

Dear Clients and Friends,

Re: **Survey On Legal Terms of Venture Capital Transactions – First Half of 2006**

We are pleased to present the results of our survey for the first half of 2006, analyzing the legal terms commonly used in venture capital financings in Israeli and “Israeli related” hi-tech companies and comparing these terms to those commonly used in the Silicon Valley, United States.

This survey is presented this time on a six-month period basis for the periods surveyed, without rolling one quarter forward, and provides an analysis of the legal terms of venture capital transactions closed during the first half of 2006, as compared with the results covered by our earlier surveys on a half-year basis.

In preparing our survey for the first half of 2006, we examined the terms of 57 venture capital financings of Israeli and “Israeli-related” hi-tech companies, each for an investment amount of no less than US \$500,000. The survey included only equity transactions in which venture capital funds participated, and not bridge loan transactions or investments made solely by “angels”.

The number of surveyed Israeli transactions constitutes approximately 60% of the relevant transactions that closed during the covered period and that met our qualifying criteria, and includes a majority of the more significant transactions in terms of funds invested.

As always, this survey was produced in coordination with Fenwick & West LLP., a leading Silicon Valley law firm. Our cooperation with Fenwick & West in producing this survey has enabled us also to present to you their corresponding survey covering Silicon Valley venture financings during the covered period, and thus to draw an interesting comparison between the terms commonly used in Israel and those commonly used in the Silicon Valley.

With respect to the interesting issue of round valuations, which is commonly thought to demonstrate the current atmosphere in the venture capital industry, it appears that **the number of up-rounds continues to outnumber the number of down-rounds for the fifth consecutive time since the beginning of 2004!** In this respect, it should be noted that the results of the survey indicate that up-rounds constitute a relatively high majority equaling two-thirds of all of the investment rounds which were surveyed for a rather lengthy period, since the beginning of May 2005.

With respect to distribution preferences granted to investors – Alongside the increase of the use of participation rights for preferred shares in distributions upon “exits” and liquidations which returned and increased to levels previously surveyed, from 85% in the previous half-year period to 93% in the current half-year period, the use of interest provisions or cumulative dividends that are to be paid to investors as preferential payments in distributions, decreased from 78% in the parallel period in 2005 and from 68% in the previous half-year period to 56% in the half-year period surveyed in this survey, and the use of multiple liquidation preference provisions dropped from 18% in the second half of 2005 to 9% in the half-year period surveyed in this survey.

SHIBOLETH

עורכי דין ונוטריונים ADVOCATES & NOTARIES

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In addition, use of redemption provisions decreased in rounds surveyed in this survey in comparison to their use in previous surveys.

In comparison to the results found in the survey of the Silicon Valley for the first half of 2006, it appears that in Israeli transactions, investors continue to make broader use of senior liquidation preferences (80% in Israel in comparison to 45% in the Silicon Valley), interest provisions or cumulative dividends that are to be paid to investors as preferential payments in distribution (56% in Israel in comparison to 5% in the Silicon Valley), participation rights (93% in Israel in comparison to 68% in the Silicon Valley) and full ratchet anti dilution protection (28% in Israel in comparison to 3% in the Silicon Valley).

We hope that you find this survey useful and interesting. **To be placed on an email list for future editions of this survey, please go to www.shibolet.com.**

To receive a copy of the Fenwick & West Venture Capital Survey summarizing venture capital terms in the Silicon Valley, please go to www.fenwick.com/vctrends.htm.

For additional information about this report, please contact Mr. Lior Aviram at L.Aviram@shibolet.com or Ms. Limor Peled at L.Peled@shibolet.com, Tel: +972 (3) 7778333.



**SHIBOLETH
in cooperation with
FENWICK & WEST LLP**

**Trends in Legal Terms in Venture Financings
in Israel
(First Half of 2006)**

- **Background** – We have analyzed the terms of venture financings for 57 Israeli and Israeli-related technology companies that reported raising money in the first half of 2006. Our survey does not include financing rounds of less than US \$500,000. The tables below also show, for purposes of comparison, the results of our previously released surveys.
- **Financing Round** – The financings closed in the first half of 2006 and in the periods covered by our previous surveys may be broken down by types of round, or series, as follows:

Series	H1'06	H2'05	H1'05	H2'04	H1'04	H2'03
A	21%	34%	28%	35%	20%	22%
B	28%	27%	22%	21%	36%	30%
C	19%	12%	26%	25%	26%	22%
D	19%	17%	9%	11%	8%	19%
E and higher	13%	10%	15%	8%	10%	7%

- **Price Change** – The financings closed in the first half of 2006 and in the periods covered by our previous surveys may be broken down by the directions of the change in price as compared to each company's respective previous round, as follows:

Price Change	H1'06	H2'05	H1'05	H2'04	H1'04	H2'03
Down	26%	30%	19%	43%	42%	62%
Flat	9%	4%	16%	12%	3%	28%
Up	65%	66%	65%	45%	55%	10%

The percentages of financing transactions that were down-rounds, broken down by series, were as follows:

Series	H1'06	H2'05	H1'05	H2'04	H1'04	H2'03
B	31%	36%	0%	25%	24%	73%
C	27%	20%	33%	56%	62%	55%
D	18%	29%	25%	43%	0%	56%
E and higher	14%	25%	14%	40%	80%	50%

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

H1'06	H2'05	H1'05	H2'04	H1'04	H2'03
80%	81%	76%	80%	78%	82%

The percentages of financing transactions with senior liquidation preference, broken down by series, were as follows:

Series	H1'06	H2'05	H1'05	H2'04	H1'04	H2'03
B	75%	73%	80%	85%	61%	82%
C	73%	100%	75%	75%	92%	75%
D	91%	71%	75%	71%	75%	82%
E and higher	86%	100%	71%	100%	100%	100%

- **Multiple-Based Liquidation Preferences** - The percentage of financing transactions with senior liquidation preferences that included multiple preferences was as follows:

H1'06	H2'05	H1'05	H2'04	H1'04	H2'03
9%	18%	16%	24%	23%	44%

Of the financings in which there were senior liquidation preferences based on multiples, the range of the multiples may be broken down as follows:

Range of multiples	H1'06	H2'05	H1'05	H2'04	H1'04	H2'03
>1x- 2x	100%	75%	25%	88%	100%	88%
>2x - 3x	0%	0%	75%	0%	0%	6%
> 3x	0%	25%	0%	12%	0%	6%

- **Participation in Liquidation** - The percentage of transactions, out of the total number of financing transactions, which included participation rights in liquidation were as follows:

H1'06	H2'05	H1'05	H2'04	H1'04	H2'03
93%	85%	91%	79%	90%	91%

Out of those financing transactions the terms of which provided for participation, the percentages of those in which no cap was placed on the investors right to participation were as follows:

H1'06	H2'05	H1'05	H2'04	H1'04	H2'03
57%	57%	69%	60%	67%	59%

- **Cumulative Dividends and/or Accrued Interest as Part of the Liquidation Preference** – Cumulative dividends and/or accrued interest constituted part of the liquidation preferences in the following percentages of financings:

H1'06	H2'05	H1'05	H2'04	H1'04	H2'03
56%	68%	78%	52%	62%	54%

- **Anti-dilution Provisions** - The use of anti-dilution provisions in the financings which took place in the first half of 2006 and in the periods covered by our previous surveys may be broken down as follows:

Type of Provision	H1'06	H2'05	H1'05	H2'04	H1'04	H2'03
Full Ratchet	28%	39%	31%	30%	28%	38%
Weighted Average	65%	61%	65%	64%	66%	55%
None	7%	0%	4%	6%	6%	7%

- **Pay-to-Play Provisions** - The use of pay-to-play provisions in the financings which took place in the first half of 2006 and in the periods covered by our previous surveys may be broken down as follows:

H1'06	H2'05	H1'05	H2'04	H1'04	H2'03
9%	15%	0%	13%	14%	9%

- **Redemption** – The percentage of transactions in the first half of 2006 and the periods covered by our previous surveys, out of the total number of financings in each respective period, in which the terms provided for mandatory redemption or redemption at the option of the venture capitalist was as follows:

H1'06	H2'05	H1'05	H2'04	H1'04	H2'03
14%	20%	17%	21%	26%	27%

- **Corporate Reorganizations** – The percentage of post-Series A financing transactions in the first half of 2006 and the periods covered by our previous surveys, out of the total number of financings in each respective period, which involved the conversion of senior securities into more junior securities was as follows:

H1'06	H2'05	H1'05	H2'04	H1'04	H2'03
2%	2%	7%	2%	10%	14%

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Analysis of Legal Terms of Venture Financings of Israeli Companies and a Comparison of Those Terms with the Terms of Venture Financings in the Silicon Valley (First Half of 2006)

- **Background** – We have analyzed the terms of venture financings for 57 Israeli based/related technology companies that reported raising at least \$500,000 in the first half of 2006, and compared those terms to the terms of venture financings for 191 technology companies headquartered in the Silicon Valley (the San Francisco Bay Area) that reported raising money in the same period.
- **Financing Round** – The Israeli financings may be broken down according to type of round as follows:
 Series A – 21% (compared to 13% in the Silicon Valley)
 Series B – 28% (compared to 38% in the Silicon Valley)
 Series C – 19% (compared to 22% in the Silicon Valley)
 Series D – 19% (compared to 15% in the Silicon Valley)
 Series E and higher – 13% (compared to 12% in the Silicon Valley)
- **Price Change** – The financings during the first half of 2006 may be broken down by the directions of the change in price as compared to the each company's respective previous round, as follows:

Price Change	Israel	Silicon Valley
Down	26%	19%
Flat	9%	9%
Up	65%	72%

The percentages of financing transactions that were down-rounds, broken down by series, were as follows:

Series	Israel	Silicon Valley
B	31%	14%
C	27%	24%
D	18%	21%
E and higher	14%	25%

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

Israel	Silicon Valley
80%	45%

The percentages of financing transactions senior liquidation preference, broken down by series, were as follows:

Series	Israel	Silicon Valley
B	75%	32%
C	73%	64%
D	91%	48%
E and higher	86%	46%

- **Multiple-Based Liquidation Preference** –The percentages of financing transactions with senior liquidation preferences that included multiple preferences was as follows:

Israel	Silicon Valley
9%	15%

Of the financings in which there were senior liquidation preferences based on multiples, the range of the multiples may be broken down as follows:

Range of Multiples	Israel	Silicon Valley
>1x - 2x	100%	80%
>2x - 3x	0%	10%
>3x	0%	10%

- **Participation in Liquidation** –The percentage of transactions, out of the total number of financing transactions, that provided for participation rights in liquidation were as follows:

Israel	Silicon Valley
93%	68%

Out of those financing transactions the terms of which provided for participation, the percentages of those in which no cap was placed on the investors right to participation were as follows:

Israel	Silicon Valley
57%	59%

- **Cumulative Dividends/Interest Accrual** – Cumulative dividends or interest accruals (which is an Israeli concept similar to cumulative dividends) constituted part of the liquidation preferences under the terms of the following percentages of financings:

Israel	Silicon Valley
56%	5%

- **Anti-dilution Provisions** – The use of anti-dilution provisions in the financings were as follows:

Type of Provision	Israel	Silicon Valley
Full Ratchet	28%	3%
Weighted Average	65%	94%
None	7%	3%

- **Pay-to-Play Provisions** – The use of pay-to-play provisions in the financings was as follows:

Israel	Silicon Valley
9%	13%

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

Israel	Silicon Valley
14%	30%

- **Corporate Reorganizations** – The percentages of post-Series A financings involving a corporate reorganization (conversion of senior securities) were as follows:

Israel	Silicon Valley
2%	10%

For additional information about this report please contact Barry Kramer at 650-335-7278; bkramer@fenwick.com or Michael Patrick at 650-335-7273; mpatrick@fenwick.com at Fenwick & West; or Lior Aviram – laviram@shibolet.com or Limor Peled – lpeled@shibolet.com, at SHIBOLETH 972-3-7778333. To be placed on an email list for future editions of this survey please go to www.fenwick.com/vctrends.htm or to www.shibolet.com.