

Dear Clients and Friends,

Re: **Survey On Legal Terms In Capital Venture Transactions – Fourth Quarter of 2005/First Quarter of 2006**

We are pleased to present the results of our survey for the fourth quarter of 2005/first quarter 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 used in the Silicon Valley, United States.

This survey relates to a six-month period, rolling one quarter forward in comparison to our previous survey, and provides an analysis of the legal terms of venture capital transactions closed during the fourth quarter of 2005 and the first quarter of 2006, as compared with those of similar transactions closed during the periods covered by our earlier surveys.

In preparing our survey for the fourth quarter of 2005/first quarter of 2006, we examined the terms of 53 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 over 50% of the relevant Israeli venture financings that closed during the covered period and met our qualifying criteria, and includes a majority of the most 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 practiced in Israel and those used in the Silicon Valley.

The most interesting and noticeable result of the survey is that **the number of up-rounds continued to increase, constituting more than 70%** of all of the surveyed investment rounds in the current survey – the highest percentage for all periods surveyed by us since the third quarter of 2003! It is important to note that the aforementioned result is consistent with the situation in the Silicon Valley – where the number of up-rounds also increased to over 70% of the surveyed investment rounds.

Alongside this increase of up-rounds, we witnessed a **decrease in the number of down-rounds** of the surveyed investment rounds from 30% in the second half 2005 to 23% in the current survey. The aforementioned result is also consistent with the trend in the Silicon Valley, and, with respect to both surveys, these results represent the **largest gap between up-rounds and down-rounds in comparison to all other periods that have been surveyed.**

# SHIBOLETH

עורכי דין ונוטריונים ADVOCATES & NOTARIES

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In addition, with respect to other terms, the survey results indicated some “softening” with respect to certain investors’ protective provisions – The use of weighted average anti dilution protection increased while the use of full ratchet anti dilution protection decreased – this survey indicated that 68% of the surveyed investment rounds provided weighted average anti dilution protection and 28% provided full ratchet anti dilution protection, as opposed to the results of 61% and 29%, respectively, from the second half of 2005.

The same trend was evidenced in the use of interest provisions or cumulative dividends calculated as a rate of the investment amount, thus allowing investors to receive additional returns on their investment, which continued to decrease to 60%, and was also evidenced in the use of multiple liquidation preference provisions which dropped from 18% in the second half of 2005 to 10% in the period surveyed in this survey.

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](http://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](http://www.fenwick.com/vctrends.htm).**

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**SHIBOLETH, YISRAELI, ROBERTS, ZISMAN & CO.**  
**in cooperation with**  
**FENWICK & WEST LLP**

**Trends in Legal Terms in Venture Financings  
in Israel  
(Fourth Quarter of 2005 & First Quarter of 2006)**

- **Background** – We have analyzed the terms of venture financings for 53 Israeli and Israeli-related technology companies that reported raising money in the fourth quarter of 2005 and in the first quarter 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 fourth quarter of 2005/first quarter of 2006 and in the periods covered by our previous surveys may be broken down by types of round, or series, as follows:

Series	Q4/05+ Q1/06	H2'05	H1'05	H2'04	H1'04	H2'03
A	34%	34%	28%	35%	20%	22%
B	23%	27%	22%	21%	36%	30%
C	15%	12%	26%	25%	26%	22%
D	23%	17%	9%	11%	8%	19%
E and higher	5%	10%	15%	8%	10%	7%

- **Price Change** – The financings closed in the fourth quarter of 2005/first quarter 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	Q4/05+ Q1/06	H2'05	H1'05	H2'04	H1'04	H2'03
Down	23%	30%	19%	43%	42%	62%
Flat	6%	4%	16%	12%	3%	28%
Up	71%	66%	65%	45%	55%	10%

Up-rounds continued to outpace down-rounds by the largest margin since our survey began, constituting more than 70% of the surveyed rounds. The percentages of financing transactions that were down-rounds, broken down by series, were as follows:

Series	Q4/05+ Q1/06	H2'05	H1'05	H2'04	H1'04	H2'03
B	25%	36%	0%	25%	24%	73%
C	13%	20%	33%	56%	62%	55%
D	33%	29%	25%	43%	0%	56%
E and higher	0%	25%	14%	40%	80%	50%

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

Q4/05+ Q1/06	H2'05	H1'05	H2'04	H1'04	H2'03
83%	81%	76%	80%	78%	82%

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

Series	Q4/05+ Q1/06	H2'05	H1'05	H2'04	H1'04	H2'03
B	75%	73%	80%	85%	61%	82%
C	75%	100%	75%	75%	92%	75%
D	92%	71%	75%	71%	75%	82%
E and higher	100%	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:

Q4/05+ Q1/06	H2'05	H1'05	H2'04	H1'04	H2'03
10%	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	Q4/05+ Q1/06	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:

Q4/05+ Q1/06	H2'05	H1'05	H2'04	H1'04	H2'03
91%	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:

Q4/05+ Q1/06	H2'05	H1'05	H2'04	H1'04	H2'03
52%	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:

Q4/05+ Q1/06	H2'05	H1'05	H2'04	H1'04	H2'03
60%	68%	78%	52%	62%	54%

- **Anti-dilution Provisions** - The use of anti-dilution provisions in the financings which took place in the fourth quarter of 2005/first quarter of 2006 and in the periods covered by our previous surveys may be broken down as follows:

Type of Provision	Q4/05+ Q1/06	H2'05	H1'05	H2'04	H1'04	H2'03
Full Ratchet	28%	39%	31%	30%	28%	38%
Weighted Average	68%	61%	65%	64%	66%	55%
None	4%	0%	4%	6%	6%	7%

- **Pay-to-Play Provisions** - The use of pay-to-play provisions in the financings which took place in the fourth quarter of 2005/first quarter of 2006 and in the periods covered by our previous surveys may be broken down as follows:

Percentages (out of total number of financings in the relevant period) having pay-to-play provisions-

Q4/05+ Q1/06	H2'05	H1'05	H2'04	H1'04	H2'03
13%	15%	0%	13%	14%	9%

- **Redemption** – The percentage of transactions in the fourth quarter of 2005/first quarter 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:

Q4/05+ Q1/06	H2'05	H1'05	H2'04	H1'04	H2'03
17%	20%	17%	21%	26%	27%

- **Corporate Reorganizations** – The percentage of post-Series A financing transactions in the fourth quarter of 2005/first quarter 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:

Q4/05+ Q1/06	H2'05	H1'05	H2'04	H1'04	H2'03
2%	2%	7%	2%	10%	14%

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**FENWICK & WEST LLP  
 SHIBOLETH, YISRAELI, ROBERTS, ZISMAN & CO.**

**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  
 (Fourth Quarter of 2005 & First Quarter of 2006)**

- **Background** – We have analyzed the terms of venture financings for 53 Israeli based/related technology companies that reported raising at least \$500,000 in the fourth quarter of 2005 and in the first quarter of 2006, and compared those terms to the terms of venture financings for 216 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 – 34% (compared to 17% in the Silicon Valley)
  - Series B – 23% (compared to 37% in the Silicon Valley)
  - Series C – 15% (compared to 17% in the Silicon Valley)
  - Series D – 23% (compared to 13% in the Silicon Valley)
  - Series E and higher – 5% (compared to 16% in the Silicon Valley)
- **Price Change** – The financings during the fourth quarter of 2005 and in the first quarter 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:

<b>Price Change</b>	<b>Israel</b>	<b>Silicon Valley</b>
Down	23%	17%
Flat	6%	11%
Up	71%	72%

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

<b>Series</b>	<b>Israel</b>	<b>Silicon Valley</b>
B	25%	11%
C	13%	8%
D	33%	36%
E and higher	0%	24%

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

Israel	Silicon Valley
83%	41%

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

Series	Israel	Silicon Valley
B	75%	26%
C	75%	43%
D	92%	64%
E and higher	100%	53%

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

Israel	Silicon Valley
10%	19%

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%	79%
>2x - 3x	0%	21%
>3x	0%	0%

- **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
91%	65%

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
52%	52%

- **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
60%	4%

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

<b>Type of Provision</b>	<b>Israel</b>	<b>Silicon Valley</b>
Full Ratchet	28%	6%
Weighted Average	68%	88%
None	4%	6%

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

<b>Israel</b>	<b>Silicon Valley</b>
13%	13%

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

<b>Israel</b>	<b>Silicon Valley</b>
17%	29%

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

<b>Israel</b>	<b>Silicon Valley</b>
2%	10%

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