. There are at least three other relatively early stage competitors with similar business models, two of which are already backed by sophisticated venture investors. To date, GSIQ has been able to bootstrap and angel finance (£ 150K) its way to building a community currently approaching 250,000 members.

GSIQ was originally organized as a private limited liability company (BV) under Dutch law, but it reorganized its top level entity as a Delaware corporation in January 2012 shortly after it was accepted and enrolled into the Spring 2012 program of a Tech All Stars accelerator ("TASA"). The three co-founders of GSIQ each own 700,000 shares of common stock. Marnix, a Dutch angel investor and entrepreneur, purchased 360,000 shares of common stock of GSIQ for £ 150K in February 2012. TASA owns 240,000 shares of common stock. Options to purchase an additional 300,000 shares of common stock have been granted to individuals who have joined the GSIQ team as employees, contractors, consultants and advisors since its inception.

GSIQ participated in the TASA Investor Day program in mid May 2011. Jason, a General Partner of Ravenous Ventures IV, L.P. ("Rave"), the European arm of a venture capital firm headquartered in Silicon Valley with over US\$1.5B in assets under management, attended the TASA Investor Day and was impressed enough by the GSIQ pitch that he invited the GSIQ team to make a presentation to his firm in late-May 2012. GSIQ management let it be known that GSIQ would be very pleased to sell a 20% equity stake in exchange for £ 750K, and management was also confident that with that amount of equity at its disposal GSIQ could achieve the following milestones within twelve months or less: (i) community over 1,000,000 members, (ii) revenue over £ 150K/month, and (iii) gross profit over £ 10K/month. After several follow-up meetings with GSIQ management and considerable market due diligence, Rave delivered to GSIQ on Friday, June 15, 2012, a proposed Term Sheet to lead a Series A financing, a copy of which is incorporated into this Playbill.

Rave has engaged Roger, a partner in Dewey Cheatem & Howe LLP, a global law firm that represents dozens of venture capital firms doing business in the USA and Europe, to draft the Series A Term Sheet and definitive documents contemplated thereby, perform legal due diligence, and provide such other legal services as may be necessary and appropriate to negotiate and close the proposed Series A financing.

GSIQ has engaged Tina, a well known startup and emerging growth company lawyer based in the London office of Schwartz & Shields LLP, a mid-size law firm with offices in major financial and tech centers in the USA and Europe. Tina has reviewed the proposed Series A Term Sheet, and provided her initial written comments and feedback thereon to GSIQ's Board of Directors.



Jens, the CEO of GSIQ, has requested a meeting with Jason on June 20, 2012, to discuss the proposed Series A Term Sheet. Jens has asked Tina to attend the meeting as counsel to GSIQ. Jason normally prefers that the first meeting between him and the CEO of a prospective portfolio company be among principals only (no lawyers), with a view towards enabling him to explain the purposes and intent of the various proposed terms and conditions, with ample time for questions and answers without concern for the meter/billable hours. Never having raised VC financing before, Jens does not understand a lot of language and "legalese" contained in Rave's proposed term sheet, and he believes that he will be more comfortable and effective at the meeting if Tina is by his side as counsel to GSIQ. Jason has many years of experience negotiating term sheets and the various legal agreements contemplated thereby, and to avoid racking up more legal fees at this point in the deal process, he opts to attend the meeting without Roger's participation.

TALKING POINTS

Jens and Tina have a number of questions regarding the proposed Term Sheet. Tina and Jens suggest that in their experience, meetings of this sort are most efficient and productive if the parties can first identify the main questions and potential points of contention.

ECONOMIC ISSUES

1. Price
 - A. Pre- and Post-Money Valuation. GSIQ was asking for £3M in pre-money valuation, and Rave is meeting that request. GSIQ is asking for £3.75M post-money valuation, and Rave is offering £3.75M (1st Closing) and £4.5M (2nd Closing).
 - B. Equity Dilution: GSIQ is asking for 20%. Rave is offering 20% (1st Closing) and 33% (2nd Closing).
 - C. Questions/Issues: What is the purpose of Rave's proposal to create a tranching financing? Is the 2nd Closing a "call" (i.e., "mandatory" at the option of GSIQ) or an "option" ("discretionary" at the option of Rave)? Who decides if milestones have been achieved?
2. Liquidation Preference
 - A. Why is there a 2X liquidation preference? How does that work in operation?
 - B. What is the rationale behind a term that gives Rave both a liquidation preference, first, and full participation rights on an as-converted basis, second? Isn't that getting two bites at the apple? Is that fair?
 - C. What is "market"? Are "market" terms different in UK vs Continental Europe vs USA?
3. Vesting/Reverse Vesting on Founders Stock and Options
 - A. If the founders' stock has already been issued, then why would VC, angel and/or *co-founders* want "reverse vesting" (i.e., buyback rights)? Is it "fair"?
 - B. What is "market" in terms of reverse vesting on founders stock. What are the tax consequences? Who could/should incur the tax risks/expenses?
 - C. What is "market" for vesting on forward-looking option grants?



- D. Is there a big difference in what is "market" between UK vs Continental Europe vs USA?
- E. What about acceleration provisions in the event of M&A? What is the difference between a "single trigger" and "double trigger" acceleration provision?

4. Option Pool

- A. How much is "enough"? For how long a period is it intended to last?
- B. How does size of unallocated option pool affect pre- and post-money valuation?

5. Anti-dilution Formula

- A. What is the difference between "full ratchet" and "weighted average" antidilution formulas? What is difference between "broad-based" and "narrow-based" weighted average antidilution formulas?
- B. What is "market"?
- C. Are there differences between UK vs Continental Europe vs USA?
- D. Is this solely an "economic" issue, or is this also a "control/voting" issue?

CONTROL ISSUES

1. Composition and Election of Board of Directors

- A. What is the "right" number of directors for an early stage company – 3, 4 or 5?
- B. If common holders have right to elect one (or two) directors, and Series A holders have right to elect one (or two) directors, then how is the third (or fifth) director selected (i.e., by mutual consent of other directors, or by vote of all shareholders as a single class, or what)?
- C. Should one board seat automatically go to the CEO?
- D. Are there differences between UK vs Continental Europe vs USA in terms of standard board composition and corporate governance?
- E. What about board observers – is that a good idea or common practice?
- F. How are inside and outside directors generally compensated?

2. Protective Provisions

- A. Why should investors get the right to veto certain actions?
- B. Are protective provisions/veto rights generally meant to restrict or intrude into operations or ordinary course of business matters?
- C. What is "market"?
- D. What about using "materiality" qualifiers?
- E. What about use of "belt and suspenders" protective provisions – at both the board level (Series A board designee), and shareholder level?
- F. When should these protection provisions terminate?

3. Drag-Along Rights

- A. Why and when should the preferred stock holders (in this case a minority of the voting stock) be able to force a sale of the company?
- B. How might founders and management be adversely impacted, and what alternatives exist as protection?
- C. What is "market"?



D. Are there differences between UK vs Continental Europe vs USA (and even in USA, among different states/coasts) in terms frequency and structure of drag-along rights?

4. Redemption Rights

- A. What is the rationale for redemption rights?
- B. Are there any traps for the unwary, such as adverse change provisions or mandatory features that create accounting and balance sheet issues?
- C. What is market?

5. Right of First Refusal/Right of Co-Sale

- A. How has the emergence of private secondary markets changed standard terms and conditions for this once universally accepted agreement?
- B. If it's good for the geese (the common holders), should it be good for the ganders (the preferred holders) too?
- C. What is market?

6. No Shop/Confidentiality

- A. What is the rationale for shutting down the dating process?
- B. Would a simple nonsolicitation be good enough instead?
- C. How long is "long enough" and should obligations terminate immediately if the VC terminates the process?
- D. Should acquisitions be carved out?

TO FOLLOW-UP WITH CAST MEMBERS

THE CAST	EMAIL ADDRESSES
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