

2012 Venture Capital Report

CORPORATE



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2	US Market Review and Outlook
6	Regional Market Review and Outlook <ul style="list-style-type: none">– California– Mid-Atlantic– New England– Tri-State
10	Selected WilmerHale Venture Capital Financings
12	Law Firm Rankings – Eastern US
14	European Market Review and Outlook
15	Law Firm Rankings – Europe
16	JOBS Act Loosens Fundraising Restrictions on Private Companies
17	Misclassification of Independent Contractors
18	Trends in Venture Capital Financing Terms
19	Trends in VC-Backed Company M&A Deal Terms
20	<i>Initial Public Offerings: A Practical Guide to Going Public</i>

MARKET REVIEW

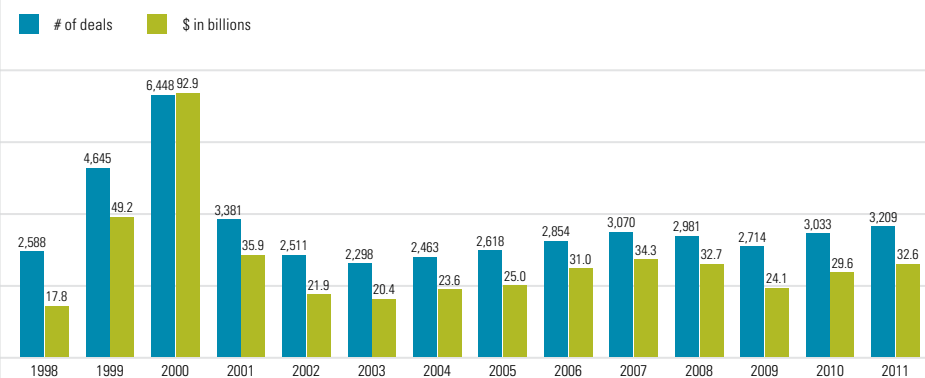
In 2011, the venture capital market produced its heaviest deal flow in a decade, with total proceeds that rivaled the levels of 2007 and 2008, despite lingering economic uncertainty and poor capital market conditions in the late summer and early fall. Liquidity performance was also impressive, with a steady stream of VC-backed IPOs and the highest median acquisition price in VC-backed M&A transactions since the peak of the dot-com boom in 2000.

There were 3,209 reported venture capital financings raising total proceeds of \$32.6 billion in 2011, compared to 3,033 financings that raised \$29.6 billion in 2010. The number of financings in 2011 was the highest since 2001, when 3,381 deals were reported. Deal volumes were fairly level throughout 2011, producing quarterly totals of 754, 835, 817 and 803 transactions. Total proceeds in 2011 were nearly as high as the amounts raised in 2007 and 2008, before the global economic recession that curtailed investment activity. Once all transactions have been reported, financing proceeds in 2011 are likely to represent the largest annual tally since 2001.

The median size of all venture capital financings increased from \$4.4 million in 2010 to \$5.0 million in 2011, reversing three consecutive annual declines, although the median financing size in 2011 was still lower than the figure for each year in the period from 1999 to 2008. The median financing size for life sciences companies increased from \$5.0 million in 2010 to \$6.0 million in 2011, its highest level since 2008. For information technology companies, the median financing size declined again, from \$5.0 million to \$4.7 million, representing the lowest median financing size since at least 1998. The steady decline in the median financing size for information technology companies partly reflects the ability of many technology companies to commence operations with lower levels of funding than historically required, due to various technological advances.

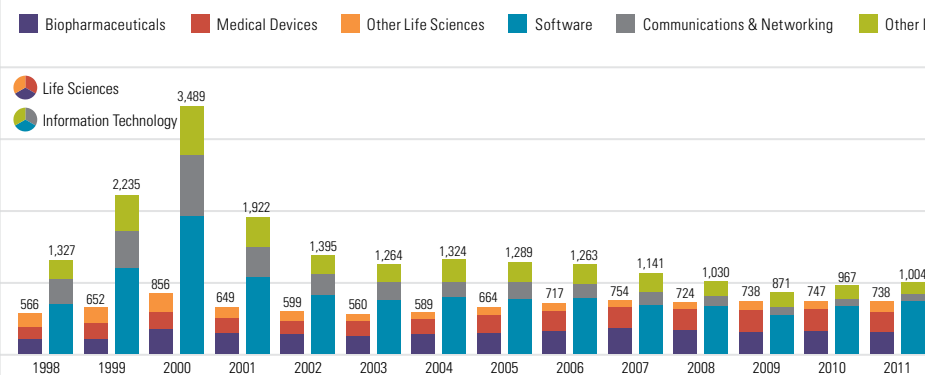
Amid strong competition for attractive deals, valuations of venture-backed

US Venture Capital Financings – 1998 to 2011



Source: Dow Jones VentureOne

US Venture Capital Financings by Industry – 1998 to 2011



Source: Dow Jones VentureOne

companies increased sharply from 2010 to 2011. The median pre-money valuation for all venture financings was \$21.0 million in 2011—the highest figure since 2000—compared to \$17.0 million in 2010. Among life sciences companies, the median pre-money valuation nearly doubled, increasing from \$13.1 million in 2010 to \$24.8 million in 2011. Information technology companies saw a more modest increase in median pre-money valuation, from \$11.2 million to \$15.0 million.

Seed and first-round venture capital financings accounted for 42% of the total

number of venture financings in 2011 (compared to 37% in 2010) and 18% of the total amount of venture capital investment (unchanged from the level in 2010). Seed and first-round financings have constituted between 29% and 42% of the total number of all venture financings in each year since 2001. The proportion of seed and first-round investing activity over the past decade, however, is significantly lower than the proportion prior to 2001. The increase in early-stage investing in 2011 reflects a reduction in the average time from initial funding to a liquidity event—which decreases the amount of

money needed for investment in later-stage companies—as well as lower barriers to entry in certain technology sectors, resulting in an increase in the number of companies being formed and funded.

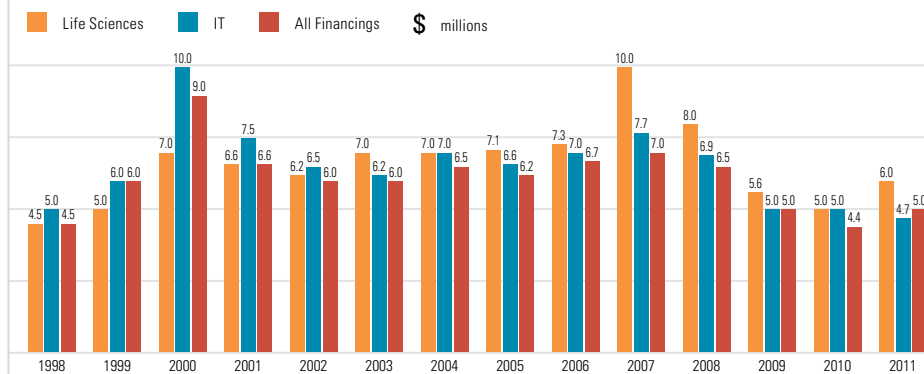
Venture capital investing by industry sector in 2011 was largely consistent with longer-term trends. Information technology companies represented 31% of all venture capital financings in 2011 (compared to 32% in 2010), while life sciences companies constituted 23% in 2011 (compared to 25% in 2010). In 2011, for the third consecutive year, the amount invested in life sciences companies (\$8.4 billion) exceeded the amount invested in information technology companies (\$7.9 billion).

The geographic breakdown for venture capital investing has remained fairly constant since 1996 (the first year for which this data is available). California—which has led the country in this regard in each year since 1996—accounted for 42% of all venture financings in 2011 (1,344 financings). Massachusetts, home to 10% of the companies receiving venture financing in 2011 (332 financings), again finished second in this category, as it has in each year since 1996, narrowly edging out New York, also with a 10% market share (317 financings). Texas (143 financings) and Pennsylvania (124 financings) rounded out the top five positions for 2011, concluding a repetition of the state rankings from 2010.

The IPO market remained receptive to VC-backed companies in 2011, continuing the recovery that began in 2010 after VC-backed IPOs all but disappeared for most of 2008 and 2009. In 2011, a total of 42 US venture-backed companies went public in the United States, down just one from the 43 in 2010. The largest VC-backed IPO of 2011 was the \$1.0 billion offering by Zynga, followed by Groupon's \$700 million IPO. The median amount of time from initial funding to an IPO was 6.5 years in 2011, down from 8.1 years in 2010 and the lowest since the 5.6-year median recorded in 2005.

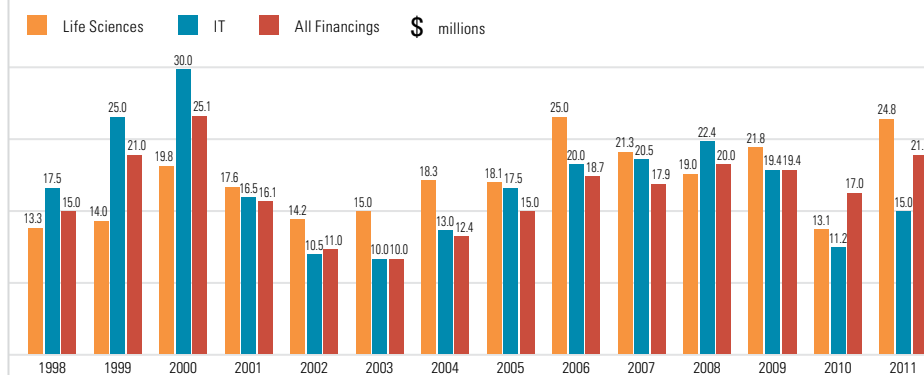
The ratio of pre-IPO valuations to the median amount raised prior to IPO by venture-backed companies going public increased to 5.4:1 in 2011 from 4.1:1 in

Median Size of US Venture Capital Financings – 1998 to 2011



Source: Dow Jones VentureOne

Median Pre-Money Valuation in US Venture Capital Financings – 1998 to 2011



Source: Dow Jones VentureOne

2010—the second-highest level since 2000 (a higher ratio means higher returns to pre-IPO investors). This ratio was between 3.1:1 and 5.3:1 for each year from 2001 to 2008. In contrast, this ratio ranged from 7.7:1 to 10.0:1 from 1997 to 2000, due to very large pre-IPO valuations by younger companies, and spiked temporarily to 8.9:1 in 2009 based on a very small sample size of VC-backed IPOs that year.

The M&A market for venture-backed companies was favorable in 2011. Although the number of reported acquisitions of VC-backed companies

declined from 560 in 2010 to 477 in 2011, purchase prices jumped, fueled by the availability of large cash balances by strategic buyers. The median acquisition price for venture-backed companies soared to \$71 million in 2011 from \$40 million in 2010. The median amount of time from initial funding to acquisition dipped to 5.3 years in 2011 from 5.4 years in the prior year—continuing a four-year trend of annual declines. With a shorter timeline to liquidity, the median amount raised prior to acquisition also declined in 2011—dropping from \$19.4 million to \$17.0 million.

The largest VC-backed company acquisition of 2011 was Plexxikon's acquisition by Daiichi Sankyo for \$805 million (plus milestone payments of up to \$130 million), followed by Ardian's acquisition by Medtronic for \$800 million (plus milestone payments based on annual revenue growth). There were a total of 14 VC-backed company acquisitions for at least \$500 million in 2011, compared to eight in the prior year.

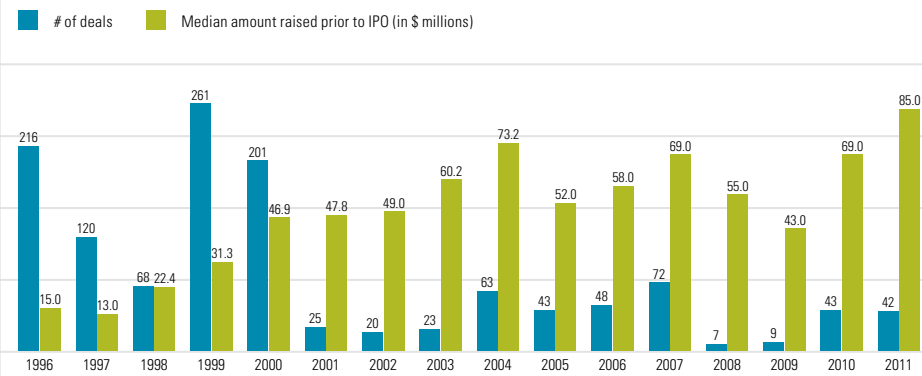
The ratio of median acquisition price to median amount raised prior to acquisition was 4.2:1 in 2011, compared to 2.1:1 in 2010 and 1.3:1 in 2009 (a higher ratio means higher returns to pre-acquisition investors). The spike in this ratio in 2011 reflected the combination of very strong valuations and shorter time periods to acquisition. The 2011 ratio was the highest since the stratospheric ratio of 10.0:1 in 2000 at the height of the dot-com craze, when young companies routinely were acquired for outsized prices.

The above comparison of the ratios of valuations to the financing amounts required to achieve liquidity events indicates that returns to venture capital investors remain higher on IPOs than on M&A transactions. The higher valuations ascribed to IPO companies are offset, in part, by the fact that the median amount raised prior to liquidity event for M&A companies (\$17.0 million in 2011) is generally much lower than the amount for IPO companies (\$85.0 million in 2011), and the longer timelines from initial funding to liquidity for IPO companies (6.5 years in 2011) than for M&A companies (5.3 years in 2011).

Moreover, venture investors generally achieve liquidity more rapidly in an M&A transaction (which frequently yields the bulk of the purchase price in cash at closing) than in an IPO (which generally involves a post-IPO lockup period of 180 days and market uncertainty on the timing and prices of subsequent sales).

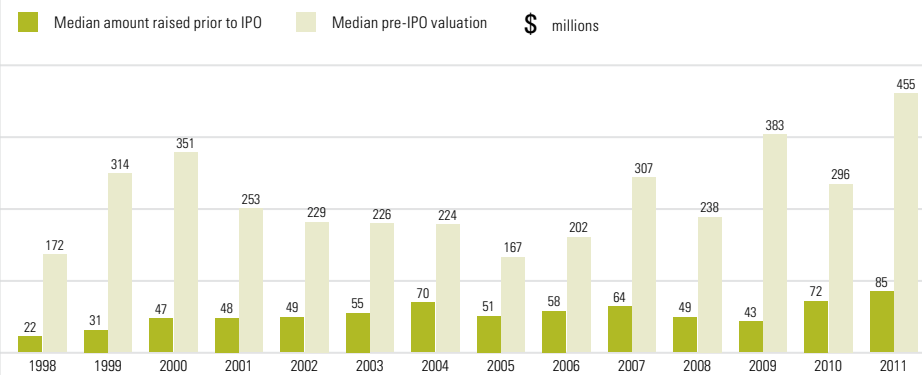
The ratio of M&A transactions to IPOs for venture-backed companies was 11:1 in 2011 and 13:1 in 2010. Compared to the preceding two years, when this ratio was approximately five times higher, the results for 2010 and 2011 are close to historical norms. The M&A/IPO ratio

Venture Capital-Backed IPOs – 1996 to 2011



Source: Dow Jones VentureOne and SEC filings
The above chart is based on US IPOs by VC-backed US issuers.

Median Amount Raised Prior to IPO and Median Pre-IPO Valuation – 1998 to 2011



Source: Dow Jones VentureOne

for VC-backed exits was 10:1 during the period 2004–2007, 19:1 during the period 2001–2003, and less than 3:1 during the Internet boom of 1998–2000.

OUTLOOK

The outlook for the venture capital market over the coming year is generally positive. Early results for 2012 bear out this optimism, although economic concerns and the continuing sovereign debt crisis in Europe could dampen expectations.

In the first quarter of 2012, venture capital investing was largely consistent with the

comparable period of the prior year and overall trends in the marketplace, while liquidity outcomes improved further from the already positive results of 2011.

Approximately \$6.3 billion was invested in 717 reported venture capital financings in the first quarter of 2012. These totals were lower than the reported amounts for the corresponding period of 2011, although the number of financings in the first quarter of 2012 should approach the prior year's figure once all financings have been reported. Final proceeds for the first quarter of 2012 will likely fall short

of the corresponding figure from the first quarter of 2011, but the prior year's results were inflated by several extremely large financings by mature private companies.

The overall number of IPOs by venture-backed companies increased from 11 in the first quarter of 2011 to 20 in the first quarter of 2012, including prominent IPOs by several well-known companies. In May 2012, Facebook produced the largest VC-backed IPO in history—with \$16.0 billion in proceeds.

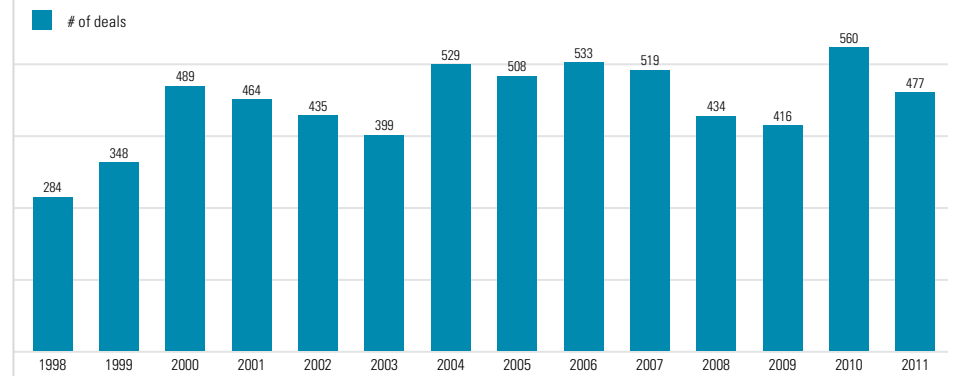
Reported acquisition activity declined from 139 deals in the first quarter of 2011 to 94 deals in the first quarter of 2012, although delayed reporting probably explains much of the decrease in volume. The average acquisition price more than doubled, however, from \$92 million to nearly \$193 million, underscoring the willingness of strategic buyers to pay large amounts for attractive targets. The largest transaction of the first quarter of 2012 was the acquisition of Liberty Dialysis by Fresenius Medical Care for \$1.7 billion. Subsequently, Facebook announced an agreement to acquire Instagram for \$1 billion.

The level of venture capital financing activity over the balance of 2012 will be significantly affected by general economic conditions, investor confidence and the health of the IPO market for VC-backed companies.

Investor interest in the consumer Internet sector should remain strong, although valuations may undergo a correction from the recent levels that at times have seemed reminiscent of the dot-com era. Valuations in other sectors could also come under pressure if conditions in the economy at large and in the capital markets worsen.

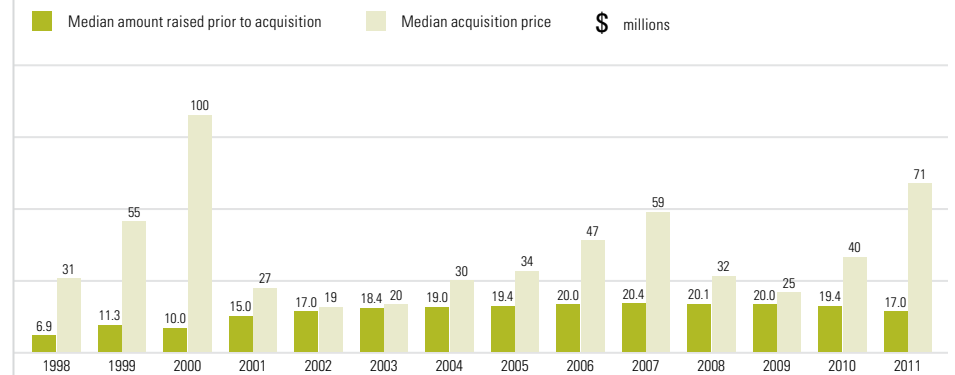
The clean technology and renewable energy sector should benefit from heightened environmental awareness, the availability of government funding, and the long-term trend in rising energy prices. Problems with distribution, larger numbers of competing technologies, and the need in many cases for significantly larger investment amounts than in traditional VC-backed industries may cause some investors to approach this market cautiously.

Acquisitions of US Venture-Backed Companies – 1998 to 2011



Source: Dow Jones VentureOne

Median Amount Raised Prior to Acquisition and Median Acquisition Price – 1998 to 2011



Source: Dow Jones VentureOne

Ongoing globalization in venture investing is likely to continue. International markets such as China, India and parts of Southeast Asia, as well as portions of Eastern Europe and South America, are spawning increased entrepreneurial activity and innovation, and the regulatory environments in those countries are also becoming more hospitable to foreign investment.

The liquidity outlook for VC-backed companies remains bright. On the heels of a very good IPO market for venture-backed companies in the preceding two years,

deal flow picked up in the first quarter of 2012. In addition, the JOBS Act, enacted in early April, should encourage additional VC-backed companies to join an already robust pipeline of IPO candidates.

Prospects for the M&A market also appear promising. Strategic acquirers have excess cash to deploy, and the existence of a credible IPO alternative enhances the leverage of venture-backed companies in negotiating acquisition prices. Both the IPO and M&A markets could soften if the economy stagnates or extreme volatility returns to the capital markets. ■

CALIFORNIA

California companies reported 1,344 financings in 2011, up 10% from the 1,227 financings in 2010. After soaring to nearly \$19 billion in 2010, proceeds declined 14% to \$16.35 billion—still the second-highest total since 2000. Liquidity outcomes for California VC-backed companies were generally strong in 2011.

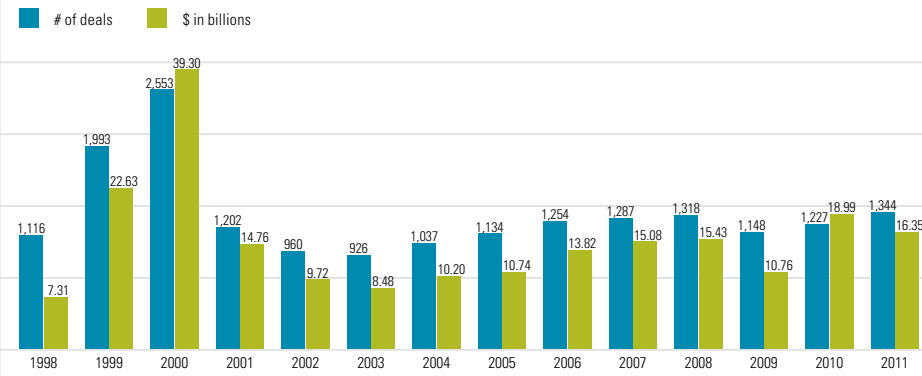
Roughly four times the size of the next-largest venture capital market in the United States, California was responsible for 42% of the nation's financing transactions in 2011. The year's deal tally was the largest ever achieved in California, other than during the peak of the dot-com boom—in 2000, California produced a staggering 2,553 financings, with nearly \$40 billion in proceeds.

California's venture capital market spans all industry sectors, with particular strengths in consumer Internet, information technology, life sciences, cleantech, consumer retail and media/entertainment. With a 41% market share, information technology was the largest sector in the state in 2011, followed by life sciences at 18%. California's best-known VC-backed companies are, of course, in social media.

The state generated 22 IPOs by VC-backed companies in 2011, compared to 19 in 2010. The number of reported acquisitions of California VC-backed companies declined from 274 in 2010 to 228 in 2011, but still surpassed any other year on record. In 2011, California produced three of the country's five largest VC-backed IPOs and the two largest venture-backed company acquisitions.

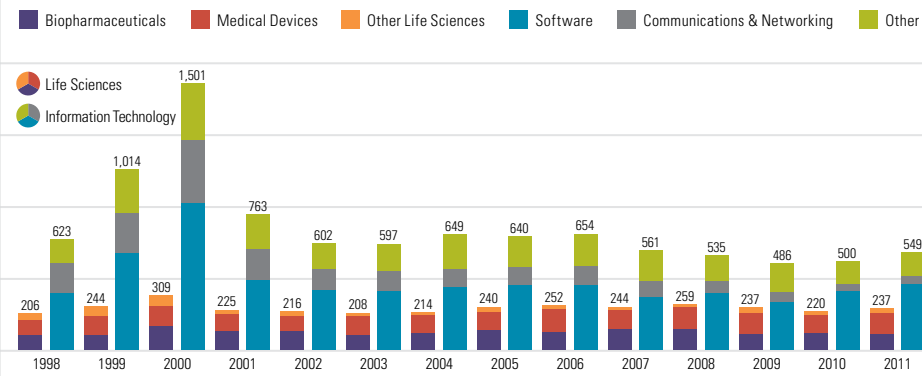
We expect California to maintain its venture capital leadership in the coming year. Future growth in financing activity and continued strength in liquidity will depend, in part, on general economic conditions, the willingness of strategic buyers to pay attractive premiums, and the overall health of the capital markets. Year-to-date liquidity highlights include Facebook's \$16.0 billion IPO, Instagram's proposed acquisition for \$1 billion (also by Facebook), and Efficient Frontier's \$400 million acquisition by Adobe Systems.

California Venture Capital Financings – 1998 to 2011



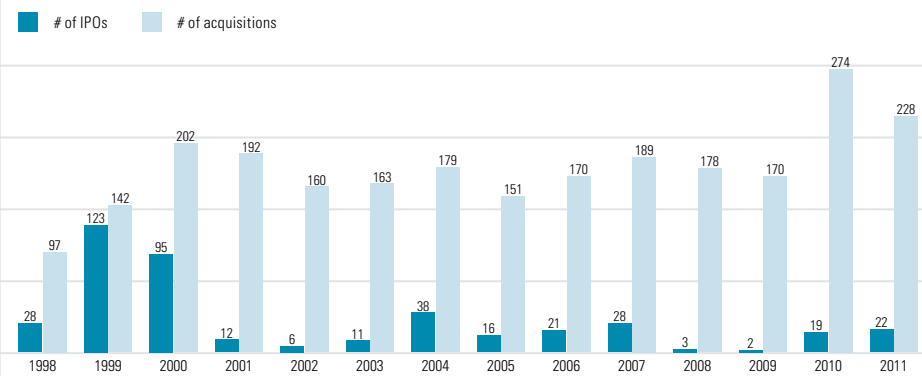
Source: Dow Jones VentureOne

California Venture Capital Financings by Industry – 1998 to 2011



Source: Dow Jones VentureOne

California Venture-Backed IPOs and Acquisitions – 1998 to 2011



Source: Dow Jones VentureOne

MID-ATLANTIC

The number of reported venture capital financings in the mid-Atlantic region of Virginia, Maryland, North Carolina, Delaware and the District of Columbia increased 8%, from 163 in 2010 to 176 in 2011, while proceeds jumped 30%, from \$1.48 billion to \$1.92 billion—the highest level of proceeds since 2001. Although they do not rival the deal activity that prevailed between 1999 and 2001, annual tallies for venture capital financings and proceeds in the mid-Atlantic region remain above the levels seen in the pre-bubble years.

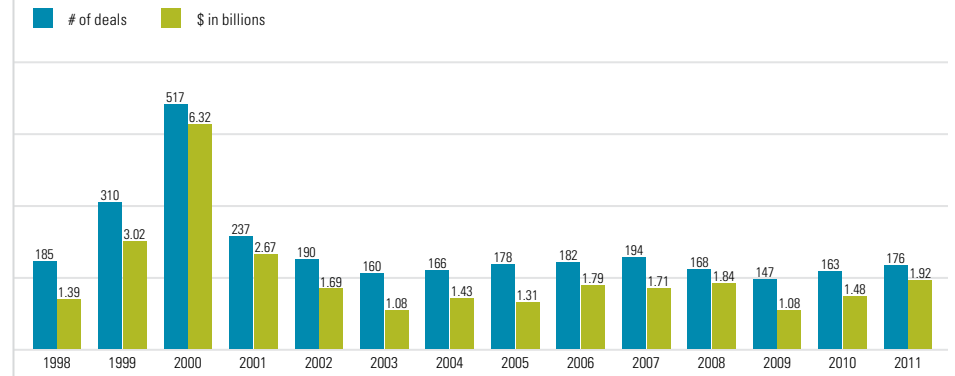
The percentage of all mid-Atlantic financings completed by information technology companies increased from 36% in 2010 to 39% in 2011. The region's life sciences sector—which had outpaced the information technology sector in 2009—saw its market share inch up from 29% to 30%.

After three VC-backed IPOs in 2010, the mid-Atlantic region produced only one IPO in 2011—Tranzyme's \$54.0 million offering.

In contrast to the downturn in the region's IPO activity from 2010 to 2011, the number of reported acquisitions of mid-Atlantic VC-backed companies increased from 36 to 50. Virginia continued to lead the region in VC-backed M&A transactions in 2011, with 27 deals, followed by North Carolina with 11 and Maryland with nine. The region's largest M&A transaction of the year was the \$650 million acquisition of TARGUSinfo by Neustar, followed in size by Open Text's acquisition of Metastorm for \$182 million.

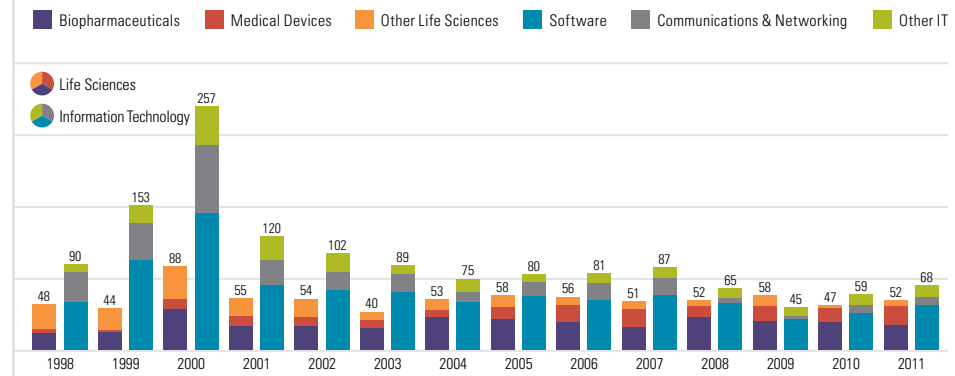
In the coming year, we expect that the mid-Atlantic region will remain a leading investment center for technology and life sciences companies and will spawn additional candidates to pursue IPOs. We also expect the region to continue to produce attractive acquisition candidates. Year-to-date liquidity highlights include BioReliance's acquisition by Sigma-Aldrich for \$350 million and Millennial Media's IPO raising \$132.6 million.

Mid-Atlantic Venture Capital Financings – 1998 to 2011



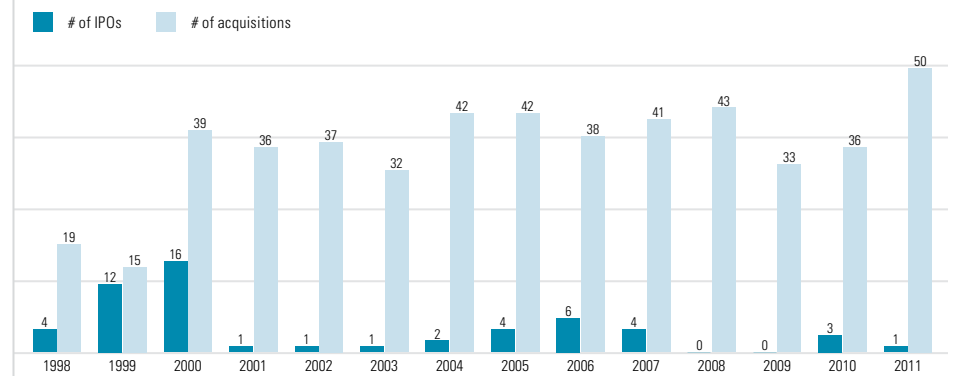
Source: Dow Jones VentureOne

Mid-Atlantic Venture Capital Financings by Industry – 1998 to 2011



Source: Dow Jones VentureOne

Mid-Atlantic Venture-Backed IPOs and Acquisitions – 1998 to 2011



Source: Dow Jones VentureOne

NEW ENGLAND

New England companies reported 409 financings in 2011, up 9% from the 376 financings in 2010, while proceeds leapt 41%, from \$2.79 billion to \$3.94 billion. The number of financings and amount of proceeds were the largest in New England since 2001.

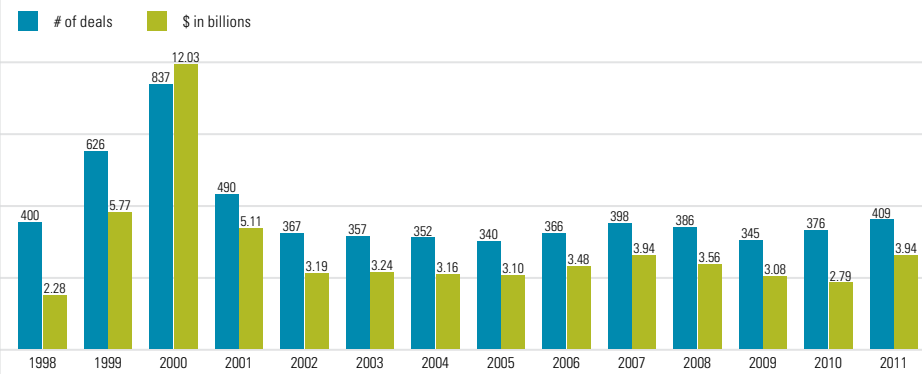
New England continues to be a leading center of activity for technology and life sciences companies. In 2011, the number of financings by life sciences companies edged out the number of financings by information technology companies, as the two sectors swapped places in the rankings again. Information technology companies accounted for 33% of New England's venture capital financings in 2011 (down from 37% in 2010) and life sciences companies contributed 36% of the region's financings (up from 35%).

New England generated four venture-backed IPOs in 2011—from BG Medicine (\$35.0 million), Carbonite (\$62.5 million), Tangoe (\$100.9 million) and Zipcar (\$174.3 million)—compared to three IPOs in the prior year.

The number of reported acquisitions of VC-backed companies in New England declined from 82 in 2010 to 73 in 2011—still the second-highest figure since 2007. The region produced three of the nation's 10 largest deals of 2011: the acquisition of Advanced BioHealing by Shire for \$750 million, the acquisition of ITA Software by Google for \$700 million, and the acquisition of Salient Surgical Technologies for \$525 million by Medtronic. In addition, BioVex Group was acquired in 2011 by Amgen for \$1 billion (including potential milestone payments).

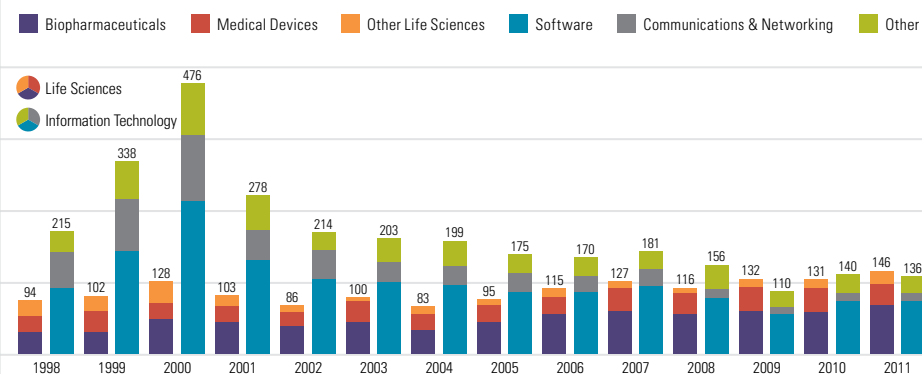
We expect New England—and Massachusetts in particular—to remain one of the country's most appealing environments for emerging companies and a hub of venture capital and IPO activity during the coming year. Year-to-date liquidity highlights include the acquisition of Kiva Systems by Amazon.com for \$775 million and the IPOs of Demandware (\$101.2 million), Merrimack Pharmaceuticals (\$105.3 million) and Verastem (\$63.3 million).

New England Venture Capital Financings – 1998 to 2011



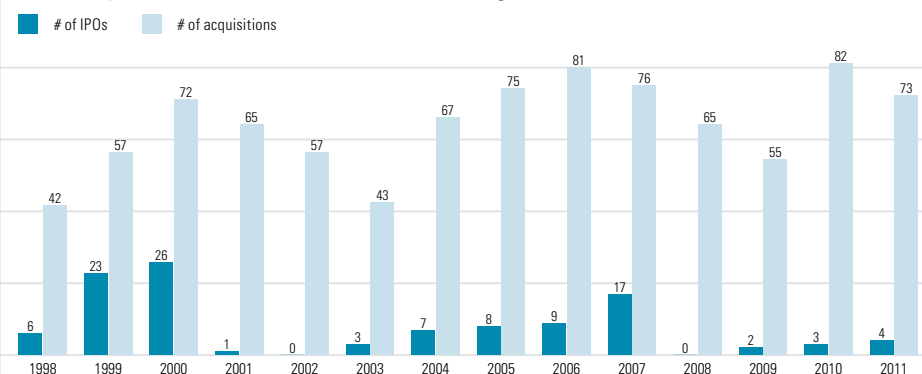
Source: Dow Jones VentureOne

New England Venture Capital Financings by Industry – 1998 to 2011



Source: Dow Jones VentureOne

New England Venture-Backed IPOs and Acquisitions – 1998 to 2011



Source: Dow Jones VentureOne

TRI-STATE

The number of reported venture capital financings in the tri-state region of New York, New Jersey and Pennsylvania increased from 479 in 2010 to 495 in 2011—the region's highest annual tally since 2000—while proceeds rose from \$3.31 billion to \$3.67 billion. New York led the region's financing activity, with 317 financings—once again just behind Massachusetts in the state rankings. Underscoring the pronounced shifts in tri-state investments over the past decade, between 2001 and 2011, the number of financings in New York increased by 45%, while deal flow was relatively constant in Pennsylvania and dropped by more than half in New Jersey.

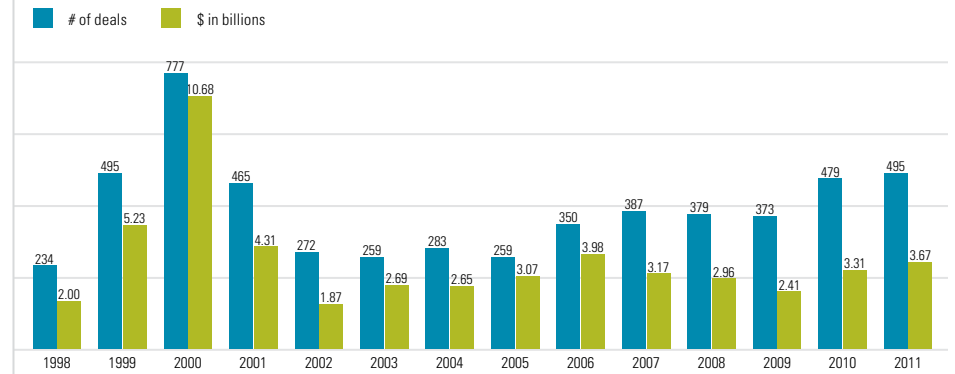
Information technology companies garnered the largest share of the tri-state region's VC financing market in 2011, with 28% of the region's financings, up from 25% in 2010. Life sciences companies, after leading the tri-state region's rankings in 2009, accounted for only 17% of the region's financings in 2011, down from 24% in the prior year.

After generating a robust total of eight VC-backed IPOs in 2010, the tri-state region had one solitary IPO in 2011—the \$42.0 million offering of Pacira Pharmaceuticals—as exit activity shifted toward acquisitions.

Reported acquisitions of venture-backed companies in the tri-state region increased 9%, from 89 in 2010 to 97 in 2011, on the heels of the doubling of VC-backed company M&A activity from 2010 to 2011. The region's largest deal of 2011 was the acquisition of Quidsi by Amazon.com for \$545 million.

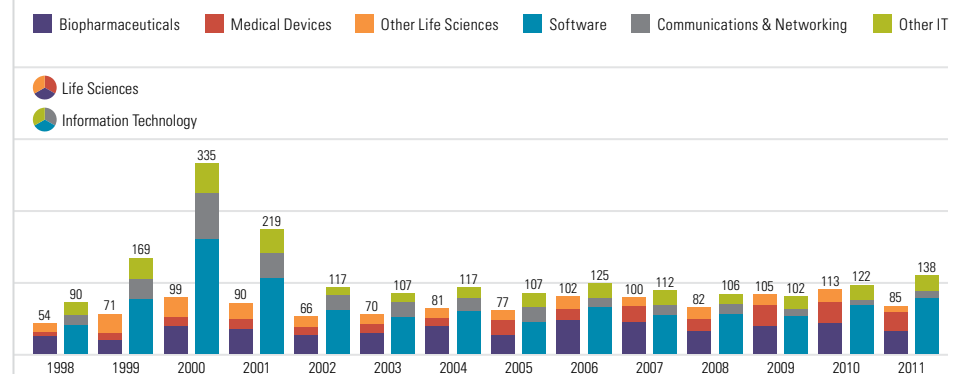
We believe that, over the coming year, the tri-state region's strengths in the life sciences and information technology industries—particularly in the consumer Internet space—will continue to foster a favorable environment for VC-backed startup companies and produce viable IPO and acquisition candidates. Year-to-date liquidity highlights include the IPOs of EPAM Systems (\$72.0 million) and FX Alliance (\$62.4 million). ■

Tri-State Venture Capital Financings – 1998 to 2011



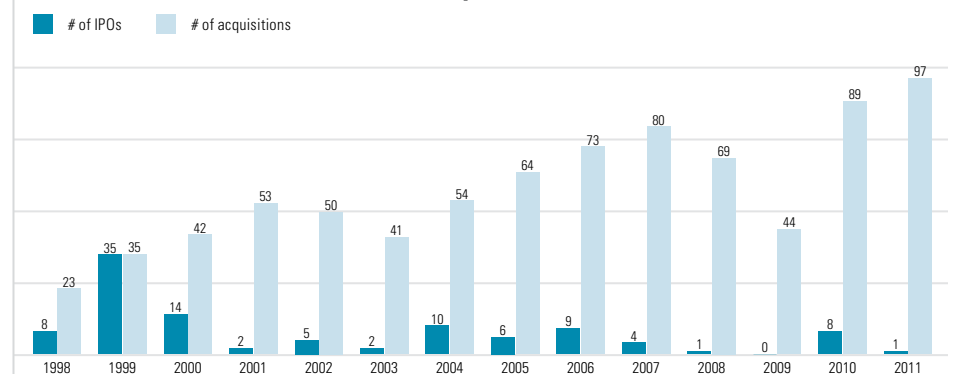
Source: Dow Jones VentureOne

Tri-State Venture Capital Financings by Industry – 1998 to 2011



Source: Dow Jones VentureOne

Tri-State Venture-Backed IPOs and Acquisitions – 1998 to 2011


















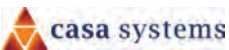






Source: Dow Jones VentureOne

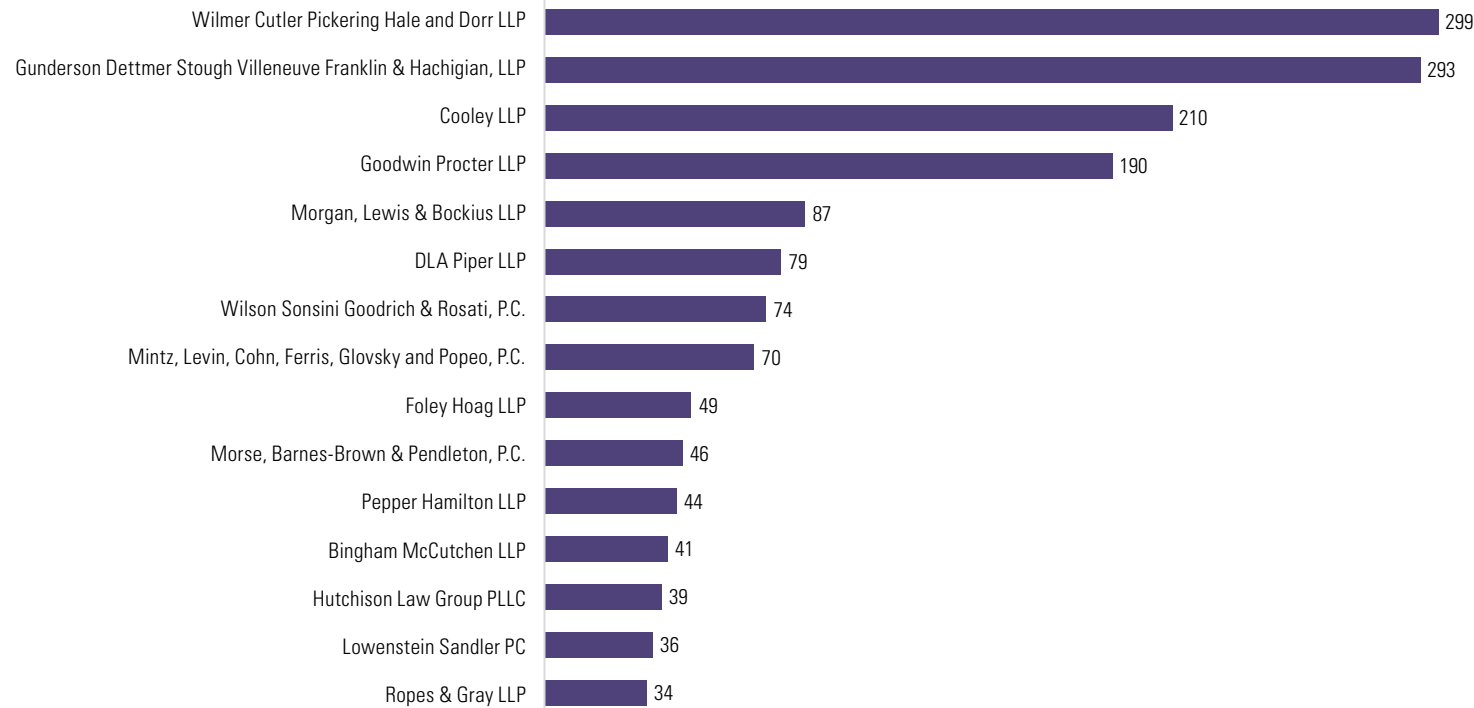
Counsel of Choice for Venture Capital Financings

SERVING INDUSTRY LEADERS IN TECHNOLOGY, LIFE SCIENCES, ENERGY AND CLEANTECH, FINANCIAL SERVICES, COMMUNICATIONS AND BEYOND



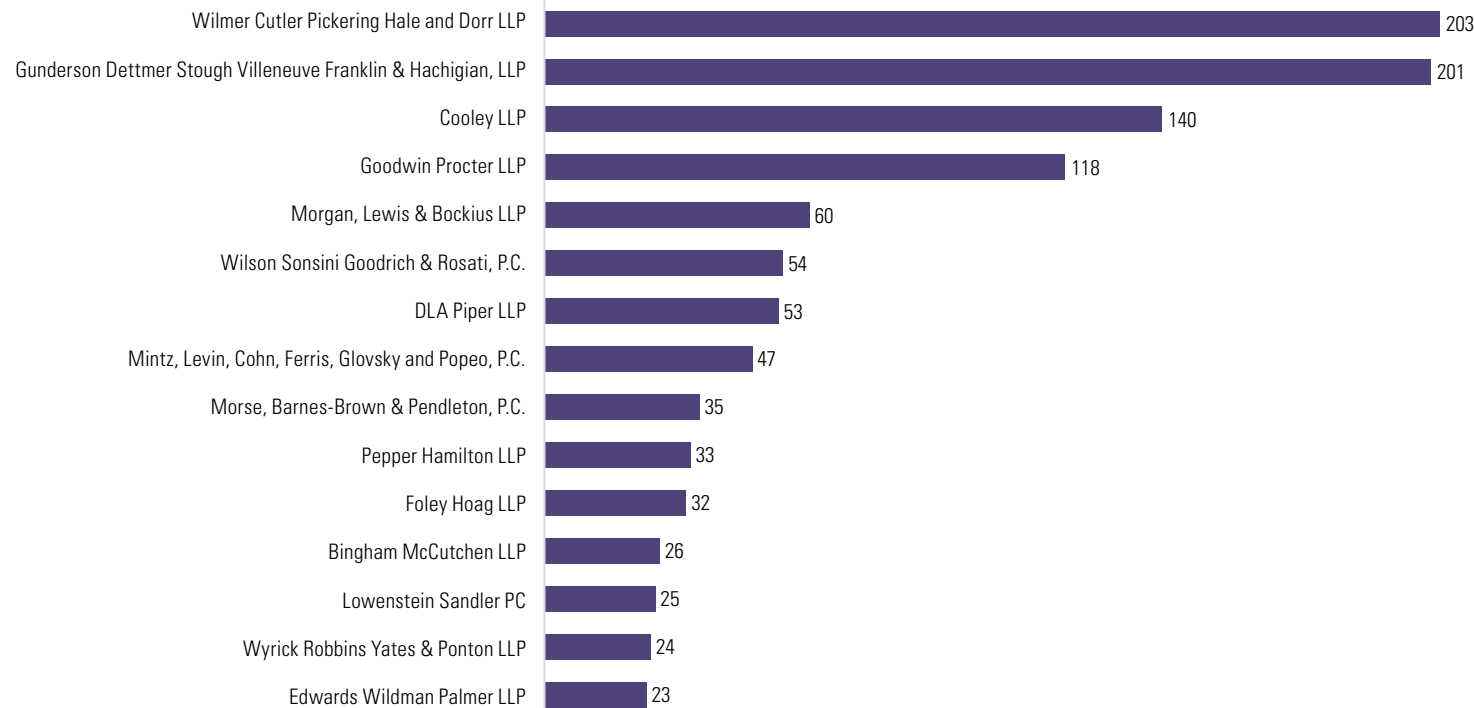
 Allena <small>PHARMACEUTICALS</small>	 LATTICE ENGINES <small>Sell Smarter</small>	 MERRIMACK <small>PHARMACEUTICALS</small>	 Semprus <small>BIOSCIENCES</small>	 mc10	 catabasis		
\$15,000,000 <i>First Round</i> September 2011	\$15,000,000 <i>Second Round</i> May 2011	\$77,000,000 <i>Late Stage</i> April 2011	\$18,000,000 <i>Second Round</i> December 2010	\$15,000,000 <i>Second Round</i> August 2011	\$47,600,000 <i>First Round</i> December 2011		
 Constellation <small>Pharmaceuticals</small>	 RHYTHMIA <small>medical</small>	 TransMedics	 Metamark <small>GENETICS, INC.</small>	 KIOR	 AYLUS networks	 agios	
\$15,000,000 <i>Second Round</i> June 2011	\$7,000,000 <i>Third Round</i> September 2010	\$36,000,000 <i>Late Stage</i> February 2010	\$22,000,000 <i>Second Round</i> July 2010	\$55,000,000 <i>Third Round</i> April 2011	\$16,000,000 <i>Fourth Round</i> June 2011	\$78,000,000 <i>Third Round</i> November 2011	
 LASER LIGHT ENGINES	 480 biomedical	 nanoterra	 LINK <small>medicine</small>	 PETRA SOLAR <small>Midstream Energy By Design</small>	 BIOSCALE	 CvaScience <small>Commercial and Consumer Health</small>	 366 <small>Technologies</small>
\$13,000,000 <i>Second Round</i> September 2010	\$15,000,000 <i>Second Round</i> September 2011	\$17,200,000 <i>First Round</i> December 2010	\$45,000,000 <i>Third Round</i> April 2010	\$40,000,000 <i>Second Round</i> January 2010	\$25,000,000 <i>Fourth Round</i> May 2010	\$6,000,000 <i>First Round</i> July 2011	\$28,400,000 <i>Second Round</i> October 2010
 CERULEAN <small>LEADERSHIP IN BIOPHARMACEUTICALS</small>	 casa systems	 BINOPTICS	 TETRAPHASE <small>PHARMACEUTICALS</small>	 tōkai pharmaceuticals	 Daktari	 SEED	
\$15,000,000 <i>Fourth Round</i> December 2011	\$96,000,000 <i>Late Stage</i> April 2010	\$13,300,000 <i>Late Stage</i> August 2011	\$45,000,000 <i>Third Round</i> May 2010	\$23,000,000 <i>Fourth Round</i> September 2011	\$10,000,000 <i>Second Round</i> December 2011	\$15,000,000 <i>Fourth Round</i> May 2011	

Counsel to Eastern US Companies Receiving VC Financing – 2007 to 2011



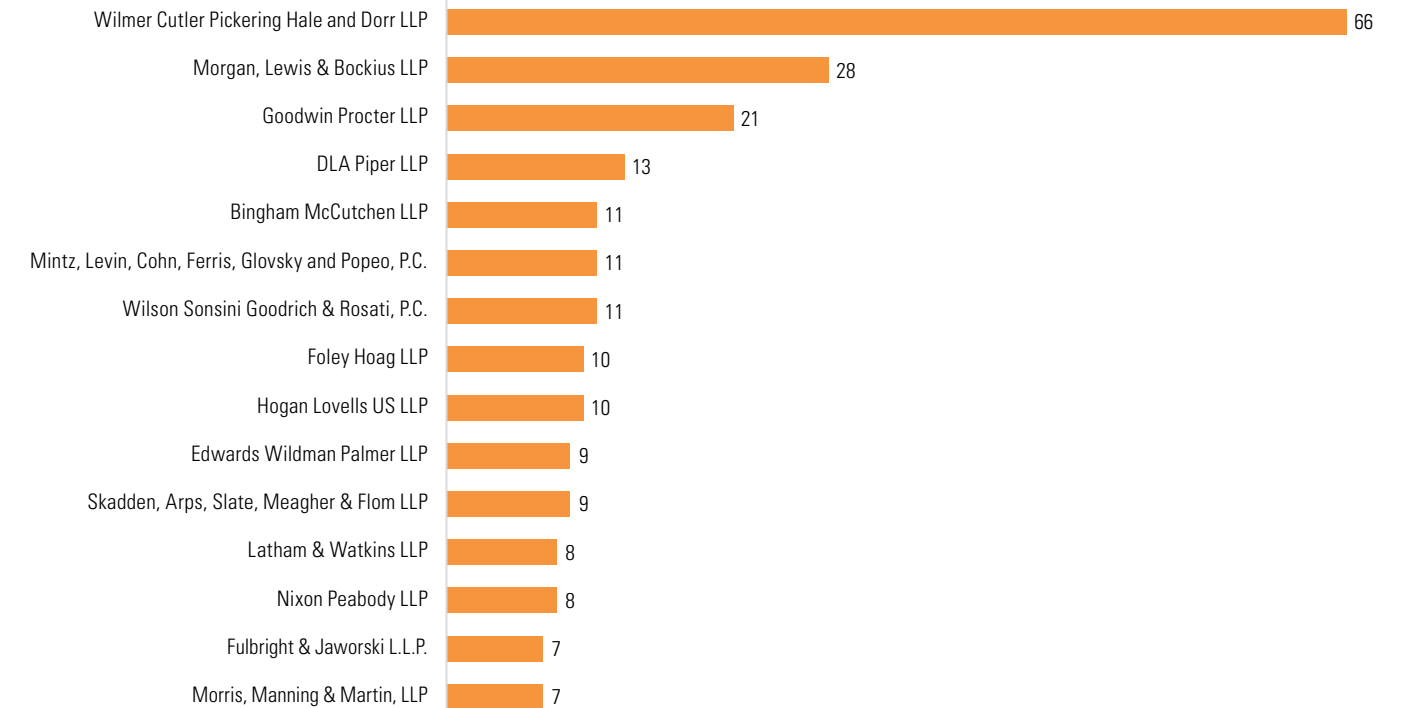
*The above chart is based on companies located east of the Mississippi River that completed a seed, first, second, later-stage or restart round of venture capital financing between 2007 and 2011.
Source: Dow Jones VentureOne*

Counsel to VC-Backed Companies at Year-End 2011 – Eastern US



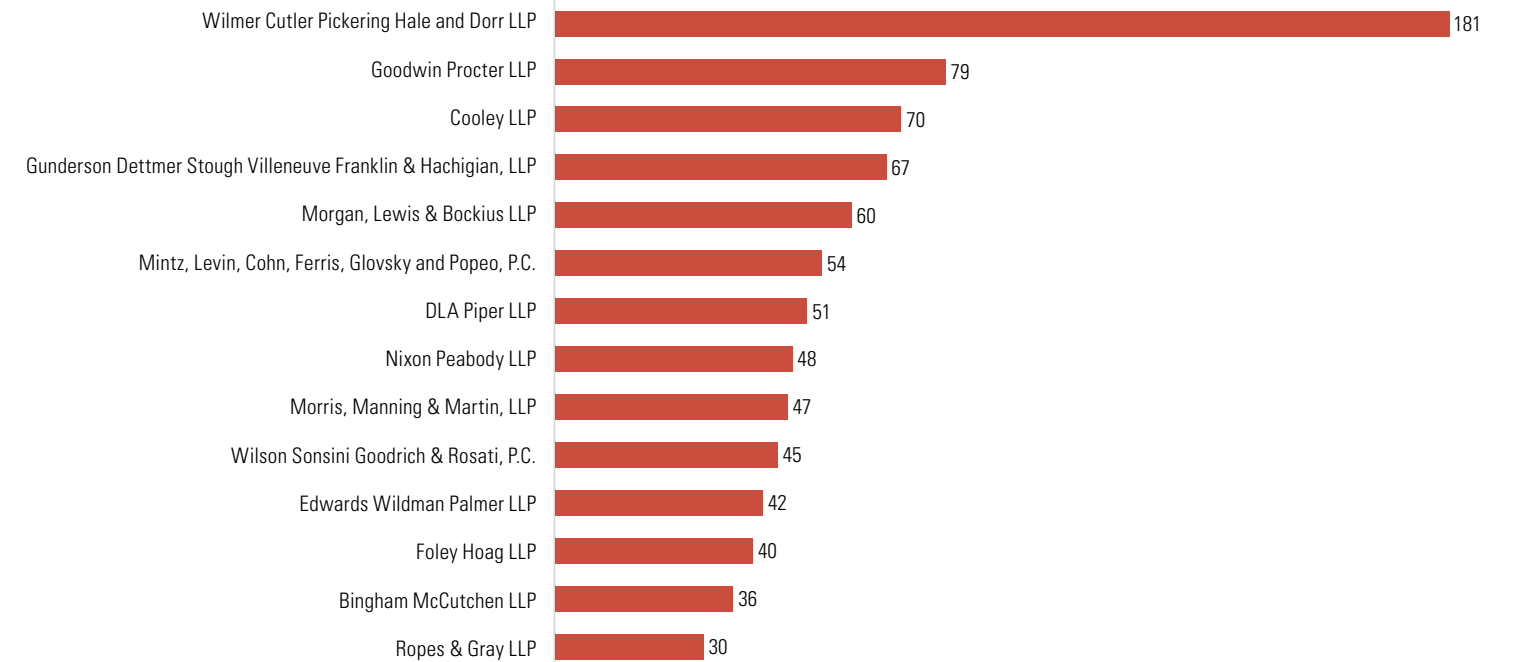
*The above chart is based on VC-backed companies located east of the Mississippi River that were private and independent as of the end of 2011.
Source: Dow Jones VentureOne*

Company Counsel in IPOs of Eastern US VC-Backed Companies – 1996 to 2011



*The above chart is based on VC-backed companies located east of the Mississippi River.
Source: Dow Jones VentureOne and SEC filings*

Company Counsel in Sales of Eastern US VC-Backed Companies – 1996 to 2011



*The above chart is based on VC-backed companies located east of the Mississippi River.
Source: Dow Jones VentureOne*

REVIEW

Weighed down in 2011 by concerns over economic conditions and the sovereign debt crisis, the European venture capital market reversed its gains of the prior year to post its lowest transaction tally in more than a decade. Financing proceeds also declined in 2011, but by a lower percentage. Liquidity outcomes for European VC-backed companies were generally comparable to the solid results posted in 2010.

Venture capital financing proceeds in Europe decreased from €5.0 billion in 2010 to €4.4 billion in 2011, while the number of reported financings dropped from 1,253 to 1,012. Once all 2011 transactions have been reported, this gap should narrow, but is unlikely to be fully bridged.

In 2011, the software sector again accounted for the largest portion of the European venture capital market, representing 19% of all financings, followed by biopharmaceuticals with a 12% market share. Overall, information technology companies accounted for 27% of Europe's venture capital financings in 2011 and life sciences companies contributed 22%.

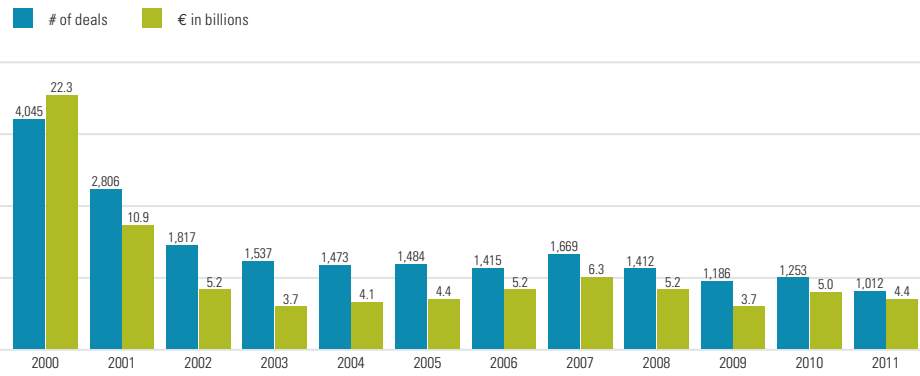
Once again, the United Kingdom was the largest venture capital market in Europe in 2011, generating 27% of the year's financings, followed by France (21%), Germany (12%) and Sweden (7%).

In 2011, the number of IPOs by European venture-backed companies dropped to 14 from 18 in the prior year, but average company proceeds increased from €24 million to €50 million. The largest IPO of 2011 was Yandex's \$1.435 billion offering. The number of acquisitions of European VC-backed companies edged down, from 176 in 2010 to 154 in 2011.

OUTLOOK

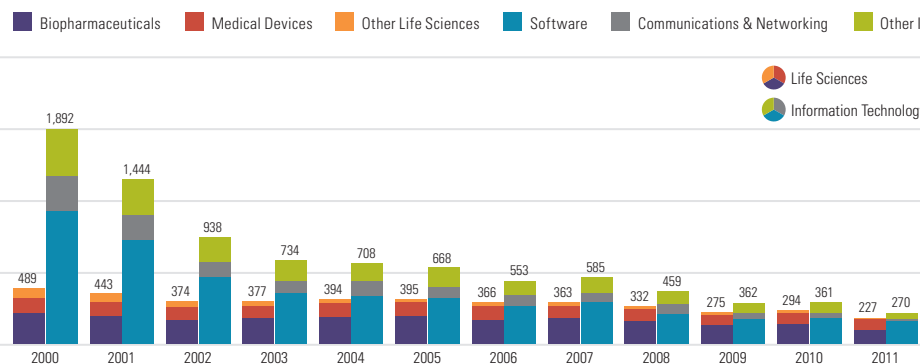
Year-to-date results for the European venture capital market reflect an uncertain outlook in light of economic concerns. Financing activity, IPOs and acquisitions in the first quarter of 2012 all trailed the results from the corresponding period of 2011. Although delayed reporting undercuts the reliability of first-quarter comparisons, these early results suggest that the European venture capital market will face challenging conditions in 2012. ■

European Venture Capital Financings – 2000 to 2011



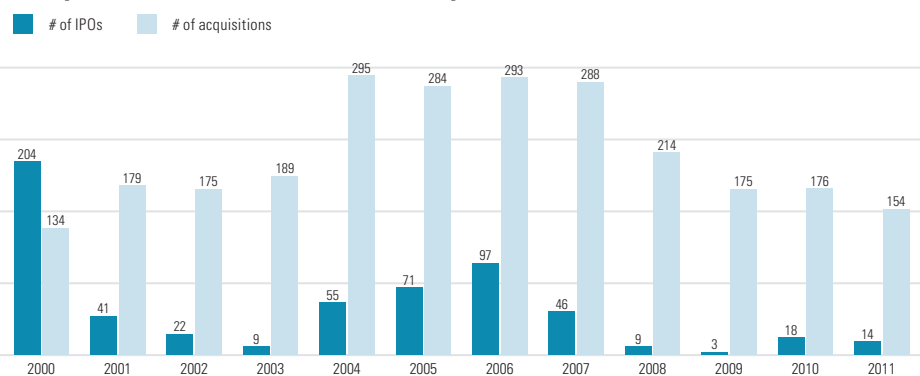
Source: Dow Jones VentureOne

European Venture Capital Financings by Industry – 2000 to 2011



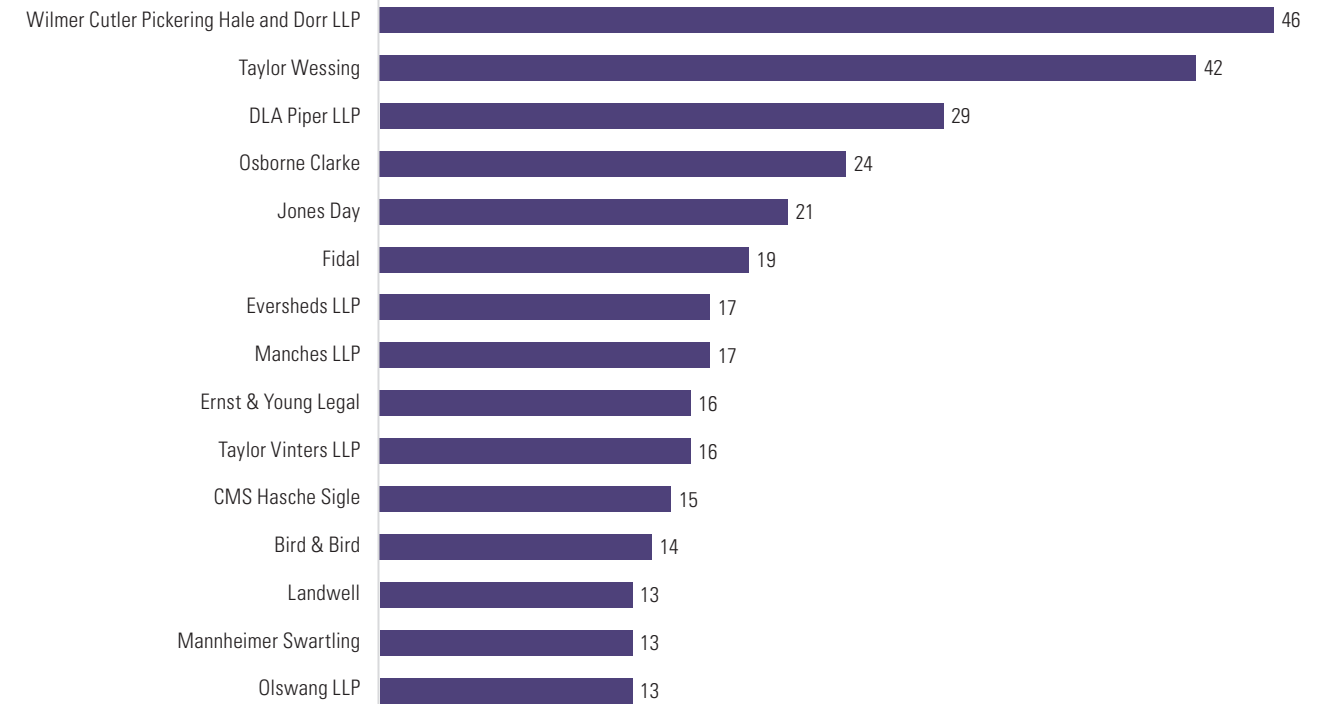
Source: Dow Jones VentureOne

European Venture-Backed IPOs and Acquisitions – 2000 to 2011



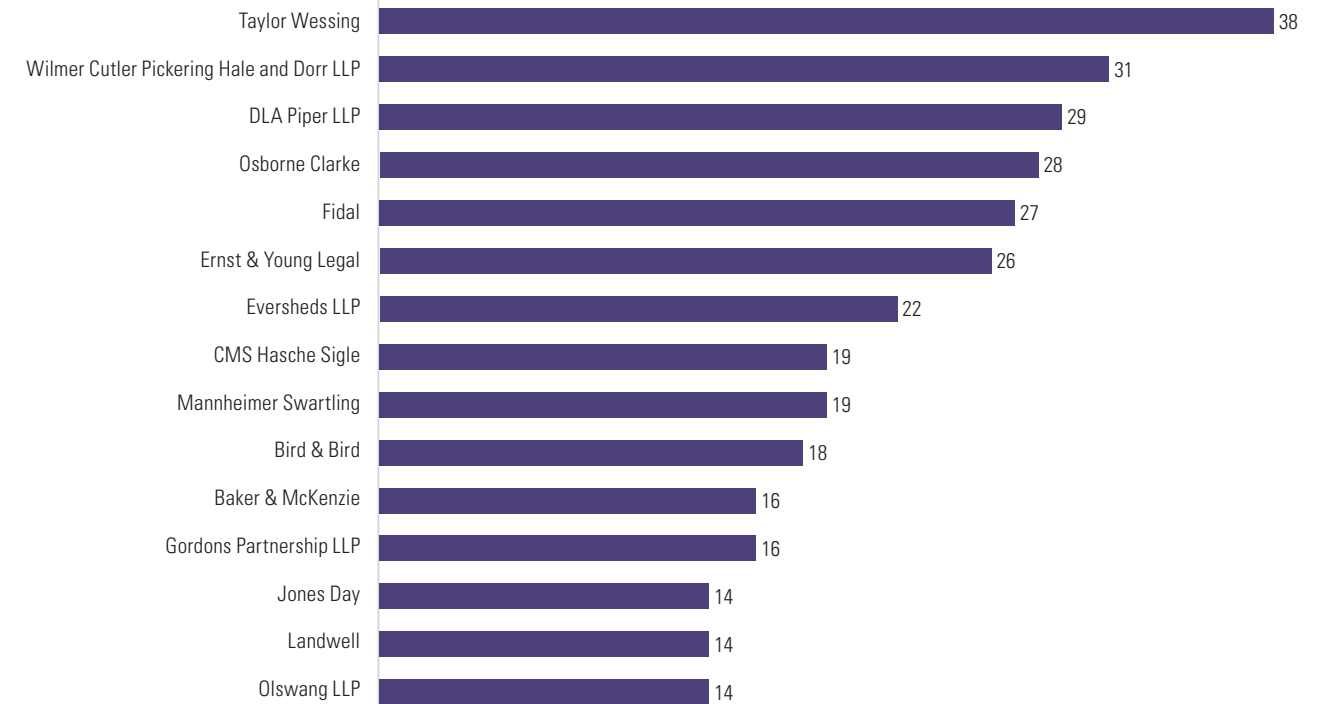
Source: Dow Jones VentureOne

Counsel to European Companies Receiving VC Financing — 2007 to 2011



The above chart is based on European companies that completed a seed, first, second, later-stage or restart round of venture capital financing between 2007 and 2011. Source: Dow Jones VentureOne

Counsel to VC-Backed Companies at Year-End 2011 – Europe



The above chart is based on European VC-backed companies that were private and independent as of the end of 2011. Source: Dow Jones VentureOne

Enacted with great fanfare on April 5, 2012, the Jumpstart Our Business Startups Act (JOBS Act) is intended to spur job creation and economic growth by improving access to the capital markets for startup companies. In addition to facilitating IPOs by relaxing certain disclosure regulations and accounting and auditing standards for “emerging growth companies,” the JOBS Act loosens fundraising restrictions on private companies and increases the maximum number of stockholders a private company may have without being forced to become an SEC reporting company.

ELIMINATION OF BAN ON GENERAL SOLICITATION

Current SEC rules prohibit general solicitation and general advertising to attract investors in private placements conducted pursuant to Regulation D. Within 90 days after the JOBS Act’s enactment, the SEC is required to amend its rules to permit general solicitation and general advertising in placements under Rule 506 (which is part of Regulation D), provided that all purchasers in those transactions are accredited investors. The SEC is also required to eliminate the prohibitions in Rule 144A placements on general solicitation, general advertising and making offers to investors who are not qualified institutional buyers, as long as all purchasers are qualified institutional buyers. A company must take reasonable steps to verify that purchasers are accredited investors or qualified institutional buyers, as applicable, using methods to be determined by the SEC.

NEW CROWDFUNDING EXEMPTION

Upon adoption of SEC rules within 270 days after enactment of the JOBS Act, private US companies will be able, without registration, to publicly offer and sell up to \$1 million of securities in “crowdfunding” transactions within a 12-month period, subject to the following restrictions:

- The amount any individual investor may invest must not exceed (1) the greater of \$2,000 or 5% of the annual income or net worth of the investor, if either

the annual income or net worth of the investor is less than \$100,000, and (2) 10% of the annual income or net worth of the investor, not to exceed a maximum aggregate investment of \$100,000 by the investor, if either the annual income or net worth of the investor is equal to or more than \$100,000.

- An intermediary, either a broker or “funding portal,” must be used in the transaction, and the intermediary must, among other things, register with the SEC; register with any applicable self-regulatory organization; ensure that investors understand the risks of the investment and can bear the burden of possibly losing the investment; conduct a background check on each officer, director and 20% stockholder of the company; make sure that no investment limits are exceeded; and comply with any other requirements the SEC may prescribe.
- Companies have to file with the SEC and provide certain information to investors, including an anticipated business plan, the financial condition of the company, a description of the intended use of the proceeds, and a description of the ownership and capital structure of the company.
- Investors have a private right of action for rescission under the Securities Act for material misstatements and omissions. Claims may be brought against the company; the company’s directors, principal executive officers, principal financial officer, controller or principal accounting officer; and any person who offers or sells the security in the offering.
- Companies need to disclose a target offering amount and the deadline to reach the target offering amount. Companies must provide regular updates regarding their progress in meeting the target offering amount.
- Companies must not advertise the terms of the offering, except for notices that direct investors to the intermediary. Companies may not compensate, directly or indirectly, anyone for promoting the offering through the intermediary’s communication channels, without

taking the proper steps, which the SEC shall determine, to ensure that such promoter discloses that compensation in each promotional communication.

- Companies must file ongoing reports with the SEC, including financial statements, subject to rules, exceptions and termination dates to be determined by the SEC, and comply with such other requirements as the SEC may prescribe.
- Investors may not resell securities for one year, beginning on the date of purchase, except to the company; to an accredited investor, as part of an SEC-registered offering; to family members; or in connection with death or divorce.

HIGHER STOCKHOLDER THRESHOLD FOR EXCHANGE ACT REGISTRATION

The JOBS Act increases the stockholder threshold at which an issuer must register its securities under the Exchange Act and become an SEC reporting company from 500 holders of any class of equity security to either (1) 2,000 persons, or (2) 500 persons who are not accredited investors.

For purposes of the new threshold, securities held by persons who received the securities pursuant to an employee compensation plan in transactions exempt from registration under the Securities Act (such as Rule 701) are excluded. In addition, within 270 days after enactment of the JOBS Act, the SEC is required to exempt securities acquired pursuant to crowdfunding transactions from the minimum stockholder threshold for Exchange Act registration, subject to any conditions the SEC prescribes.

The increase in the registration threshold and the exclusion from such calculations of securities issued in employee compensation and crowdfunding transactions will allow some large private companies to remain private longer, and may allow some companies to avoid creating new classes of equity security as a workaround to the old 500-person limit. The change may also encourage some companies to grant equity more broadly within the company or to stop including restrictions on grants that were intended to keep the company below the 500-person limit. ■

The improper classification of an employee as an independent contractor (or other non-employee) can expose an employer to significant tax and non-tax liabilities. Although employers of any size can encounter these issues, startup companies—often motivated to utilize contractors for greater flexibility—are particularly prone to incorrect employee classifications.

WORKER CLASSIFICATION

Generally, a worker is properly classified as an employee when the business for which the worker performs services has the right to determine not just *what* work must be accomplished but also *how* that work must be accomplished. Whether a business has this right to “direct and control” a worker depends on the facts and circumstances of the particular relationship. No one fact is determinative, and facts and circumstances that are relevant in the context of one industry or state may not be relevant in another.

Although many determinations are fairly straightforward—a salaried, benefits-eligible worker who has signed an employment agreement requiring the worker to adhere to the company’s policies and procedures and to refrain from working for any other businesses (generally an employee), versus a worker hired to complete a specific task that is outside the company’s ordinary course of business within a fixed timeframe for a fixed fee and who may simultaneously provide the same or similar services for other businesses (generally a non-employee)—many may be unclear. For example, a worker who is paid on commission, reimbursed for any work-related expenses, may work either from home or business premises, and is provided a handbook of the employer’s general policies but is free to perform the same or similar work for other parties that do not directly compete with the employer’s business could be either an employee or a non-employee.

CONSEQUENCES OF WORKER MISCLASSIFICATION

As difficult as it may be to classify a worker, failure to do so properly has important tax and non-tax consequences. Worker misclassification implicates a business’s federal income tax withholding obligations, as well as Social Security, Medicare and unemployment taxes otherwise payable, and may expose the employer to significant penalties and interest charges. Potential non-tax liabilities include the failure to provide workers’ compensation and unemployment insurance; violations of employment discrimination and immigration laws, overtime requirements and pension plans; and the failure to provide certain benefits, such as paid vacation, sick time, equity and bonus opportunities, and contributions to pension plans that are otherwise provided to employees.

VOLUNTARY CLASSIFICATION SETTLEMENT PROGRAM

In the fall of 2011, the Internal Revenue Service (IRS) launched the Voluntary Classification Settlement Program (VCSP). The VCSP allows eligible employers to prospectively reclassify as employees workers erroneously classified as independent contractors or other non-employees, and significantly reduces the federal tax liability related to the worker misclassification for prior years.

An employer may participate in the VCSP if it meets certain eligibility requirements:

- the employer must have consistently treated the class of workers to be reclassified as non-employees and filed all required Forms 1099 for each relevant worker for the previous three years; and
- the employer may not be under audit by the IRS at all or under audit by the US Department of Labor (DOL) or a state agency specifically with respect to the classification of workers. If the employer has previously been audited by the IRS or DOL concerning the classification of workers, it is eligible for the program only if it has complied with the results of the audit.

The employer must file an application for the VCSP with the IRS on new Form 8952 at least 60 days before the date it wants to begin treating its workers as employees. Once accepted into the VCSP, the employer enters into a closing agreement with the IRS, pursuant to which it agrees to:

- treat the class or classes of workers it wishes to reclassify as employees for future tax periods;
- pay 10% of the employment tax liability that may have been due on compensation paid to the workers for the most recent tax year, as determined from the already reduced rates available for reclassification; and
- for the first three calendar years after the agreement is signed, be subject to a special six-year statute of limitations on the assessment of employment taxes, instead of the three-year period that would otherwise generally apply.

In exchange for agreeing to these conditions, the employer will not be liable for any interest or penalties on the employment tax liability amount paid under the agreement and will not be subject to an employment tax audit with respect to worker classification of the reclassified workers for prior years.

CONCLUSION

Although the VCSP is not a panacea (it does not provide any relief for non-tax liabilities attributable to worker misclassification and there is a 10% tax liability), it provides employers with a means to prospectively reclassify workers and significantly reduce the federal tax liability related to worker misclassification for prior years. In addition, employers can take comfort that participation in the VCSP will not open an employer to retrospective reclassification of employees for DOL or state agency purposes: the IRS has said it will not share any of the information gleaned from VCSP applications with the DOL or the states. Still, an employer’s decision as to whether to avail itself of the VCSP should be made based on all relevant facts and legal considerations. ■

Based on hundreds of venture capital financing transactions we handled from 2007 to 2011 for companies and venture capitalists in the United States and Europe, we have compiled the following deal data:

Deals with Multiple Liquidation Preferences		2007	2007 Range	2008	2008 Range	2009	2009 Range	2010	2010 Range	2011	2011 Range
A "multiple liquidation preference" is a provision that provides that the holders of preferred stock are entitled to receive more than 1x their money back before the proceeds of the liquidation or sale are distributed to holders of common stock.	Series A	4%	1.5x – 2x	3%	3x	0%	N/A	4%	2x	7%	1.2x – 3x
	Post-Series A	7%	1.5x – 2x	14%	1.3x – 3x	19%	1.5x – 5x	10%	1.5x – 2x	4%	1.3x – 1.5x
Deals with Participating Preferred		2007	2007 Range	2008	2008 Range	2009	2009 Range	2010	2010 Range	2011	2011 Range
"Participating preferred" stock entitles the holder not only to receive its stated liquidation preference, but also to receive a pro-rata share (assuming conversion of the preferred stock into common stock) of any remaining proceeds available for distribution to holders of common stock.	Series A Total	57%		53%		30%		33%		24%	
	Capped	42%	2x – 6x	35%	2x – 5x	25%	2x – 3x	18%	2x – 3x	45%	2x – 3x
	Post-Series A Total	62%		56%		57%		44%		34%	
	Capped	37%	2x – 5x	41%	2x – 5x	35%	2x – 6x	45%	1.6x – 5.5x	30%	1.75x – 8x
Deals with an Accruing Dividend		2007	2008	2009	2010	2011					
"Accruing dividends" are generally payable upon liquidation or redemption of the preferred stock. Because the sale of the company is generally deemed to be a "liquidation," the accrued dividend effectively increases the liquidation preference of the preferred stock.	Series A	43%	53%	41%	23%	18%					
	Post-Series A	38%	36%	41%	30%	43%					
Anti-Dilution Provisions		2007	2008	2009	2010	2011					
A "full ratchet" anti-dilution formula is more favorable to the investors because it provides that the conversion price of the preferred stock will be reduced to the price paid in the dilutive issuance, regardless of how many shares are involved in the dilutive issuance. In contrast, a "weighted average" anti-dilution formula takes into account the dilutive impact of the dilutive issuance based upon factors such as the number of shares and the price involved in the dilutive issuance and the number of shares outstanding before and after the dilutive issuance.	Series A										
	Full Ratchet	9%	6%	0%	0%	2%					
	Weighted Average	91%	94%	100%	100%	98%					
	Post-Series A										
Full Ratchet	5%	5%	9%	4%	3%						
Weighted Average	95%	95%	91%	96%	97%						
Deals with Pay-to-Play Provisions		2007	2008	2009	2010	2011					
"Pay-to-play" provisions provide an incentive to investors to invest in future down rounds of financing. Investors that do not purchase their full pro-rata share in a future down round lose certain rights (e.g., their anti-dilution rights are taken away or their shares of preferred stock may be converted into common stock).	Total	28%	23%	35%	20%	19%					
	% of Total That Convert to Common Stock	79%	92%	87%	100%	82%					
	% of Total That Convert to Shadow Preferred Stock	21%	8%	13%	0%	18%					

We reviewed all merger transactions between 2005 and 2011 involving venture-backed targets (as reported in Dow Jones VentureOne) in which the merger documentation was publicly available and the deal value was \$25 million or more. Based on this review, we have compiled the following deal data:

Characteristics of Deals Reviewed	2005	2006	2007	2008	2009	2010	2011	
Sample Size	39	53	33	25	15	17	51	
Cash	69%	68%	48%	76%	60%	71%	73%	
Stock	10%	8%	0%	4%	0%	6%	4%	
Cash and Stock	21%	24%	52%	20%	40%	23%	23%	
Deals with Earnout		2005	2006	2007	2008	2009	2010	2011
With Earnout	15%	17%	39%	12%	27%	29%	29%	
Without Earnout	85%	83%	61%	88%	73%	71%	71%	
Deals with Indemnification		2005	2006	2007	2008	2009	2010	2011
With Indemnification								
By Target's Shareholders	100%	94%	100%	96%	100%	100%	98%	
By Buyer ¹	46%	38%	48%	48%	36%	17%	43%	
Survival of Representations and Warranties ²		2005	2006	2007	2008	2009	2010	2011
Shortest	9 Months	12 Months	6 Months ³	12 Months	6 Months	9 Months	12 Months ⁴	
Longest	24 Months	36 Months	36 Months	24 Months	18 Months	21 Months	24 Months	
Most Frequent	12 Months	12 Months	12 and 18 Months (tie)	12 Months	18 Months	18 Months	18 Months	
Caps on Indemnification Obligations		2005	2006	2007	2008	2009	2010	2011
With Cap	100%	100%	97%	95%	100%	100%	100%	
Limited to Escrow	79%	84%	78%	81%	71%	71%	77%	
Limited to Purchase Price	5%	2%	9%	14%	0%	6%	2%	
Exceptions to Limits ⁵	73%	84%	97%	62%	71%	94%	96%	
Without Cap	0%	0%	3%	5%	0%	0%	0%	
Escrows		2005	2006	2007	2008	2009	2010	2011
With Escrow	97%	96%	94%	96%	93%	100%	94%	
% of Deal Value								
Lowest	2%	3%	3%	3%	10%	2%	5%	
Highest	20%	20%	43%	15%	15%	25%	31%	
Most Frequent	10%	10%	10%	10%	10%	10%	10%	
Length of Time								
Shortest	6 Months	12 Months	6 Months	12 Months	12 Months	9 Months	12 Months	
Longest	24 Months	36 Months	60 Months	36 Months	18 Months	36 Months	36 Months	
Most Frequent	12 Months	12 Months	12 and 18 Months (tie)	12 Months	12 and 18 Months (tie)	18 Months	18 Months	
Exclusive Remedy	84%	90%	73%	83%	46%	53%	78%	
Exceptions to Escrow Limit Where Escrow Was Exclusive Remedy⁵	66%	86%	100%	85%	83%	80%	97%	
Baskets for Indemnification		2005	2006	2007	2008	2009	2010	2011
Deductible	38%	48%	48% ⁶	43% ⁷	43%	56%	38% ⁸	
Threshold	62%	52%	39% ⁶	48% ⁷	57%	44%	60% ⁸	
MAE Closing Condition		2005	2006	2007	2008	2009	2010	2011
Condition in Favor of Buyer	82%	98%	97%	88%	100%	100%	98%	
Condition in Favor of Target⁹	13%	23%	44%	21%	20%	19%	15%	
Exceptions to MAE		2005	2006	2007	2008	2009	2010	2011
With Exception¹⁰	79%	85%	91%	92%	93%	94%	94% ¹¹	

¹ The buyer provided indemnification in 25% of the 2005 transactions, 41% of the 2006 transactions, 53% of the 2007 transactions, 50% of the 2008 transactions, 40% of the 2009 transactions, 80% of the 2010 transactions, and 29% of the 2011 transactions where buyer stock was used as consideration. In 17% of the 2005 transactions, 35% of the 2006 transactions, 56% of the 2007 transactions, 25% of the 2008 transactions, 40% of the 2009 transactions, 33% of the 2010 transactions, and 23% of the 2011 transactions where the buyer provided indemnification, buyer stock was used as consideration.

² Measured for representations and warranties generally; specified representations and warranties may survive longer.

³ In two cases representations and warranties did not survive, but in one such case there was indemnity for specified litigation, tax matters and appraisal claims.

⁴ In one case representations and warranties did not survive.

⁵ Generally, exceptions were for fraud, willful misrepresentation and certain "fundamental" representations commonly including capitalization, authority and validity. In a limited number of transactions, exceptions also included intellectual property representations.

⁶ Another 13% of these transactions used a "hybrid" approach with both a deductible and a threshold.

⁷ Another 4% of these transactions used a "hybrid" approach with both a deductible and a threshold and another 4% had no deductible or threshold.

⁸ Another 2% of these transactions used a "hybrid" approach with both a deductible and a threshold.

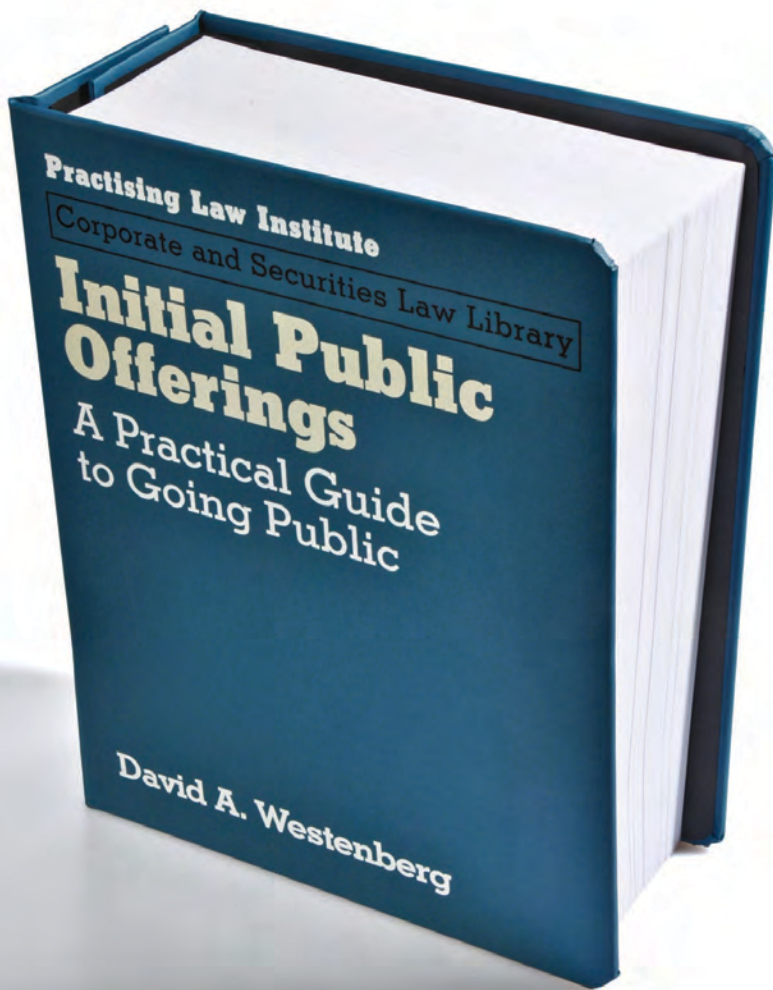
⁹ In 80% of these transactions in 2005, 83% of these transactions in 2006, 86% of these transactions in 2007, 60% of these transactions in 2008, 100% of these transactions in 2009, 67% of these transactions in 2010, and 86% of these transactions in 2011, buyer stock was used as consideration.

¹⁰ Generally, exceptions were for general economic and industry conditions.

¹¹ Excludes one transaction where the specified exceptions do not apply for purposes of a standalone "material adverse effect" closing condition.

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Data Sources

WilmerHale compiled all data in this report from the VentureSource database from Dow Jones VentureOne, except as otherwise indicated. For law firm rankings, IPOs by VC-backed companies and sales of VC-backed companies are included under the current name of each law firm.

Special note on data: Due to delayed reporting of some transactions, the venture capital financing and M&A data discussed in this report is likely to be adjusted upward over time as additional deals are reported. Based on historical experience, the adjustments in US data are likely to be in the range of 5–10% in the first year following the initial release of data and in smaller amounts in succeeding years, and the adjustments in European data are likely to be more pronounced.



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