The University of Pennsylvania
The Wharton School
Management Department

Venture Capital and Entrepreneurial Management

MGMT 804 – WEMBA East, Spring 2014

Raffi Amit
Robert B. Goergen Professor of Entrepreneurship
Phone: (215) 898-7731
Email: amit@wharton.upenn.edu
http://www.wharton.upenn.edu/faculty/amit.html

Doug Collom
Vice Dean, Wharton | *San Francisco*
Phone: (415) 267-6314
Email: collom@wharton.upenn.edu

TA: TBA

Course Overview and Design

This elective course focuses on venture capital and the typical venture-backed start-up company, based on conventions and practices in the United States.

Venture capital and the technology sector that it supports[1] continue to evolve structurally. This evolution traces from the dot-com bubble of 1998-2000; the dramatic economic upheaval in 2008-2009; the explosive growth of companies with an Internet-based business model; the globalization of business in general; the expansive adoption of consumer-based technologies, products and services; and other influential changes. Our class will cover traditional conventions in the industry that have historically shaped investor and company behaviors, as well as the structural changes that we are witnessing now.

Among the many factors that are currently impacting the industry, we will discuss the following:

- Venture capital funds typically have a 10-year life, and venture capital as an asset class that developed the late 1970's has historically produced a 15-20% pooled return on investment. But the soaring returns resulting from the dot-com era and the inflated valuations during this period crashed hard, and for many years in the decade following the bust, venture capital returns were deeply in the red. At the end of 2010, the average pooled return for the industry was still negative (-2.2%), and only nudged back into positive territory in 2011 (3.3%)—considerably underperforming the S&P 500 and the Russell 2000 during the last few years. So why is venture capital still viable? Because today, average returns for the last 25 years, inclusive of the dark years following the bust, are at 19.8% (in comparison with the S&P 500 and the Russell 2000 which over the same period stand at 9.2% and 9.4% respectively).

[1] For purposes of our class, the technology sector includes companies in a wide range of industries that look to venture capital as a principal financing resource. These industries include traditional technology companies (software, internet, semiconductor, electronic hardware, etc.), biotech companies (medical device, pharmaceutical, healthcare, etc.), clean and green tech companies (fuel cell, solar panel, wind, battery storage, conservation technologies, etc.), homeland security companies, and consumer companies (social media, e-commerce, gaming, Web 2.0, etc.).

- That's not to say the venture capital industry has had an easy time of it. The industry is experiencing a period of seismic change, perhaps one that permanently changes the infrastructure. The VC industry is still in a state of contraction. Of the approximately 1,000 VC firms in existence in 2000, only about 300 are still actively investing today. In a similar vein, of the approximately 9,000 principals in the VC industry in 2007, that number has declined to approximately 6,000 in 2013. As a corollary to the state of industry contraction, there is a remarkable "flight to quality" among the institutions that provide funding as limited partners to the venture firms. As a result, the top tier firms such as Sequoia Capital, Andreessen Horowitz, Kleiner Perkins, Accel and others have been successful in both fundraising and securing deal flow, while many lesser firms are changing their business models, downsizing, or just quietly closing up shop.

- Structural changes to the investment ecosystem are unprecedented and having a major impact on the traditional venture capital model. The range of resources and tools that are now freely available to founders has substantially lowered the required initial capital to start a business—this development has resulted in an explosion of new early stage companies, and has greatly reduced the dependence of the entrepreneurial community on VC firms for traditional early stage funding. In addition, the investment ecosystem abounds in alternative financing channels that have recently emerged, including: incubators and accelerators that provide money as well as mentoring; legitimate crowdfunding made possible by recent regulatory changes; "demo days" sponsored by numerous business associations, angels and super-angels; "stage-agnostic" VC firms willing to make small investments simply to get access to promising young startups; even PE firms and investment banking firms looking to build a relationship with the prospect of future business. With all these alternative financing sources now in play, the competition for deal flow is intense, forcing the traditional institutional VC firms to rethink their business models and re-evaluate their competitive strategies. It is also tilting the playing field strongly in favor of entrepreneurs as they negotiate financing terms with VCs.

- There are two ways for an investor typically to "exit" a venture-backed business—either by way of an IPO or through a merger or acquisition. Since the dotcom bust in 2000, the U.S. public equity markets have been constrained. During the period from 1990-1999, the U.S. markets witnessed an average of 500 IPOs per year; since the dotcom bust, the average number of IPOs has fallen to well below 100 a year. There has lately, however, been a resurgence of tech companies successfully completing IPOs, providing working capital for the company and liquidity for shareholders. As of the end of the third quarter in 2013, there were a total of 54 tech company IPOs—already more than the 50 tech company IPOs that were completed in all of 2012. During that same quarter, a total of 81 additional companies (tech and non-tech) have filed registration statements, promising a solid pipeline of more IPOs to come in future quarters. Although there is some concern that the activity and valuation levels are beginning to feel like the "bubble" that preceded the dotcom crash, the tech companies going public today tend to be more mature, have established business models and indicate higher sustainability. The health of the VC industry in general, in terms of liquidity and financial returns, crucially depends on the continuation of this current trend.
- In the social media/consumer app/mobile/internet gaming space, startup companies frequently require only modest amounts of capital—in some cases less than $50,000—to demonstrate proof of concept, and their all-in equity capital requirements are significantly less than in

sectors such as semiconductors, enterprise software, big data, cloud computing, 3-D printing and the like. In addition, the time horizon for a startup in this space to achieve an exit through a sale or merger frequently requires only two or three years (to wit, the sale of Instagram to Facebook for $1.01 billion took only 24 months from start to sale; similarly, it took Snapchat 26 months to prompt a rumored purchase offer of $4 billion from Google—which the founders have turned down). Valuations at these levels are both good and bad: they attract enormous interest from the entrepreneurial community that generates the launch of many new startups; but the resulting tidal wave of seed stage companies looking for their first institutional financing has resulted in a "Series A crunch," and more recently a "Series B crunch" as the market winnows out even funded companies that lack solid prospects.

Other factoids and observations about the state of play in the startup/venture capital arena:

- Based on a sampling of 549 ventures, the average age of a successful entrepreneur in high growth industries is 40. Twice as many successful entrepreneurs are over 50 as under 25. Over 75% of entrepreneurs have more than 6 years of industry experience, and half have more than 10 years when they launch a startup.

- A notable compensation trend is that founder/CEO's are taking lower salaries in favor of negotiating for a higher percentage of equity; in the period from 2011 to the present day in 2013, founder/CEO salaries have declined 24%, equity has increased 32%.

- Based on a database of 30 top startup companies held in the portfolio of one prominent VC firm in the last few years:
    - The median founders team consisted of two individuals (average is 2.4 individuals)
    - 54% of the teams had at least one "technical" founder
    - 30% of the teams had no technical founders
    - 10% of the founders had an MBA

The course will take all of these factors into consideration from the different and distinct perspectives of both the entrepreneur and the venture capital investor (including the angel and early stage professional investor). As well, we will address management issues regarding the working relationship between the VC and the entrepreneur, corporate governance, and executive compensation.

The entrepreneur's perspective addresses the challenges in organizing and financing the venture. Examination of this perspective reveals how entrepreneurs gain an understanding of the context and mechanics of valuing the business. Together, these matters help define the financing requirements of the business and suggest the approach for where and how to raise capital, and thereafter manage the relationship with investors.

Complementing, and sometimes in counterpoint to, the entrepreneur's outlook, is the perspective of the professional investor, which explores issues of concern to investors in evaluating, structuring and pricing venture capital investments. Insights gained from these class discussions will be valuable for students considering a career in venture capital, while also providing essential information for entrepreneurs. As we explore the venture capitalist's perspective, we will address several aspects of the investment process including the term sheet content and structure, term sheet negotiation, valuation methods, and the impact of successive rounds of financing on capitalization and ownership. All of these factors set the stage for the relationship between management and investors as well as the governance of the company.

The course is pragmatic in its orientation. We will attempt to expose students to both perspectives simultaneously. It will cover seven principal areas relevant to the privately held high-growth-potential start-up.

These include:

- A brief overview of the venture capital industry today, as well as a discussion of the typical venture fund structure and related venture capital objectives and investment strategies;

- Common organizational issues encountered in the formation of a venture-backed start-up, including matters relating to initial capitalization, intellectual property, and early stage equity incentive and compensation arrangements;

- Valuation methodologies that form the basis of the negotiation between the entrepreneur and the venture capitalist in anticipation of a venture investment;

- The challenges of fundraising, due diligence, financing strategies, and the importance of the business plan and presentation

- Elements of compensation, both cash and equity, that are common to venture-backed companies in the technology sector;

- Typical investment terms found in the term sheet and the dynamics of negotiation between the entrepreneur and the venture capitalist;

- Corporate governance in the context of a venture-backed start-up company and the typical dynamics that play out between VC and the entrepreneur in the post-financing phase.

The course is designed principally to address the interests of students who expect to embark on an entrepreneurial career, expect to assume a managerial role with a venture-backed start-up company, or wish to pursue a career in venture capital. The course assumes a basic understanding of general business principles. In light of the time constraints associated with a half-unit course, the curriculum is confined to key fundamentals in the area of venture capital and start-up companies. The course will touch upon a range of fields including finance, accounting, executive compensation, strategy and corporate law and will attempt to identify mainstream “best practices” in the area of high growth potential start-ups. Students completing the course will have a solid understanding of the questions and issues that face the typical start-up.

Other Course Features and Resources

- There will be a dedicated Canvas site for our course. Lecture notes, Caselettes, course materials that are not copyrighted by a third party and periodic announcements will be posted on this Canvas site. The Canvas URL is:

  https://wharton.instructure.com/courses/1224474

- **You will be able to access Study.net through Canvas. All third party copyrighted readings are found on Study.net. You should receive an email with log-in information from Study.net at the beginning of the semester. Please contact customerservice@study.net with any logon issues.**

Requirements and Evaluation

The assigned readings in the course are in the range of moderate to heavy, particularly at the beginning of the course. This syllabus, the assignments, and the readings have been organized so that students can manage the requirements efficiently. As in all courses, the lectures and discussions in the classroom will be much more meaningful if the required readings have been studied in advance. From time to time, mid-course changes in presentations or materials may be made to achieve academic objectives.

The readings are divided into two components: Required Readings and Supplemental Materials. The Required Readings are generally comprised of secondary source materials provided for background. The Supplemental Materials consist of optional reading materials and examples of legal or business documents included for the purpose of illustrating the themes discussed in class. All required readings and supplemental readings, organized by session, can be found on Canvas or in the Study.net window found on the Canvas website.

The short case studies, or caselettes, which will be used in this course are based on actual occurrences (with some degree of poetic license as appropriate) and are substantially shorter than the traditional case study. Each caselette has been prepared with the objective of highlighting "best practices," conventions in the industry, or issues that are commonly encountered. The caselettes will be found on Canvas, and are part of the required readings. The classes generally will involve both lecture and case discussions, with interaction and dialogue with the instructor strongly encouraged.

For each caselette, specific study questions have been assigned. In most class sessions, we will consider these questions and the material in the case.

Students are asked to form study group teams of up to 5 students per team. Study groups are expected to meet to discuss each caselette. Choose your teammates carefully – changes will not be allowed once your study group team has been formed. As a group assignment is due for our first class meeting, you are encouraged to form your study group before our first session.

Student Grades

The Wharton MBA grading practices will be used. The final course grade will be computed as follows:

• Classroom participation	15%
• Case memos and other assignments	25%
• Negotiation submissions & presentation	15%
• Quiz	45%

Individual class participation: Active class participation is very important for this course. The quality of your comments counts as much as your participation activity level. Because so much of the learning in this course occurs in the classroom, it is important that you attend every class. If you have to miss class, for one reason or another, please notify the instructor and the TA in advance by e-mail. All students are expected to participate in class discussions. Students should expect to be cold called. You are required to **display your Wharton issued name tent in each class to facilitate teacher/student interaction.** Note: Failure to display your Wharton issued name tent may result in not getting **<u>any</u>** credit for the class session in which your name tent was not displayed.

Case write-ups and other assignments: For each of the assigned caselettes or cases, before the start of class, each study group team will turn in a hard copy of the write-up in which the study questions are addressed. The instructors recognize the challenges of responding to the study questions of each caselette given the pace of the course.

The write-up should be double-spaced, font size 11, and as a guideline should be limited to four pages in length. The four page limit is for text only. You may attach as many numerical calculations as you wish BUT your submission must integrated into a single file. The names of the students in the study team must appear on front page of the memo. Write these as if you were writing a recommendation to the major decision-maker in the case.

Write-ups will not be accepted after the class has met. **Credit will only be given to write-ups which are submitted in hard copy at the <u>beginning</u> of the class to which the caselette was assigned**. **No credit will be given for write-ups which are handed in late or not handed in.**

Since 40% of your course grade depends on group work, you will be asked to evaluate the contributions of each of your study group colleagues using a form that will be distributed in class. The scores will affect individual grades on group assignments. Submission of this form in a timely manner is a requirement of this course.

QUIZ: Will be held on Saturday, February 15 during class time. It may be taken on an open book/open notes basis. Students should bring a calculator to the quiz. No laptops are allowed.

Note: The instructors will take great care to grade as fairly as possible. Students wishing to discuss their exam and/or grade must make an appointment with the TA to do so.

Lecture Notes

PDF files of the PowerPoint slides used in class will be posted onto Canvas prior to class.

Required Texts

Course Readings: MGMT 804: Venture Capital and Entrepreneurial Management, Spring 2014 edition, compiled by Raffi Amit and Doug Collom. All readings are available on Canvas or Study.net.

Learning Environment

Consistent with the MBA Resource Guide students are expected to strictly adhere to **Concert Rules,** including:

- Class starts and ends exactly on time. Students and faculty are expected to be prompt.
- Students remain in attendance for the duration of the class, except in an emergency. Students who leave the class while it is in session will be readmitted at the break.
- Students display their nameplates.
- All phones and electronic devices are turned off.

Note: The instructors, at their sole discretion, will apply grade penalties for any and all violations of these **Concert Rules**.

Management 804 Course Outline At-A-Glance WEMBA West, Spring 2014				
Session Number	***Date***	***Topic***	***Case/activity*** (Caselettes are located on Canvas)	***Submissions Due***
1	Friday, January 17, 2014 1:30 p.m. – 4:30 p.m.	Session 1A: Course Introduction: The VC industry Today-An Industry in Transition Session 1B: Organizational Issues and Initial Capitalization in the Formation of a Start-Up	Caselette #1: Organizational Issues in the Formation of a Start-Up	Case Memo
2	Saturday, January 18, 2014 7:30 a.m. – 12:00 p.m.	Session 2A: Fundraising Challenges Session 2B: First Round Financing Valuation Methodologies (Lecture Only) Session 2C: Lecture on Term Sheets	Caselette # 2: Considerations in Establishing the Initial Capitalization of the Start-Up Caselette # 3: Issues Encountered in Connection with a First Round Financing	Case Memos
3	Friday, January 31, 2014 1:30 p.m. – 4:30 p.m.	Session 3A: Valuation Methodologies Session 3B:The Term Sheet Session 3C: Term Sheet Negotiation Project Assigned and Explained	HBS Problem Set case #N9-396-090 Caselette #4: Liquidation Preferences and Anti-dilution Formulas Caselette #5: Analysis of a Typical Venture Capital Term Sheet	Prepare Questions 1-6 Case Memos
4	Friday, February 14, 2014 1:30 p.m. – 4:30 p.m.	Session 4A: Compensation Guest Speaker		

		Session 4B: In Class Review Session		
5	Saturday, February 15 7:30 a.m. – 9:00 a.m. 1:00 p.m. – 4:00 p.m.	Session 5A: Class Presentations on Term Sheet Negotiations Session 5B: Corporate Governance Session 5C: Quiz		Detailed guidance of negotiations in class See details of deliverables on page 15

Detailed Course Outline

Friday, January 17, 2014
1:30 p.m. – 4:30 p.m.

Session 1A: Course Introduction: The VC Industry Today; VC Firm Structure and Activities

Session 1B: Organizational Issues and Initial Capitalization in the Formation of a Start-Up
Submissions Due: Case Memo

Session 1A

- An overview and brief history of the venture capital industry and its role in fostering the growth firms
- Current industry trends
- The typical venture fund structure and investment terms; venture capital objectives and investment strategies; role of the general partners

Session 1A Required Reading

- "A Note on the Venture Capital Industry," Harvard Business School (HBS # 9-295-065, July 12, 2001)
- "How Venture Capital Works," by B. Zider, Harvard Business Review (Nov-Dec 1998)

Session 1A Supplemental Reading

- "3Q13 US Activity Sets Stage for Breakout Year," Renaissance Capital, 3Q13 Quarterly Review
- "A Hardware Renaissance in Silicon Valley," by Nick Bilton and John Markoff, The New York Times (August 26, 2012)
- "Can Entrepreneurship Be Taught?" by Noam Wasserman, Wall Street Journal (March 19, 2012)
    - "Yes: Learn About the Pitfalls," by Noam Wasserman, Wall Street Journal (March 19, 2012)
    - "No: The Best Class Is Real Life," by Victor W. Hwang, Wall Street Journal (March 19, 2012)
    - "Made or Born? Characteristics of successful entrepreneurs," by Ernst & Young, Wall Street Journal (March 19, 2012)
- "Dollars Invested by Venture Capitalists Rise 12 Percent in Q3 2013," PwC Money Tree Report (October 18, 2013)
- "Fund Performance: The Troubled Life of 1999 Funds," by Mark Boslet, Venture Capital Journal (October 15, 2012)
- "IPO Market Momentum Breaks Full Year 2013 Totals, According to PwC's Q3 IPO Watch," PwC Press Release (October 2, 2013)
- "Is the Venture Industry Shrinking? Not So Much," by Russ Garland, Wall Street Journal (June 10, 2013)
- "Math Beats Myth for LPs Investing in Venture," by Rory O'Driscoll, Scale Venture Partners (May 10, 2013)
- "Ouch: Ten Year Venture Returns Still Lag the Broader Markets," by Sarah Lacy, PandoDaily (July 30, 2013)
- "Silicon Valley: Feel the Froth," by Rolfe Winkler and Matt Jarzemsky, Wall Street Journal (October 17, 2013)
- "Spring In Venture Capital," by Todd Hixon, Forbes (September 18, 2013)
- "The Other Problem with Venture Capital: Management Fees," by Chris Dixon (August 26, 2009)
- "The VC Industry is Broken. Now What?" by Stacey Higginbotham, Bloomberg Business Week (May 8, 2012)
- "Venture Capital Funds Raised $4.1 Billion During Third Quarter 2013," National Venture Capital Association Press Release (October 7, 2013)
- "Venture Fundraising Flat as More LPs Avoid the Asset Class," by Joanna Glasner, Venture Capital Journal (October 2013)

- "Why VCs Aren't Insanely Rich," by Arie Shpanya, Venture Beat (October 21, 2013)
- National Venture Capital Association Yearbook 2013
- U.S. Venture Capital Index and Selected Benchmark Statistics, Cambridge Associates (June 30, 2013)

Session 1B

- Forming the company; creating a capital structure in preparation for venture funding
- Founders' stock and foundations of equity incentive arrangements
- Financial valuation methodologies; the art and the science of valuation
- Financing strategies and the impact of dilution

- ***Caselette #1*:** Organizational Issues in the Formation of a Start-Up **(Due at the beginning of class)**

Session 1B Required Reading

- "The Legal Forms of Organization," Harvard Business School (HBS # 9-898-245, February 19, 2004)
- "The Legal Protection of Intellectual Property," Harvard Business School (HBS # 9-898-230, April 17, 1998)
- "The Process of Forming the Company." Chapter 3 of High tech start-up: the complete handbook for creating successful new high tech companies, by J. Nesheim (2000)
- "Venture Capitalists," Chapter 9 in High tech start-up: the complete handbook for creating successful new high tech companies, by J. Nesheim (2000)

Session 1B Supplemental Reading

- "Avoiding Trouble: Provisions in Previous Employment Documents that Every Start-up Company Founder Needs to Review," by Yokum Taku, WSGR Entrepreneurs Report (Winter 2008)
- "Dividing Equity Between Founders," by Chris Dixon (August 23, 2009)
- "Don't Build Your Startup Outside of Silicon Valley," Harvard Business Review (October 23, 2013)
- "Dream Teams: The Characteristics of Billion-Dollar Startup Founders," by Tomasz Tunguz, Red Point (October 29, 2013)
- "Entrepreneurs Get Better With Age," by Whitney Johnson, Harvard Business Review Blog Network (June 27, 2013)
- "Vesting of Founders' Stock: Beyond the Basics," by Doug Collom, WSGR Entrepreneurs Report (Spring 2008)
- "Founder Vesting: Five Tips For Entrepreneurs," by Scott Edward Walker, Walker Corporate Law Group (September 10, 2009)
- "Selecting and Protecting a Company Name," by Aaron Hendelman, WSGR Entrepreneurs Report (Summer 2008)
- "Top 10 Intellectual Property Tips for Early-Stage Companies," by Peter Eng, WSGR Entrepreneurs Report (Summer 2008)
- "Starting Up: Sizing the Stock Option Pool," by Doug Collom, WSGR Entrepreneurs Report (Summer 2008)
- "Startup Companies and Financing Basics," by Yoichiro Taku, WSGR Entrepreneurs Report (Fall 2007)

Saturday, January 18, 2014
7:30 a.m. – 12:00 p.m.

Session 2A: Fundraising Challenges
Session 2B: First Round Financing
Valuation Methodologies (Lecture Only)
Session 2C: Lecture on Term Sheets
Submissions Due*: *Case Memos

Session 2A

- Raising Capital; the role of the business plan; fundraising strategies
- Due Diligence: content and process

Session 2A Required Reading

- "How to Write a Great Business Plan," by W. Sahlman, Harvard Business Review (July-Aug 1997)
- "VC Nomenclature and the Investor Spiral," by Manu Kumar, CNNMoney (May 16, 2011)

Session 2A Supplemental Reading

- "Best Practices For Raising a VC Round," by Chris Dixon (May 4, 2011)
- "David Cohen: Accelerators and Incubators are More than a Fad," by Mark Boslet, Venture Capital Journal (October 2012)
- "Due Diligence Reveals All," AlwaysOn: The Insider's Network (October 21, 2008)
- "Fundraising Workshop," Deloitte & Touche
- "How to Prepare for a Presentation to a VC," by Carl Showalter, Opus Capital
- "How to Raise Money," by Paul Graham (September 2013)
- "LinkedIn's Series B Pitch to Greylock – Pitch Advice for Entrepreneurs" by Reid Hoffman
- "Top Universities Producing VC-backed Entrepreneurs," Pitch Book Blog (October 23, 2013)
- "Venture Capital Firms, Once Discreet, Learn the Promotional Game," by Nicole Perlroth, New York Times (July 2012)
- "Vetting Entrepreneurs Is More Art Than Science," by Constance Loizos, Venture Capital Journal (July 2010)
- "Writing a Business Plan: Startup Ideas," Sequoia Capital
- Sample executive summaries

Session 2B

- Basic building blocks involved in equity financings with venture investors
- Corporate structures to support financing
- ***Prepare Caselette #2*:** Considerations in Establishing the Initial Capitalization of the Start-Up **(Due at the beginning of class)**
- ***Prepare Caselette #3*:** Issues Encountered in Connection with First Round Financing (**Due at the beginning of class)**

Session 2B Required Reading

- "Structuring the Financing," by Stanley C. Golder in Pratt's Guide to Private Equity Sources, by Thomson Venture Economics (2004)
- "Venture Capital Negotiations: VC versus Entrepreneur." Harvard Business School (HBS# 9-800-170, March 2, 2000)

Session 2B Supplemental Reading

- "Crowdfunding Successes Making VCs Take Notice," by Tom Stein, Venture Capital Journal (July 29, 2013)
- "Financing a start-up? Ask yourself these three questions." by Roger Ehrenberg, CNNMoney (May 19, 2011)
- "Naval Ravikant on Future of Angelist, What Worries Him," by Cromwell Schubarth, Silicon Valley Business Journal (July 26, 2013)
- "Perfecting Your Pitch," by Brad Feld, WSGR Entrepreneurs Report (Winter 2008)
- "Seed Funding Is Up, Silicon Valley/Bay Area Is Tops But…," by Cromwell Schubarth, Silicon Valley Business Journal (October 22, 2013)
- "Seed Venture Capital Funding In San Francisco Bay Area On Pace For Record Year," CB Insights (July 25, 2013)
- "Shackles Fall Off Fundraising For Startups. Should We Worry?," by Sarah

McBride, Venture Capital Journal (October 13, 2013)

- "Law Opens Financing of Start-Ups to Crowds," by Jenna Wortham, New York Times (September 22, 2013)
- "VCs Address Series A Crunch By Ramping Up Early-Stage Investing," by Mark Boslet, Venture Capital Journal (November 18, 2013)
- "VCs Flock To San Francisco As Deal Pace Soars," by Alastair Goldfisher, Venture Capital Journal (November 18, 2013)
- First Amended and Restated Articles of Incorporation

Session 2C

- Environmental factors surrounding term sheets
- Selected critical elements in venture term sheets

Session 2C Required Reading

- "Anti-Dilution Protection: What You Need to Know," by Mark Baudler, WSGR Entrepreneurs Report (Spring 2008)
- "Liquidation Preferences: What They Really Do," by Craig Sherman, WSGR Entrepreneurs Report (Winter 2007)

Session 2C Supplemental Reading

- "The Entrepreneurs Report: Private Company Financing Trends," Wilson Sonisini Goodrich & Rosati Professional Corporation (Q3 2013)
- "Q3 2013 Company Friendly Deal Terms as Up Rounds Increase," Cooley Venture Financing Report, (Q3 2013)
- "Competing In the Venture Capital Industry," by Michael B. Fishbein, Huffington Post (July 11, 2013)
- "Later Stage Rounds and 'Setting the Bar Too High,'" by Chris Dixon (December 13, 2011)
- "Navigating Down-Round and Dilutive Financings," by Yokum Taku, WSGR Entrepreneurs Report (Fall 2008)
- "What is a Convertible Bridge Note with a Price Cap?" By Yoichiro ("Yokum") Taku, (January 11, 2010)

Friday, January 31, 2014
1:30 p.m. – 4:30 p.m.

Session 3A: Valuation Methodologies
Session 3B: The Term Sheet
Session 3C: Term Sheet Negotiation
Project Assigned and Explained
Submissions Due: Prepare Questions 1-6; Case Memos

Session 3A

- ***Case Discussion*****:** The Venture Capital Method – Valuation Problem Set (HBS case # N9-396-090)**- Questions 1 through 6 are due at the beginning of class**

Session 3A Required Reading

- "A Note on Valuation in Private Company Settings." Harvard Business School (HBS # 9-297-050, April 2002)
- "Ownership, Dilution, Negotiation, and Valuation," Chapter 7 in High tech start-up: the complete handbook for creating successful new high tech companies, by J. Nesheim (2000)
- "Valuation: What It's Worth," Venture Edge 2001

Session 3A Supplemental Reading

- "Venture Capital Valuations On the Rise," Pitch book (October 1, 2013)
- "Welcome to The Unicorn Club: Learning From Billion-Dollar Startups," by Aileen Lee, Cowboy Ventures, TechCrunch (November 2, 2013)

Session 3B

- Review and discuss caselettes regarding term sheets
- ***Prepare Caselette #4:*** Liquidation Preferences and Anti-dilution Formulas (**Due at the beginning of class)**
- ***Prepare Caselette #5*:** Analysis of a Typical Venture Capital Term Sheet (**Due at the beginning of class)**

Session 3B Required Reading

- Convertible Note Financing (Summary of Terms)
- Memorandum of Terms for Preferred Stock (negotiated)
- Memorandum of Terms for Preferred Stock (non-negotiated company favorable)
- Memorandum of Terms for Preferred Stock (non-negotiated investor favorable)
- Terms for Private Placement of Series Seed Preferred Stock

Session 3B Supplemental Reading

- "How Do the Sample Series Seed Financing Documents Differ From Typical Series A Financing Documents?," by Yokum Taku, Wilson Sonsini Goodrich & Rosati (March 14, 2010)
- "Ideal First Round Funding Terms," by Chris Dixon
- "Memorandum of Terms," WSGR Term Sheet Generator
- "Plain Preferred Term Sheet," TheFunded Founder Institute
- "Rounds of Financing," Macabacus
- "Term Sheet for Series A Preferred Stock Financing," NVCA Model Documents
- Convertible Note Bridge Financing Summary of Terms
- Terms for Private Placement of Series Seed Preferred Stock

Session 3C
Term Sheet Negotiation Assignment

- Materials explained
- Selection of negotiating teams

Note: At the end of this class session we will confirm with you the pairing of the negotiation teams: Each team will be designated as either Entrepreneurs or as VCs.

We will pair two VC teams against a single Entrepreneur team. Each Entrepreneur team will get term sheets which reflect initial offers from the two different VC teams. Everyone will get a "backgrounder" document which explains the assignment in great detail.

For the class on **Saturday, February 15**, each team will be required to summarize and present to the class the results of the term sheet negotiation.

The exact details of the negotiation process and the presentations that are due on **February 14 or February 15** will be outlined in the materials which will be handed out to you.

Friday, February 14, 2014
1:30 p.m. – 4:30 p.m.

Session 4A: Compensation
Guest Speaker
Session 4B: In Class Review Session

Session 4A

- Compensation Elements
- ISOs and NSOs
- The impact of 123R on incentive compensation in the high growth potential company
- Implications of IRC section 409A
- Alternative forms of incentive compensation

Session 4A Required Reading

- "Five Compensation-Related Mistakes Startups Make (And Should Avoid)," by Caine Moss of WSGR, Venture Beat (February 9, 2010)
- "The Do's and Don'ts of Compensation for Early-Stage Company Employees," by Kristen Garcia Dumont and Jennifer Martinez, WSGR Entrepreneurs Report (Fall 2008)

Session 4A Supplemental Reading

- "Bay Area 150 Equity Compensation Practices," Compensia (October 2009)
- "If, Why, and How Founders Should Hire A 'Professional' CEO," by Reid Hoffman (January 21, 2013)
- "Option Pool Metrics Presentation," by Jim Brenner, Wilson Sonsini Goodrich & Rosati
- "The Unexpected Compensation Trends of Post-Series A Startup Founder/CEOs," by Tomasz Tunguz, Red Point
- Equity Compensation Overview Memorandum (WSGR)

Saturday, February 15, 2014

7:30 a.m. – 9:00 a.m.

1:00 p.m. – 4:00 p.m.

Session 5A: Class Presentations on Term Sheet Negotiations

Session 5B: Corporate Governance

Session 5C: Quiz

Submissions Due**: *Detailed guidance of negotiations in class. See details of deliverables below.***

Session 5A

During this session, teams will present their negotiated term sheets and discuss the issues they ran into during the negotiation.

Submissions Due:

- **Each investor team and the founders to prepare a PowerPoint presentation, which includes the final proposed valuations as well as commentary on the key terms that were critical in the negotiation of the term sheet.**
- **Founders additionally provide a detailed summary of the final agreement using the format outlined in the Negotiation Instruction handout which will be distributed in class.**

Session 5B

- Board members' duty to stockholders
- Composition and roles of the board of directors in the private company
- Sarbanes Oxley and the private company

Session 5B Required Reading

- "After The Term Sheet," by Dennis T. Jaffe and Pascal N. Levensohn (November 2003) (Missing Doc)
- "Rites Of Passage," by Pascal N. Levensohn (January 2006)

Session 5B Supplemental Reading

- "CEO Playbook for Early Stage Board Meetings," by Geoff Yang, Red Point (August 2, 2013)
- "Corporate Governance and Disclosure Practices of Venture-Backed Companies In U.S. Initial Public Offerings," Wilson Sonsini Goodrich & Rosati (July 2011-June 2012)
- "How to Turn A 'Bored' Meeting Into A Real Board Meeting," Venture Capital Journal (August 2006)
- "The Basic Responsibilities of VC-Backed Company Directors," by Working group on Director Accountability and Board Effectiveness (January 2007)

- "The Secret to Making Board Meetings Suck Less," First Round Review
- "VCs Take CEO and Board Relationships to the Next Level," by Ben Holzemer, Venture Capital Journal (July 2010)

Session 5C QUIZ

- **Bring your calculator**. (No laptops allowed.)
- *Open books*
- *Open notes*
- *Open minds…*