

Generic Term Sheet

The following outlines the terms of a proposed investment in ABC Corporation (the "Company") by certain investors (individually an "Investor" and collectively the "Investors").

Offering	A minimum of \$1,000,000 and a maximum of \$2,000,000 of new money.
Type of Security	Series A Convertible Preferred Stock ("Series A").
Price Per Share	\$0.50 per share.
Current Outstanding Securities	8,000,000 shares of fully diluted Common Stock equivalents, which includes 2,000,000 new unallocated stock options.
Valuation	Pre-money valuation of \$4,000,000.
Investors	Lead Investor \$500,000 Other investor(s) up to \$1,500,000
Date of Closing	The initial closing is to occur on or before [Insert_Date] (the "First Closing"). A second closing may take place at any time within 90 days of the First Closing (the "Final Closing").
Note Conversion	The existing convertible notes in the aggregate principal amount of \$360,000 plus interest will be converted into Series A at the First Closing.
Conditions of Closing	The Closing is subject to the following conditions: <ol style="list-style-type: none">The satisfactory completion of customary due diligence.The satisfactory review by the Investors of all relevant documents.Negotiation and execution of a definitive agreement, with standard representations and warranties, and other related documents.Other conditions of closing customary for transactions of this nature.
Use of Proceeds	All invested capital is to be used for working capital.
Board Composition	Following the First Closing, the Board will consist of five (5) directors. Two (2) Directors will represent Series A investors, one of whom shall initially be [Insert Name], two (2) Directors will represent the Common stockholders, one of whom shall initially be the CEO of the Company, and one (1) Director will be an independent Director, who shall be unanimously approved by the other Directors. At least one Series A Director will be a member of all committees of the Company's Board of Directors.
Rights, Preferences, Privileges and	1. Dividends. <ol style="list-style-type: none">No dividends will be paid on Common Stock unless

Comment [MSOffice1]: First and Final Closing logic is often used to keep the round open. If there is only one closing (actually more common), then change this language appropriately.

Comment [MSOffice2]: Include this if convertible debt exists that will convert into this security.

Restrictions of Series A Stock

equivalent dividends are paid on the Series A on an as-converted basis.

- b. No other securities shall be entitled to dividends while the Series A are issued and outstanding without the prior written consent of the majority of the Series A.
- c. Upon any voluntary or mandatory conversion of any Series A, all declared but unpaid dividends on the shares converted will be immediately due and payable in cash.

2. Liquidation Preference.

- a. In the event of any liquidation, dissolution or winding up of the Company, the Investors shall be entitled to liquidation preference equal to the investment price paid for the Series A, plus unpaid dividends, if any, prior to the distribution of any proceeds to the holders of Common Stock.
- b. Any assets remaining after such preferential distribution and any liquidation preference payment made to other Company stockholders that have liquidation preference over Common Stock will be distributed to all stockholders, including the Investors, pro rata on an as-converted basis.

3. Treatment on Reorganizations, Consolidations, Mergers and Sales of Assets. In any reorganization, consolidation or merger which results in the shareholders of all classes of stock of the Company owning less than 50% of the outstanding voting power of the surviving corporation or the sale of all or substantially all of the Company's assets, such an occurrence shall be treated as a liquidation, dissolution or winding up, unless the holders of a majority of the Series A vote otherwise.

4. Optional Conversion. Initially, the Series A will be convertible into Common Stock at a ratio of one share of Common Stock for each share of Series A. All shares of Series A will convert to Common Stock upon the vote of holders of a majority of the then outstanding shares of Series A, voting together as a single class.

5. Automatic Conversion. All shares of Series A will automatically convert to Common Stock upon a firm commitment underwritten public offering of Common Stock of the Company at a price per share equal to at least five (5) times the price paid by the Investors with gross proceeds at least \$25,000,000 (a "Qualified IPO").

6. Antidilution and Adjustment Provisions.

- a. The conversion ratio of the Series A will be subject to a weighted average ratchet antidilution adjustment in the event that the Company issues additional shares (other than under the option pool described above, upon conversion of Series A, in connection with equipment

Comment [MSOffice3]: This represents standard (or 1x) participating preferred.

or other leases, in connection with an acquisition, or in connection with a stock dividend, split or like event) at a purchase price less than the then applicable conversion price of the Series A.

- b. The conversion price will be adjusted for Common Stock splits, stock dividends and other Common Stock recapitalizations.
7. **Voting Rights.** Except as is provided in paragraph 8 below, the Series A will vote with the Common Stock as one class on an as-converted basis.
 8. **Protective Provisions.** For so long as 25% of the Series A remain outstanding remain outstanding, consent of the holders of a majority of the Series A will be required for any action which:
 - a. Materially alters or affects the rights, preferences or privileges of the Series A.
 - b. Increases or decreases the authorized number of shares of Series A.
 - c. Creates or issues any series or class of shares having a preference or priority equal or senior to the Series A as to the payment of dividends or liquidation, or having redemption rights, registration rights or antidilution protection equal or senior to the Series A.
 - d. Declares or pays any dividend on Common Stock (other than stock dividends).
 - e. Results in the sale, conveyance, or other disposition or encumbrance of all or substantially all of the Company's property or business or a merger or other similar transaction in which 50% or more of the voting power of the Company is transferred.

Comment [MSOffice4]: This is actually a pretty light set of protective provisions. Larger funds would probably have a list with 3-4 times as many items. For example, approval of the company taking on debt over a certain amount ...

Business Plan

The Company will prepare an annual business plan, with financial projections (operating budget), for Board approval, no later than 30 days prior to the beginning of each fiscal year.

Information Rights

The Company will provide to each holder of Series A:

- a. Quarterly, within 30 days after quarter-end, the President will provide the Investors with a brief report (1-2 pages) describing important operational activities during the prior quarter and indicating whether the Company is, or is not, in compliance with this and other major agreements, and discussing variances from budget.
- b. Yearly, at the option of the Investors, within 90 days after year-end, the Company will provide the Investors with an audit from the Company's auditors and a statement from the chief financial officer (or upon request of Investors, the Company's auditors)

regarding compliance with the terms of any financing agreements.

Registration Rights

1. **Demand Rights.** At any time after six months after the Company's first registration statement for a public offering of its shares of common stock, a majority of the Investors may require that the Company file a registration statement for at least 25% of their Series A shares (or any lesser percentage if the aggregate offering price to the public would exceed \$1 million) and the Company will use its best efforts to cause such shares to be registered. The Company will not be obligated to make more than two (2) registrations under this demand right. If the registration is withdrawn at the request of the Investors, it does not count toward the two (2) demand rights.
2. **S-3 Demand Rights.** If available for use by the Company, upon the vote of a majority of the Investors, they will be entitled to unlimited S-3 registrations, provided the aggregate offering price is in excess of one million dollars (\$1,000,000), subject to a ninety (90) day, not to exceed one hundred fifty (150) days, deferral by the Company. No more than one S-3 registration right may be exercised in any twelve (12) month period.
3. **Piggyback Rights.** The Investors will be entitled to unlimited "piggyback" registration rights on registrations of the Company except for the Company's IPO.
4. **Underwriter Cutbacks.** All piggyback registration rights will be subject to underwriter cutbacks, with shares being registered subject to the following priorities:
 - a. All holders of registration rights pro rata based on share ownership.
 - b. All Company shares.
 - c. All other shareholders.
5. **Expenses of Registration.** The expenses of the registrations (exclusive of underwriting discounts and commissions) set forth in the above paragraphs will be borne by the Company.
6. **Transfer Rights.** The Investors all have the right to transfer the registration rights to a subsequent owner of the Series A.
7. **Selection of Underwriter.** The Company may select any underwriter for the purpose of any offering contemplated herein, subject to the approval of the Investors, which approval will not be unreasonably withheld.
8. **Termination of Rights.** All registration rights will terminate for an Investor when at least one of the following is true:
 - a. All of the Investor's shares may be sold during a single three-month period under Rule 144.
 - b. All of the Investor's shares may be transferred under Rule 144(k).

The Company will not grant registration rights to any other person

that are superior to the foregoing registration rights. The Company will not grant registration rights to any other person that are of equal priority to the foregoing registration rights without the consent of the holders of a majority of the Converted Stock and Series A Stock, together on an as-converted basis.

Comment [MSOffice5]: This last paragraph is probably not all that typical, but we usually put it in to ensure that we keep substantially the same registration rights as later investors, if those later investors negotiate more investor friendly registration rights.

Right of First Refusal

In the event that any of the existing shareholders, managers, employees or other shareholders propose to sell or transfer to a third party or parties (other than to affiliates or for estate planning purposes) a number of shares of their stock, then the stock to be sold will first be offered to the Company to purchase the shares on the same terms as the third-party offer. If the Company does not purchase all of the available shares, then the investors have the right to purchase the remaining shares on a pro rata basis at the same terms. If the investors and the Company do not purchase all of the shares, then they may be offered to the third party. Future issuances of capital stock will be subject to similar rights of first refusal until the occurrence of a Qualified IPO.

Transfer Rights

The Series A Stock will be transferable from time to time and at any time with all rights pertaining thereto, in whole or in part, consistent with applicable securities laws.

Preemptive Rights

If the Company proposes to offer any securities (other than securities issuable upon conversion of Series A, securities issued in connection with the acquisition of another entity, restricted stock or options issued to employees, consultants or directors of the Company, securities issued pursuant to any stock dividend, split or the like event, or warrants issued in connection with a debt financing, strategic relationship or equipment or other lease), the investors will have the right to maintain their pro-rata ownership (on a fully converted, fully diluted basis) of the Company. Preemptive Rights will terminate upon a Qualified IPO.

Co-Sale Rights

Holders of Series A will have the right to participate on a pro-rata basis in any sale of shares by the Company founders on the same terms and conditions being offered to the Company founders (other than transfers to affiliates for estate planning purposes).

Redemption Rights

On the fifth anniversary of the First Closing, the holders of a majority of the Series A will have the right to require the Company to redeem the Series A at a redemption price equal to the greater of (i) the initial purchase price of the Series A plus declared but unpaid dividends, if any, or (ii) the fair market value of the Series A stock.

Invention, Non-Disclosure and Non-Competition Agreements

All key employees and consultants shall have executed Invention, Non-Disclosure and Non-Competition Agreements, the form of which shall be reasonably acceptable to the investors.

Right of Inspection

The investors shall have the right to inspect books and records, contracts and agreements during normal business hours.

Expenses

The Company will pay the reasonable and documented fees of the Investors' legal counsel, not to exceed **\$20,000**, plus actual out of pocket expenses, if any.

Governing Law

Delaware law will govern the Transaction Documents, including corporate documents of the Company.