



**Fully Diluted  
Post Financing  
Capitalization:**

See attached Exhibit A (assuming a total investment of \$25,000,000).

**Closing:**

On or before June 30, 2002, with additional closings allowed for up to 30 days after the initial closing.

**Stock Option Plan:** The existing Stock Option Plan will be amended as part of this financing to increase the number of shares authorized under the plan. The total shares under the plan will be 35,000,000 after the proposed financing. These options will be awarded by the Board of Directors and will be subject to four-year vesting. Stock acquired by employees through the Option Plan will be subject to (1) the right of the Company to repurchase any non-vested stock at the price paid by the employee in the event of termination prior to four years of employment after the closing, (2) a right of first refusal in favor of the Company to purchase any vested stock at the bona fide offered price (which right terminates upon a public offering by the Company), and (3) a restriction against transfer of non-vested stock (other than to a family trust).

**Description of  
Preferred  
Stock:**

The Company will create a new series of Preferred Stock, the Series B Preferred Stock. The terms of the outstanding Series A Preferred Stock will be appropriately amended and restated such that all of the provisions below are substantially the same (except for matters with respect to the relative valuations of each such series and other matters indicated herein). The Series A Preferred and the Series B Preferred are collectively referred to as the "Preferred."

- (1) Dividends: Holders of the Preferred will be entitled to receive non-cumulative dividends at the rate of 9% per annum in preference to the common, when and if declared by the board. No dividends may be paid on the Common until such preferential dividend is paid in full and, thereafter, the holders of Preferred shall participate in any dividends declared on the Common on an as-converted basis.
- (2) Liquidation Preference: In the event of any liquidation or winding up of the Company, holders of the Series B Preferred will be entitled to receive on a pari passu basis with holders of the Series A Preferred and in preference to the holders of Common Stock or any other stock ranking junior to the Preferred an amount

("Liquidation Amount") equal to the greater of (i) their respective original purchase prices for such series plus any accrued but unpaid dividends or (ii) the amount that such holders would have received had they converted all Preferred Stock held by them to Common Stock immediately prior to such liquidation. After payment in full of the Liquidation Amount to the Preferred holders, the remainder of the proceeds will be paid to the holders of the Common Stock.

- (3) Merger or Reorganization of the Company: A merger, consolidation or reorganization of the Company may be deemed to be a liquidation at the discretion of the Requisite Holders. The "Requisite Holders" will be both (i) the holders of a majority of the Preferred and (ii) at least one of \_\_\_\_\_, \_\_\_\_\_ or \_\_\_\_\_ for so long as they maintain the Preferred investment. The conversion of Preferred into Common Stock of the Company shall be permitted at any time up to or simultaneously with the consummation of such merger, consolidation or reorganization of the Company.
- (4) Redemption: Unless all Preferred shares have been converted to Common, the holders of a majority of the outstanding Preferred may cause the company to repurchase the Preferred Stock at the greater of Fair Market Value (going concern basis) or the original purchase price plus accrued dividends, in two equal installments pari passu on same dates as Series A Preferred stockholders.

If the company is unable to perform to the terms of this provision, the Requisite Holders will have the right to select an intermediary or investment banker acceptable to the company to assist in the sale of the business. Management and all other stockholders will cooperate fully in the undertaking to sell the business at the time this right is exercised, with the goal of realizing Fair Market Value for the business.

- (5) Conversion: The holders of the Preferred will have the right to convert the Preferred at any time, at the option of the holder, into shares of the Common Stock of the Company. The total number of shares of the Common Stock into which the Preferred may be converted initially will be determined by dividing the Original Purchase Price per share plus any unpaid dividends by the conversion price per share. The initial conversion price for the Series B Preferred will be the Original Purchase Price. The conversion price for the Series A Preferred Stock will be adjusted to give effect to the anti-dilution protections triggered by the issuance of Series B Preferred. The conversion price will be subject to

adjustment as provided in Paragraph (7) below.

- (6) Automatic Conversion: The Preferred will be automatically converted into Common Stock at the then applicable conversion price, in the event of either (i) an underwritten public offering of shares of the Common Stock of the Company at a public offering price per share (prior to underwriter commissions and expenses) that reflects a pre-offering valuation of the Company of at least \$100,000,000 and in an offering with aggregate proceeds to the Company of not less than \$25,000,000 or (ii) the election of the Requisite Holders.
- (7) Anti-dilution Protection: If securities are subsequently issued at a price less than the conversion price, then a weighted average adjustment shall apply to the conversion price of the Preferred. The conversion price of the Preferred will also be subject to appropriate adjustment in the event that the Company effects a stock split, stock combination or stock dividend. Notwithstanding the provisions set forth above, no anti-dilution protection shall exist for issuance of securities to employees pursuant to the Stock Option Plan.
- (8) Pay-to-Play Feature: If any Purchaser that (together with its affiliated investment funds) holds at least 100,000 shares of Series B Preferred (a "Qualified Holder") fails to participate in any Qualified Financing (as defined below) on a full pro rata basis (according to its total equity ownership immediately prior to such financing), then all shares of Series B Preferred held by such Qualified Holder will lose their anti-dilution protection and preemptive rights for the Qualified Financing and future equity financings and such Series B Preferred will convert into Preferred Stock that will have identical rights to the Series B Preferred held by such Qualified Holder except for a different conversion price, no price-based anti-dilution provisions and no preemptive rights. A Qualified Financing is any down-round financing, including this proposed Series B Preferred financing, (i) approved by the Requisite Holders, (ii) in which holders of a majority of the Preferred participate on a full pro rata basis, (ii) where the Qualified Holders have been offered the opportunity to purchase their pro rata portion and (iii) such Qualified Holder declined to purchase its full pro rata portion.

When determining the number of shares held by a Purchaser or whether the provision has been satisfied, all shares held by or purchased in the Qualified Financing by affiliated investment funds shall be aggregated. A Qualified Holder shall be entitled to assign its rights to purchase shares of Preferred Stock to its affiliated funds, including funds which are not current stockholders of the

Company.

- (9) Special Ratchet: If the Company's gross revenues do not meet or exceed \$30,000,000 for the 12 months ending December 31, 2003, then the conversion price for Series A Preferred Stock will be reduced to \$\_\_\_\_\_ and the conversion price for the Series B Preferred Stock will be reduced to \$\_\_\_\_\_.
- (10) Voting Rights: The Requisite Holders must approve (i) any merger, sale of substantially all the assets, liquidation or dissolution; (ii) material and adverse changes in the rights, preferences or privileges of the Preferred; (iii) any increase or decrease in the authorized number of shares of the Preferred; (iv) any amendment to the Company's Certificate of Incorporation or Bylaws; (v) payment of dividends on Common Stock; (vi) any increase in the size of the Board; or (vii) the creation of any new class of shares having preference over the Preferred. The holders of the Preferred will be entitled to vote as a single class with the holders of the Common Stock on all other matters with each Preferred share having the number of votes equal to the number of shares of Common Stock issuable upon conversion of such Preferred share.
- (11) Preemptive Rights: The holders of at least 10,500,000 shares of Registrable Securities (each a "Major Stockholder") and the founders shall have the right to purchase a pro-rata portion of any securities offered by the Company in the future. A holder will have thirty (30) business days in which to exercise this preemptive right. Notwithstanding the provisions set forth above, no preemptive rights shall exist for issuance of securities if such issuance is to employees pursuant to the Stock Option Plan and issuances in connection with other typical offerings.
- (12) Transfer: The holders of the Preferred shall enter into an agreement which subjects the Preferred to: (1) a right of first refusal, exercisable within seven (7) business days of notice of a proposed sale, in favor of the other Preferred holders to purchase any Preferred shares offered for sale at the bona fide offer price and (2) a right of second refusal, exercisable within thirty (30) business days of the expiration of the Preferred holders' right of refusal, in favor of the Company or any third parties designated by the Company to purchase any remaining Preferred shares offered for sale at the bona fide offer price. These rights will terminate on an IPO.

## Registration

**Rights:**

The terms of the outstanding Series A Preferred Stock will be appropriately amended and restated such that all of the provisions below are substantially the same.

- (1) Demand Rights: If, at any time after the earlier of six months following an IPO or the date five (5) years from purchase of the Series A Preferred, holders of at least a majority of the Preferred (or Common Stock issued upon conversion of the Preferred or a combination of such Common Stock and the Preferred, all of which shares are hereafter referred to as "Registrable Securities") request that the Company file a registration statement under the Securities Act of 1933 covering a majority of the Registrable Securities, the Company will use its best efforts to cause such shares to be registered. The Company will not be obligated to effect more than two (2) registrations (other than on Forms S-2 and S-3) under these demand right provisions.
- (2) Registrations on Forms S-2 and S-3: Holders of 25% or more of the Registrable Securities will have the right, once per year, to require the Company to file registration statements on Form S-2 or Form S-3 (or any equivalent successor form) for at least \$1,000,000 per offering.
- (3) Piggyback Registration: Holders of Registrable Securities will be entitled to "piggyback" registration rights on all registrations of the Company, subject to the right of the Company and its underwriters, in view of the market conditions, to reduce the number of shares that the investors propose to be registered to the extent required by such market conditions.
- (4) Registration Expenses: Registration expenses (exclusive of underwriting discounts and commissions or the legal expenses of the selling stockholders) of two (2) demand registrations and all piggyback registrations will be borne by the Company, and all other expenses of registered offerings shall be borne pro-rata among the selling stockholders. The expenses of up to two (2) additional registrations on Form S-2 or Form S-3 will be borne by the Company.
- (5) Other Registration Provisions: The Registration Rights Agreement will contain other provisions which are customary in transactions of this kind.

**Information Rights:**

The Company will deliver to each Major Stockholder annual audited and monthly unaudited financial statements and an annual budget

prior to the beginning of each fiscal year as approved by the Board of Directors. In addition, the Major Stockholders will have visitation rights and will receive monthly executive summaries of the Company's activities.

**Right of First Refusal and Co-Sale:**

No Common Stock holder may transfer any shares without first offering such shares to the Company and then on a pro rata basis to the holders of the Preferred on the same terms as those received in a bona fide third-party offer. If the holders of the Preferred decline to purchase such shares, they shall be entitled to sell into such offer on a pro rata basis with the selling Common Stockholder.

**Board of Directors:**

At the closing of the sale of the Series B Preferred, the Board of Directors of the Company will consist of five (5) members, consisting of: (i) two nominees of the Common Stock, one of whom shall be the CEO of the Company (\_\_\_\_\_) and \_\_\_\_\_; (ii) one nominee designated by \_\_\_\_\_ (\_\_\_\_\_); (iii) two nominees of the Series B Preferred, one designated by \_\_\_\_\_ (for so long as it maintains its investment in the Company) and one designated by \_\_\_\_\_ (for so long as it maintains its investment in the Company). The size of the board may be increased to seven (7) members by a majority of the entire board, with one of such additional members to be an independent director designated by the board and the other to be designated by \_\_\_\_\_. Meetings of the Board will be held monthly until the Board decides a different schedule.

Directors will be indemnified by the Company to the fullest extent allowed by Delaware law.

**Standard Covenants and Representations:**

The purchase of the Series B Preferred will be made pursuant to a Stock Purchase Agreement and related agreements drafted by [Law Firm] and acceptable to the Company, which shall contain, among other things, appropriate representations and warranties of the Company, covenants of the Company reflecting the provisions set forth herein and other provisions typically found in such agreements, and appropriate conditions of closing which will include, among other things, qualification of the shares under applicable Blue Sky Laws, the filing of a Certificate of Designation and Determination of Preferences, and an opinion of counsel.

**Proprietary  
Information  
Agreements:**

Prior to closing, the Company will enter into Proprietary Information Agreements with all key employees. The Proprietary Information Agreements will contain provisions satisfactory to the Purchaser with respect to confidentiality, corporate ownership of inventions and innovations during employment, and non-competition and non-solicitation of employees and customers covenants during and after employment for two years.

**Special  
Relationships:**

As a part of due diligence, the company shall disclose in writing any special family relationships (spouse, sibling, parental, etc.) that exist between employees in the company. Any future hires involving family members shall require unanimous approval of the Board.

**Expenses:**

The Company will pay its own legal fees and reasonable legal fees of [Law Firm], counsel to the Purchasers.

**Conditions  
Precedent:**

The investment contemplated under the proposed terms would be subject to the following conditions:

1. The business, assets, financial condition, operations, results of operations and prospects of the Company are reasonably acceptable to the Investors.
2. Negotiation and execution of a definitive agreement setting forth representations and warranties of the Company and stockholders, covenants and other provisions customary in transactions of this nature.
3. Amendment of the Series A Preferred terms to closely conform with these proposed terms for the Series B Preferred stock financing, excluding the addition of the Pay to Play feature.
4. Completion of due diligence.
5. Approval of the financing by the current Board of Directors and the Stockholders of the company.