**CONVERTIBLE NOTE TERM SHEET**

**Issuer**: \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_, a \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ (the “Issuer”)

**Purchaser**:\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_, a \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ (the “Purchaser”)

**Issuance**: Convertible promissory note due \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ (the “Note”)

**Principal**: [Up to] $\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_; the Purchaser will pay face value for the Note.

**Target Closing Date**: On or before \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_, [or as soon as practicable after

satisfaction or waiver of all closing conditions] [to occur simultaneously with signing the definitive documentation]

**Interest**:

\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_% per year, capitalized into the Note’s principal.

\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_% per year default penalty.

**Payment Dates**:

Quarterly, in arrears [beginning on \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_] [Upon maturity]

**Maturity**:

Unless converted, the Note matures on the \_\_\_\_\_\_\_\_ anniversary of the closing date

**Use of Proceeds**:

Proceeds from the Note issuance must be used [for general corporatepurposes].

**Ranking**:

\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ ranking.

**Permitted Indebtedness:**

(i) Mechanics’ liens and obligations to trade creditors, (ii) existing

indebtedness \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_, and (iii) [Unsecured] indebtedness from a commercial bank or comparable lender [for (describe purpose)] in an amount not to exceed $\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_.]

**Security**:

The Note will be secured by a [first priority] [subordinated] lien on [all the Issuer’s assets and business] [real property] [assets] [accounts receivable] [intellectual property] [securities] [commercial tort claims] [contract rights] [insurance claims].]

**Guaranty**:

The Issuer’s obligations will be fully and unconditionally guaranteed [on a joint and several basis] by [the founders / subsidiaries / parent corp / other guarantor].

**Mandatory Conversion**:

The outstanding principal and interest on the Note will convertautomatically into shares of the Issuer’s \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ upon any of the following events:

The Issuer accepts a third-party cash investment [in an aggregate amount of at least$\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_in the Issuer in exchange for shares of its stock, in which case thePurchaser will receive equity of the same type and on substantially the same terms and conditions as the third-party investor or syndicate; or The issuer achieves annual [revenue, earnings, or other defined milestone] [calculated in accordance with \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_] of at least $\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_, in which case the Purchaser will receive shares of the Issuer’s common stock; or [The Issuer agrees to a change-of-control or sale of substantially all the Issuer’s business and assets to a third party.]

**Redemption:**

If the Issuer agrees to a change-of-control or sale of substantially all the Issuer’s business and assets to a third party, the Issuer must redeem the Note in cash [or liquid securities] at \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_% of the outstanding principal and interest on the Note.]

**Conversion Price**:

Upon conversion due to a third-party investment [or change-of-control], thePurchaser will receive new equity in an amount that values the Issuer’s total outstanding equity pre-money at the [minimum] [weighted average] valuation offered in that round, minus

(i)\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_% [if the conversion occurs on or before \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_,

(ii)\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_% if the conversion occurs on or before \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_, or

(iii)\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_% if the conversion occurs on or before \_\_\_\_\_\_\_\_\_\_\_\_\_] (the Discount), and in any case not to exceed an implied pre-money valuation of $\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ (the “Cap”).

Upon conversion due to the Issuer’s achieving a performance milestone, the Purchaser will receive new equity [in an amount that values the Issuer’s total outstanding equity pre-money at $\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ [at fair market value based on [a defined formula]] as determined by a mutually acceptable valuation agent, subject to the Discount and Cap].

**Board Seat / Info Rights**:

The Issuer’s Board of Directors will consist of\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ members. The Purchaser may appoint \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ member[s] to the Issuer’s Board of Directors to represent the Purchaser’s interests while the Note remains outstanding. [The Issuer will appoint [an] independent member[s] to [one] of the remaining directorships.] [Upon closing, the initial members will be [the CEO, the Purchaser representative, etc.]] The Purchaser will have customary information and inspection rights, including to receive all periodic financial and investor information reports that the Issuer prepares for its stockholders. [While the Note remains outstanding the Issuer will prepare and deliver to the Purchaser: an annual budget, annual \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ financial statements [within \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ days of each fiscal year end], quarterly unaudited financial statements [within\_\_\_\_\_\_\_\_\_\_\_ days of each fiscal quarter end].]

**Reps and Warranties**:

The Issuer will make standard representations and warranties for afinancing of this type.

**Covenants**:

The Note will contain standard affirmative and negative covenants for a financing ofthis type, including but not limited to the following covenants. [Covenant waivers require the consent of Note holders representing [a majority] \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_% of the outstanding principal and interest on the Notes.]

Affirmative covenants will require the Issuer to: continue its corporate existence maintain insurance policies on [real property] [inventory] [vehicles] [key man life] comply with applicable law pay taxes

protect its intellectual property

prepare financial reports [in accordance with \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_] on a

\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ basis and annual reports [\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ by an outside

accountant]]

Negative covenants will forbid the Issuer to: change its business or enter a new line of business dispose of its assets other than in the ordinary course of business [and not to exceed $\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ in the aggregate] enter into any agreement to merge or combine with another company

make any acquisition of another company, its business or assets [, except for certain purchases of inventory in the ordinary course of business] issue dividends, stock repurchases or redemptions, make payments with respect to subordinated debt, or make other restricted payments [in an aggregate amount exceeding $\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_] Make any loans or investments [in an aggregate amount exceeding $\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_] [other than in the ordinary course of business] incur any lien or make any negative pledge, other than mechanics’ liens in favor of suppliers incurred in the ordinary course of business incur any additional indebtedness, including guaranties, sale-leasebacks, and other contingent obligations [in an aggregate amount exceeding $\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_] [other than in the ordinary course of business] engage in any transactions with insiders or their affiliates [, except for \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_] increase the size of its Board of Directors beyond \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ members increase the annual cash compensation for any employee beyond $\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ or by more than \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_% over the previous year

**Events of Default**:

The Note will include events of default customary for financings of this type,including but not limited to the following.

Automatic events of default will give rise to a default upon their occurrence:

failure to pay interest or principal when due the Issuer’s voluntary or involuntary bankruptcy or insolvency any default by the Issuer under other material indebtedness The following events of default trigger the [Purchaser’s] right [of Note holders representing [a majority] [\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_%] of the outstanding principal and interest on the Notes] to declare a default: covenant violation inaccurate reps and warranties material legal judgment against the Issuer[including [final and unappealable] invalidation of key patent claims by a court of law] default under a material contract

**Closing Conditions:**

The parties’ obligation to close will be contingent on customary conditions for a financing of this type, including [satisfactory completion of the Purchaser’s due diligence] [regulatory approvals] [third party consents] [the Purchaser’s obtaining third-party financing in an amount sufficient to fund the purchase price and on terms satisfactory to it].

**Registration Rights**:

The holders of shares of stock issued upon the Note’s conversion will havecustomary registration rights, including the right to piggyback on any registration of shares from the same class of equity by the Issuer

**Transferability**:

The Purchaser may not transfer the Note [, except [to its affiliates and] incompliance with applicable state and federal securities laws.]

**Documentation**:

The [Issuer’s counsel] will prepare initial drafts of definitive legal documentation for review and comment by the [Purchaser’s counsel]. The definitive documentation [will combine the loan agreement terms, the convertible note [, and the security agreement] in a single document] [will consist of a note purchase agreement with attached forms of the note[s] and security agreement to be executed on closing].

**Governing Law and Jurisdiction**:

[This term sheet and the definitive documentation shall begoverned by and construed in accordance with the laws of \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ State applicable to transactions signed and to be performed solely within such state.

**Confidentiality:**

[This term sheet is Confidential Information within the meaning used in theconfidentiality agreement, dated \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_, between the parties hereto.]

[Except as otherwise required by law, the Issuer will not disclose the existence or terms of this term sheet or any of the matters referred to herein (“Confidential Information”) to any persons other than its executive officers, directors, accountants and attorneys, and shall inform all recipients of Confidential Information that they may not disclose it to third parties. The Purchaser is responsible for all such recipients’ conduct with respect to the Confidential Information. The Issuer may seek injunctive relief, in addition to other remedies, to enforce this provision.]

**Exclusivity:**

During the period commencing on the date hereof and continuing for 90 days,neither the Issuer, nor any of its respective affiliates, agents, principals, attorneys, or other representatives shall directly or indirectly contact, solicit, encourage or negotiate with any person or entity other than Purchaser with respect to any transaction involving the purchase of equity

interests of the Company, or substantially all of its business and assets (a “Competing Transaction”). If Seller receives or becomes aware of any offer to engage in a Competing Transaction, he will promptly notify Purchaser of such offer, its terms, and the offeror’s identity.

**Expenses**:

[The parties will pay their own expenses in connection with this transaction.][Contingent upon closing, the Issuer will pay all of the Purchaser’s third-party expenses from the date hereof in connection with this transaction, including legal and financial advisory fees, up to a maximum amount of $\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_, from the proceeds of the Issuance.]

**Amendment:**

The Notes may only be amended by a written instrument signed by Note holders representing a majority of the outstanding principal and interest on the Notes. Any such amendment will be binding on all Note holders.]