

**MEMORANDUM OF TERMS FOR THE PRIVATE PLACEMENT OF
SERIES A CONVERTIBLE PREFERRED STOCK**

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THIS TERM SHEET SUMMARIZES THE PRINCIPAL TERMS OF THE PROPOSED FINANCING OF (THE “COMPANY”). THIS TERM SHEET IS FOR DISCUSSION PURPOSES ONLY; THERE IS NO OBLIGATION ON THE PART OF ANY NEGOTIATING PARTY UNTIL ALL PARTIES SIGN A DEFINITIVE STOCK PURCHASE AGREEMENT. THE TRANSACTIONS CONTEMPLATED BY THIS TERM SHEET ARE SUBJECT TO THE SATISFACTORY COMPLETION OF DUE DILIGENCE. THIS TERM SHEET DOES NOT CONSTITUTE EITHER AN OFFER TO SELL OR AN OFFER TO PURCHASE SECURITIES.

FIRST ROUND OF FINANCING:

Amount to be Raised: \$ _____

Type of Security: Series A Convertible Preferred Stock (“Series A Preferred”).

Number of Shares: _____ shares.

Purchase Price: \$____ per share (the “Purchase Price”).

Investors: Certain members of the Tech Coast Angels (“TCA”)and other Qualified Investors.

Closing Date: The closing of the sale of the Series A Preferred (the “Closing”) will be on or before _____.

Post-Financing Capitalization:

<u>Class</u>	<u>Number of Shares</u>	<u>Percent</u>
Common Stock		
Employee Stock Option Pool		
Series A Preferred Stock		
Tech Coast Angels		
Total	<u>85,500,000</u>	<u>100.0%</u>

***Rights, Preferences, Privileges
and Restrictions of the
Preferred Stock:***

Dividends: The holders of shares of Series A Preferred Stock shall be entitled to receive cumulative dividends in preference to the holders of Common Stock at an annual rate of 5 % of the Purchase Price per share from legally available funds and when, as and if declared by the Board of Directors.

Voluntary Conversion: Each holder of Series A Preferred will have the right, at the option of the holder, at any time, to convert shares of Series A Preferred into shares of Common Stock at an initial conversion ratio of one-to-one.

Automatic Conversion: The Series A Preferred will be automatically converted into Common Stock, at the then applicable conversion rate, in the event of either (i) the election of holders of a majority of the then outstanding Preferred Stock, voting together as a class, or (ii) the closing of an underwritten initial public offering of the Company's Common Stock under the Securities Act of 1933 ("IPO") with aggregate proceeds of at least \$30 million at a public offering price of at least three (3) times the Purchase Price.

Redemption: Commencing five (5) years after the Closing, at the request of the holders of at least 2/3 of the then outstanding Series A Preferred, the Company will redeem the Series A Preferred at a redemption price equal to the Purchase Price plus any accrued and unpaid dividends.

Antidilution Provisions: The conversion price of the Series A Preferred shall be subject to an adjustment to prevent dilution in the event that the Company issues

additional shares of capital stock (other than common stock shares to employees, consultants, officers or directors pursuant to stock purchase or stock option plans or agreements approved by the Board, including options granted prior to the Financing) at a purchase price less than the applicable conversion price. In such an event, the conversion price shall be adjusted according to a weighted-average formula.

Liquidation Preference: In the event of any liquidation or winding up of the Company, the holders of the Series A Preferred will be entitled to receive, in preference to the holders of Common Stock, a preference amount per share consisting of the Purchase Price plus accrued and unpaid dividends, if any. Thereafter, the remaining assets of the Company will be distributed ratably to the holders of Common Stock and the Series A Preferred on an as-converted basis. A merger, acquisition or sale of all or substantially all of the assets of the Company in which the stockholders of the Company immediately prior to such event do not own a majority of the outstanding shares of the surviving corporation will be deemed to be a liquidation for purposes of the liquidation preference. The preference feature of this liquidation preference will be eliminated in the event of a liquidation where absent the preferential feature a liquidation of the Company would yield proceeds to the holders of Series A Preferred in excess of three (3) times the Purchase Price per share.

Voting Rights: The holders of shares of Series A Preferred will have the right to that number of votes equal to the number shares of common stock issuable upon conversion.

Protective Provisions

The consent of the holders of at least two thirds of the outstanding shares of Series A preferred stock (voting as a single class on an as converted basis) shall be required for any action that (i) effects a merger or sale of the Company, (ii) changes the rights, preferences or privileges of any series of preferred stock, (iii) increases or decreases the authorized number of shares of any series of preferred stock, (iv) increases the number of directors to more than seven, (v) creates a new class of stock or shares with a preference over or

on parity with the Series A Preferred with respect to voting, dividends, redemption, or upon liquidation, (vi) redeems or repurchases any shares of preferred or common stock, (vii) amends the Company's charter or bylaws, or (viii) pays cash dividends on the Company's common stock.

Employee Stock Option Pool

The Company will establish an Option Pool consisting of _____ to be granted to employees, consultants and directors of the Company pursuant to stock purchase or stock option plans or agreements approved by the Board. No more than ten percent (10%) options of the pool shall have been granted or promised as of the closing.

Vesting of management

A percentage _____ of Common Stock owned by existing and future management will be vested over four year term based on a pro rata vesting schedule.

Information Rights:

So long as a holder of Series A Preferred continues to hold 25% shares of the shares of Series A Preferred or Common Stock issued to such holder upon conversion of Series A Preferred, the Company will deliver to such holder annual and quarterly financial statements as well as an annual budget. The obligation of the Company to furnish such information will terminate at such time as the Company consummates an IPO or becomes subject to the reporting provisions of the Securities Exchange Act of 1934.

Right of First Offer:

Each holder of Series A Preferred will have a right of first offer in the event the Company proposes to offer equity securities to any person (other than (i) the issuance of capital stock to employees, consultants, officers or directors of the Company pursuant to stock purchase or stock option plans or agreements approved by the Board (including options granted prior to the Financing), (ii) the issuance of securities in connection with acquisition transactions, (iii) the issuance of securities to financial institutions or lessors in connection with commercial credit arrangements, equipment financings or similar transactions, (iv) shares issued upon conversion of the Series A Preferred, (v) the issuance of securities in a public offering, (vi) the issuance of securities pursuant to currently outstanding options, warrants, notes, or other

rights to acquire securities of the Company; or (vii) stock splits, stock dividends or like transactions) to purchase that portion of such equity securities equal to (a) the number of shares of Common Stock issued or issuable upon conversion of the Series A Preferred held by such holder of Series A Preferred divided by (b) all of the Company's Common Stock then outstanding or issuable upon exercise of options or warrants or conversion of Preferred Stock. Such equity securities shall be purchased within 20 days from notice by the Company and on the same terms as the securities are purchased by other third party purchasers of the equity securities. Such right of first offer will terminate upon an IPO or the acquisition of the Company.

The Company shall have a right of first refusal to purchase Common Stock prior to a transfer to a third party. Each of the holders of Series A Preferred and the other Common Stock holders shall have the right to purchase the shares not purchased by the Company.

***Co-Sale Right in Sales by
Common Stock holders***

If at any time prior to an IPO a holder of the Company's Common Stock seeks to sell his stock holdings to a party other than the Company, the holders of Series A Preferred will each have the right to participate in the transaction at the same terms and conditions as the selling Common Stockholder on a pro-rata basis.

Registration Rights:

Registrable Securities: All shares of Common Stock issuable upon conversion of the Preferred Stock shall be deemed "Registrable Securities."

Demand Registration: After the earlier of five years of the closing or six months after the Company has completed an IPO, holders of at least 2/3 of the Registrable Securities shall have one (1) demand registration right to request that the Company file a registration statement under the Securities Act of 1933, in order to permit such holders to sell their shares (subject to cutbacks at the underwriter's discretion).

Piggyback Registration Rights: The holders of Registrable Securities shall have unlimited piggyback registration rights, subject to pro rata cutback to a minimum of 20% of the offering (complete cutbacks on the IPO) at the underwriter's discretion.

Registration on Form S-3: Once the Company has completed an IPO, the holders of at least 20% of the Registrable Securities will have the right to require the Company to register their shares of Registrable Securities on the abbreviated registration statement on Form S-3, if available for use by the Company and only if such holders are not otherwise eligible to sell their Registrable Securities under Rule 144 of the Securities Act. The Company will not be obligated to effect more than two S-3 registration statements in any twelve-month period. There shall be a limit of a total of four such S-3 registrations.

Registration Expenses: Registration expenses (exclusive of underwriting discounts and commissions, stock transfer taxes and fees of counsel to the selling stockholders) will be borne by the Company for all demand, piggyback and S-3 registrations. The Company will also pay the reasonable fees and expenses of one special counsel to the selling stockholders.

Transfer of Registration Rights: The registration rights may be transferred to a transferee who acquires at least 75% shares of the original purchaser's Registrable Securities (or all of such the transferring holder's shares, if less), provided that the Company is given prompt notice of the transfer and the transferee agrees to be bound by the terms and conditions of the Registration Rights Agreement. Transfer of registration rights to a partner or affiliate or member of the immediate family of the transferee will be without restrictions as to minimum shareholdings.

Termination of Registration Rights: The registration obligations of the Company will terminate on the earlier of (i) five years after the IPO, or (ii) with respect to any holder of registration rights, at such time as all Registrable Securities of such holder may be sold within a three (3) month period pursuant to Rule 144 or (iii) at such time as a holder holds Registrable Securities constituting less than one percent (1%) of the outstanding voting stock of the Company.

Market Standoff: In connection with the IPO, each

holder of registration rights will be required not to sell or otherwise dispose of any securities of the Company (except for those securities being registered) for a period of 180 days following the effective date of the registration statement for such offering, and in connection with secondary offerings for a period of up to 120 days, if so requested by the underwriters of such offering.

Assignment of Technology:

The key employees of the Company (and/or holders of the Company's Common Stock) agree to assign to the Company all rights, title and interest in and to all technology and proprietary information owned by them relating to the Company's business.

Board of Directors:

Upon closing of the financing, the Bylaws of the Company shall provide that the Board of Directors of the Company shall consist of seven directors. The holders of Series A Preferred shall be entitled to elect three of the seven directors; at least two members shall be investors from the TCA group. The holders of Common Stock, voting as a separate class, shall be entitled to elect three of the seven directors, one of which shall be the CEO of the Company. The seventh position shall be an outside member chosen by the other six members of the Board. Also, there shall be a Compensation Committee and an Audit committee each comprised of three (3) members, none of the committee members shall be employees of the Company.

Purchase Agreement:

The sale of the Series A Preferred will be made pursuant to a stock purchase agreement reasonably acceptable to the Company and the Investors, which agreement will contain, among other things, appropriate representations and warranties of the Company and the Investors, covenants of the Company reflecting the provisions set forth in this term sheet and appropriate conditions to closing which will include, among other things, qualification of the shares to be sold under applicable federal and state securities laws, and the filing of Amended and Restated Certificate of Incorporation.

The Company may close on a minimum of \$750,000. The financing may remain open for up to an additional 30 days to accept additional subscriptions. The

Company will accept up to \$250,000 in excess of the maximum amount.

Other Documentation:

In addition to the Purchase Agreement, the following documents will be prepared in connection with the Financing:

- a) Board and shareholder resolutions approving transaction;
- b) Amended and Restated Certificate of Incorporation;
- c) Investor Rights Agreement;
- d) Registration Rights Agreement;
- e) Investor Questionnaires;
- f) Stock certificates; and
- g) Notice pursuant to Section 25102(f)

Preparation of Documentation:

Counsel to Investors shall prepare the required documentation in this Financing.

Expenses:

If the Financing is consummated, the Company will pay the hourly fees and expenses of counsel to the Investors, not to exceed \$30,000.

Counsel to the Investors:

Troop Steuber Pasich Reddick & Tobey, LLC