

MaRS Discovery District - Notice

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Sample Preferred Term Sheet

Corporation: [_____]

TERM SHEET¹

Date: [_____]

This Term Sheet represents the current understanding of the parties with respect to certain of the major issues relating to the proposed private offering and does not constitute a legally binding agreement. Except for the section entitled "Binding Terms" this summary does not constitute a legally binding obligation. Any other legally binding obligation will only be made pursuant to definitive agreements to be negotiated and executed by the parties. This Term Sheet does not constitute an offer to sell or a solicitation of an offer to buy securities in any jurisdiction where the offer or sale is not permitted.

THE OFFERING

Issuer: [_____], a corporation incorporated under the laws of [*insert Canada or Ontario*] (the "**Corporation**")

Securities: Class A Preferred Shares (the "**Preferred**")

Amount of the offering: \$[_____]

Price per share: \$[_____] per share (the "**Initial Price**"), based on a pre-money valuation of \$[_____] and the attached capitalization table (Appendix A).

Investor(s): [_____] and other accredited investors, acceptable to the Corporation.

Closing date: Initial closing on or before [_____]

¹ This sample Term Sheet was designed to be used in conjunction with standard MaRS articles of amendment documents, for a company's capitalization that initially includes one class of common shares ("Common Shares"). This sample Term Sheet will need to be appropriately customized for each end-user's application, including but not limited to replacing references to "Common Shares", if appropriate.

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TERMS OF THE PREFERRED

- Liquidation preference:** Preferred will have the right to receive one times the Initial Price from proceeds on a liquidation of the Corporation with balance of proceeds paid to holders of Common Shares. A sale of the Corporation's assets, merger, reorganization or similar transaction will be treated as a liquidation of the Corporation.
- Conversion:** The Preferred may be converted at any time, at the option of the holder, into Common Shares. The conversion rate will initially be 1:1, subject to customary adjustments for stock splits, stock dividends, etc.
- Automatic conversion:** Each share of Preferred will automatically convert into common shares, at the then applicable conversion rate, upon (i) the closing of a firmly underwritten initial public offering of common shares ("IPO"), or (ii) the consent the holders of at least a majority of the then outstanding shares of Preferred.
- General voting rights:** Each share of Preferred votes together with the Common Shares on all matters on an as converted basis, except as specifically noted herein or required by law.

SHAREHOLDERS AGREEMENT

- Information rights:** The Corporation will provide to each holder of at least [_____] %² of Preferred ("Major Investors"), (i) unaudited annual financial statements and (ii) unaudited quarterly financial statements and an annual business plan. This right will terminate immediately prior to the Corporation's IPO or completion of a Sale Transaction (as defined below).
- Protective provisions:** So long as any of the Preferred are outstanding, consent of majority of the then-outstanding Preferred will be required for any action that (i) amends the Articles of the Corporation if it would adversely alter the rights, preferences, privileges or powers of Preferred; (ii) changes the number of directors from current number; or (iii) approves any merger, asset sale, liquidation or other corporate reorganization or acquisition.
- Pre-emptive rights (to maintain proportionate ownership):** Each of the Major Investors will have a right to purchase its *pro rata* share of any offering of new securities by the Corporation, subject to customary exceptions. This right will terminate immediately prior to the Corporation's IPO, a Sale Transaction or [_____] ³ years after the date of Shareholders Agreement executed upon Closing.

² In Ontario, all shareholders will receive a copy of annual financial statements and additional information rights are provided to major shareholders, typically defined to be owners of 5% or more of the Corporation.

³ Management and investors may agree to have investors' rights to participate in additional financing rounds of the companies end after a certain term. The term is dependent on Corporation's financing needs and plans and typically ranges from two to four years, if a term is being set.

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Co-Sale Rights:

In the event that any shareholder (“Selling Party”) proposes to sell their shares to a third party (“Third Party”), the Selling Party agrees not to make the sale unless Third Party includes an offer to purchase the shares of the Investors on the same terms. If Third Party has specified a maximum number of shares that they are willing to buy, then the Selling Party and interested Investors may sell their pro-rata share of the amount to be purchased by Third Party.

Election of directors:

Provision agreeing to elect the following individuals to the board (i) one representative designated by the holders of Preferred [_____] ⁴ (the “Investor Nominee”); (ii) one representative designated by the Founders; and (iii) one representative designated by Common shareholders acceptable to the Investor Nominee and Founders.

Sale Transaction:

A “Sale Transaction” shall mean (i) any merger, amalgamation, reorganization, consolidation or other transaction involving the Corporation and any other corporation or other entity or person in which the persons who were the shareholders of the Corporation immediately prior to such merger, amalgamation, reorganization, consolidation or other transaction own less than fifty percent (50%) of the outstanding voting shares of the surviving or continuing entity after such merger, amalgamation, reorganization, consolidation or other transaction; (ii) the sale, exchange or transfer by the Corporation’s shareholders, in a single transaction or series of related transactions, of all of the voting shares of the Corporation; or (iii) the sale of all or substantially all of the assets of the Corporation.

OTHER MATTERS

Option pool:

The number of Common Shares reserved for issuance under the Corporation’s stock option plan will be increased to equal [_____%] ⁵ shares outstanding after issuance of the Preferred to Investors.

Share purchase agreement:

The Corporation and Investors will enter into a share purchase agreement containing standard representations and warranties, with survival period of _____ years. ⁶

Founder matters:

Each Founder shall have transferred all relevant intellectual property to the Corporation, entered into an employment agreement with the

⁴ This right may be assigned to a specific Preferred investor during term sheet phase, in which case blank will be filled in with name of that investor (fund or corporation name if they are not investing for individual account) or the blank can be removed, indicating that the majority of the Preferred will elect director to represent the Preferred.

⁵ Total number of shares reserved under the option pool is typically 10-20% of the fully-diluted capitalization of the Corporation post-money. For additional information on how to allocate stock options based on your hiring plan, you’ll find articles on www.marsdd.com website in the Entrepreneur’s Toolkit.

⁶ The typical range is from two to four years and may vary dependent on a specific representation or warranty. Investors and Founders may also want to consider indicating a minimum threshold for losses or claims associated with breach of representations and warranties as well as a maximum cap.

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Corporation and signed agreements with respect to voting and vesting their Founders shares over an agreed term of [_____] ⁷ years, the terms of such agreements satisfactory to Investors prior to Closing Date. The vesting agreement will provide for full acceleration of vesting for all shares held by the Founders on the completion of an IPO or Sale Transaction.

Expenses and fees:

The Corporation will reimburse counsel to Investors for legal fees and disbursements, up to a maximum cap of [_____] ⁸.

Expiration date:

These terms are valid until, and will expire on, [_____]. ⁹

Binding Terms:

For a period of thirty days, the Corporation agrees not to solicit offers from other parties for any financing. Without the consent of Investors, the Company will not disclose these terms to anyone other than officers, directors, key service providers, and other potential Investors in this financing.

This Term Sheet may be executed in counterparts, which together will constitute one document. Electronic signatures shall have the same legal effect as original signatures.

[Insert CORPORATION NAME]

[Insert NAME OF INVESTOR(s)]

Signature

Signature

Print name

Print name

Print title

Print title

Date

Date

⁷ The typical range is three to four years for new start-ups but may be less or not required for businesses that are more mature.

⁸ For a similar set of deal transaction documents, US law firms who have posted term sheets and related legal agreements have suggested a cap of \$10,000 may apply to completion of investment transactions; however, the cap should be negotiated in good faith between Founders and Investors with input from their respective counsel based on the complexity of the investment transaction.

⁹ Typically 30 days after the date first set forth above.

Sample Preferred Term Sheet

Appendix A – Capitalization Table

Shareholder Name	Common Shares ¹⁰	Options	Preferred Shares	Fully Diluted Shares	Pro-forma Fully Diluted Ownership %
Name Founder1	5,000,000	-	-	5,000,000	34.6%
Name Founder2	5,000,000	-	-	5,000,000	34.6%
Subtotal – Current Holdings	10,000,000	-	-	10,000,000	n/a
Investors ¹¹	-	-	3,000,000	3,000,000	20.8%
Option pool ¹²	-	1,444,444	-	1,444,444	10.0%
Total – Proforma Holdings	10,000,000	1,444,444	3,000,000	14,444,444	100%

¹⁰ Enter names and number of common shares already issued to founders and any other shareholders

¹¹ Equal to the estimated amount of investment for all Preferred Investors divided by the agreed price per share.

¹² See footnote 5 above