

XYZ CORPORATION

SUMMARY OF PRINCIPAL TERMS

This Term Sheet is intended for discussion purposes only. Neither party will be obligated to the other until the definitive agreements are negotiated and signed.

Issuer:

XYZ Corporation (the "Company"), an Oregon Corporation

Amount:

A minimum of \$2 million. A maximum of \$3,000,000

Security:

Up to 1,333,333 shares of Series A Convertible Preferred Stock ("Series A Preferred"). The exact amount and price will be based on a pre-money valuation of the Company of \$4,000,000.

Investors:

Venture Firm 1, LLP ("VC1") in the amount of not less than \$1 .5 million; other investor(s) acceptable to VC1 for up to \$1.5 million.

Investor	Shares	Dollars
VC1	666,667	\$1.5 million
Others	666,666	\$1.5 million
Total	1,333,333	\$3.0 million

Conversion of Bridge Loan:

The \$100,000 bridge loan will be converted into an 44,444 shares of Series A Preferred using a conversion price equal to the Original Purchase Price (as defined below).

Bridge Loan Warrants:

The holders of the \$100,000 bridge loan will receive warrants to purchase 31,874 shares of the Company's Series A Preferred Stock for \$2.25 per share, exercisable at any time within seven years of the closing.

Valuation:

Pre-financing valuation of \$4 million and a purchase price of \$2.25 a share for the Series A Preferred ("Original Purchase Price"). The post-financing capitalization of the Company as understood by the investors at the date hereof is attached.

Rights, Preferences, Privileges

1. Dividend Provisions: Annual per share dividend and Restrictions of Preferred on the Series A Preferred equal to 8% of the Original Stock: Purchase Price, payable when and if declared by the Board of Directors; non-cumulative. No dividends may be paid on the Common Stock unless approved by a majority of the board members appointed by the holders of Series A.
2. Liquidation Preference: In the event of any liquidation of the Company, the Series A Preferred will be entitled to receive in preference to the Common Stock an amount equal to the Original Purchase Price (adjusted for stock splits, dividends and similar events), plus any declared and unpaid dividends.

After payment to the Series A Preferred of their liquidation preference, the remaining assets distributable upon such liquidation, if any, will be paid pro rata to the holders of the Common Stock and the holders of the Series A Preferred on an as-converted basis; provided that no Series A Preferred holder shall receive an amount with respect to any share of Series A Preferred in excess of two times the Original Purchase Price (adjusted for stock splits, dividends and similar events) for such share. Any remaining assets will be distributed to the Common Stock. A merger, consolidation, reorganization or sale of all or substantially all of the Company's assets (including the exclusive licensing of the Company's intellectual property) shall be deemed a liquidation unless otherwise agreed by the holders of more than 50% of the Series A Preferred.

3. Redemption & Conversion: The Series A Preferred will not be redeemable. The Series A Preferred will be convertible at any time, at the option of the holder, into shares of Common Stock at an initial conversion price equal to the Original Purchase Price (adjusted for stock splits, dividends and similar events). Initially each share of Series A Preferred is convertible into one share of Common Stock. The conversion price will be subject to adjustment as provided in paragraph 6 below.

5. Automatic Conversion: The Series A Preferred will be automatically converted into Common Stock, at the then-applicable conversion price, (a) in the event of an underwritten public offering of shares of Common Stock at a price per share that is not less than three times the Original Purchase Price in an offering resulting in gross proceeds to the Company of not less than \$15,000,000 or (b) at any time after at least 51 percent of the Series A Preferred has agreed in writing to convert.

6. Antidilution Provisions: The conversion price of the Series A Preferred will be subject to adjustment to prevent dilution in the event that the Company issues additional shares (other than the Reserved Employee Shares described under "Reserved Employee Shares" below) at a purchase price less than the applicable conversion price. The conversion price will be subject to adjustment on a broad-based, weighted average basis which takes into account issuances of additional shares at prices below the applicable conversion price.

7. Voting Rights: Except with respect to election of directors, the holder of a share of Series A Preferred will have the right to that number of votes equal to the number of shares of Common Stock issuable upon conversion of the Series A Preferred at the time the record for the vote is taken. Election of Directors will be as described under "Board Representation" below.

8. Protective Provisions: Provided at least 25% of the shares of Series A Preferred are outstanding, consent of the holders of at least 66% of the Series A Preferred will be required for (i) any sale by the Company of all or substantially all of its assets, (ii) any merger of the Company with another entity, (iii) amendment of the Company's articles of incorporation, (iv) any recapitalization or reclassification of the outstanding capital stock of the Company, (v) any repurchase of any securities of the Company (except pursuant to agreements with employees approved by the Board of Directors providing for a right of repurchase by the Company upon certain events), (vi) any dissolution, liquidation or winding up of the business of the Company, (vii) the creation of any new class of shares having preference over or being on a parity with the Series A Preferred, (viii) the Company to engage in any business that is substantially different than that engaged in on the Closing date, (ix) the Company to become obligated under any loan or guaranty of indebtedness in excess, in the aggregate, of \$1 million, (x) the sale of any subsidiary or shares held in any subsidiary, (xi) an increase or decrease in the authorized number of members constituting the Board, (xii) for the Company to declare or pay any dividend on the Common Stock or (xiii) for the Company to grant an exclusive license for all or substantially all of the intellectual property of the Company. All board representatives of the Series A Preferred must approve the adoption or amendment of any stock option or stock incentive plan providing for the issuance of the shares of the Company to employees, directors or consultants.

Information Rights:

The Company will timely furnish the holder of the outstanding Series A Preferred Stock with annual, quarterly and monthly financial statements including Balance Sheet, Income Statement and Cash Flow Statement. Representatives of the Investors will have the right to inspect the books and records of the Company.

Registration Rights:

1. Demand Rights: Beginning the earlier of three years after the Closing Date and 12 months after the Company's initial public offering, if investors holding at least 20 percent of the Preferred (or Common Stock issued upon conversion of the Preferred) request that the Company file a Registration Statement covering at least 20 percent of the Common Stock issuable upon conversion of the Preferred with an anticipated aggregate offering price of at least \$10,000,000, 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 registrations under these demand right provisions nor more than one registration in any twelve month period.

2. Registrations on Form S-3: Holders of Preferred (or Common Stock issued upon conversion of the Preferred) will have the right to require the Company to file an unlimited number of Registration Statements on Form 5-3 (but no more than two per year), provided that the reasonably anticipated price to the public of all shares proposed to be registered is at least \$500,000.
3. Piggy-Back Registration: The Investors will be entitled to unlimited “piggy-back” registration rights on all registrations of the Company.
4. Registration Expenses: All registration expenses (exclusive of underwriting discounts and commissions or special counsel fees of a selling shareholder) shall be borne by the Company.
5. Lock-Up Provision: Upon request by the underwriter, the holders of all registerable securities shall enter into agreements not to transfer any shares beginning upon the date of the Company’s initial public offering and continuing for such period thereafter up to 180 days, provided each officer and director of the Company and all other holders of at least 1 percent of the Company’s Common Stock shall agree to execute a similar agreement.
6. Termination: All registration rights terminate five years after the Company’s initial public offering.
7. Transfer: Registration rights are transferable only with the transfer of at least 51% of the holder’s registrable securities or to a majority-owned subsidiary of a holder or a constituent partner of a holder.
8. Certain Employee Rights: Certain key employees to be named by the Board of Directors shall have piggy-back registration rights on any investor demand registrations, subject to underwriter’s cutback and subordinate to the Investors, and on Company initiated registrations, subject to underwriter’s cutback and pro rata with investors.

Board Representation:

The Board will consist of five members. So long as the Series A holds 5% or more of the fully diluted shares of the Company one member of the Board of Directors will be selected by VC1 (initially <person 1>) and one member of the Board will be selected by VC2 (initially <person 2>). One member of the Board of Directors will be selected by the holders of the Company’s Common Stock; one member will be proposed by the holders of Series A and be subject to approval by the holders of Common and one member will be proposed by the holders of Common and be subject to approval by the holders of Series A.

For the Board members that are outside directors, such directors will be compensated on terms typical of such arrangements. It is contemplated that such outside directors will not receive salaries, but will receive reimbursement of expenses.

A Board member appointed by the holders of Series A shall serve on each of the audit committee and the compensation committee of the Company. If no such committees currently exist, this provision will apply to such committees when, and if they are formed or established.

Key Man Insurance:

As determined by the Board of Directors.

Preemptive Right to Purchase

If the Company proposes to offer additional shares (other New Securities: than Reserved Employee Shares or shares issued in the initial public offering or the acquisition of another company or shares issued upon conversion or exercise of outstanding securities), the Company will first offer all such shares to the Investors on a pro rata basis. This preemptive right will terminate upon an underwritten public offering of shares of the Company.

Stock Restriction and Rights of First Refusal and Co-Sale:

All present holders of the Common Stock of the Company who are employees of the Company will execute a Stock Restriction Agreement with the Company pursuant to which the Company will have an option to buy back at a cost of \$0.001/share a portion of the shares of Common Stock held by such person (excluding Other Originally Vested Shares as defined below) in the event that such shareholder’s employment with the Company is terminated prior to the expiration of 36 months from April 30, 2001. One thirty sixth percent (1/36%) of the shares will be released each month from

the repurchase option based upon continued employment by the Company. In addition, the Company and the holders of the Series A Preferred will have a right of first refusal with respect to any employee's shares proposed to be resold, or alternatively (in the case of the Series A Preferred holders), the right to participate in the sale of any such shares to a third party, which rights will terminate upon a public offering. "Other Originally Vested Shares" means 15% of the total shares of Common Stock held by each of the founders of the Company as of the Closing.

Reserved Employee Shares:

The Company will reserve 777,778 shares of Common Stock for options granted or stock issued to employees, directors and consultants of the Company (the "Reserved Employee Shares") after the Closing Date. The Reserved Employee Shares will be issued from time to time under such arrangements, contracts or plans as recommended by management and approved by the Board. Employees, directors, and consultants, other than the founders of the Company, who hold Common Stock or options granted for Common Stock will be subject to vesting as follows: Twenty-five percent of the shares will be released in a single cliff after one year and the remaining shares will be released in equal quarterly increments during the three years thereafter. In addition, the Company and the holders of the Series A Preferred will have a right of first refusal with respect to any employee's shares proposed to be resold, or alternatively (in the case of the Series A Preferred holders), the right to participate in the sale of any such shares to a third party.

Proprietary Information and Invention Agreement

Each employee of the Company will enter into a proprietary information and inventions agreement in a form reasonably acceptable to the Investors.

The Purchase Agreement:

The purchase of the Series A Preferred will be made pursuant to a Stock Purchase Agreement and other documents drafted by counsel to VC1 and reasonably acceptable to the Company and the Investors, which agreements shall contain, among other things, appropriate representations and warranties of the Company, covenants of the Company reflecting the provisions set forth herein, and appropriate conditions of closing.

Expenses:

The Company will bear the legal fees and other out-of-pocket expenses of the Investors with respect to the transaction, not to exceed \$15,000.

Indemnification:

The Company will agree to indemnify directors to the maximum extent permitted by law.

Board Meetings:

The Company's Board of Directors will hold monthly meetings.

Conditions to Closing:

- (i) Completion of financial, accounting, and legal due diligence
- (ii) The Company shall have delivered to the Investors an SBA confirmation letter in the form hereto
- (iii) Resolution of any legal issues

Expiration Date:

This term sheet expires at 5:00 PM on May 31, 2001 unless accepted in writing by an authorized representative of the Company.

Expected Close Date:

<month>, <day>, <year> unless mutually agreed upon by all parties.

Confidentiality:

This term sheet and any related correspondence is to be held in strict confidence and is not to be disclosed to any other party without the prior written approval of VC1.

OTHER THAN THE "CONFIDENTIALITY" PROVISIONS, THIS SUMMARY OF TERMS DOES NOT CONSTITUTE ANY FORM OF BINDING CONTRACT BUT RATHER IS SOLELY FOR THE PURPOSE OF OUTLINING THOSE TERMS

PURSUANT TO WHICH DEFINITIVE AGREEMENTS MAY ULTIMATELY BE ENTERED INTO. THE INVESTMENT DESCRIBED IN THIS SUMMARY OF TERMS IS CONTINGENT UPON, AMONG OTHER THINGS, APPROVAL BY THE COMPANY'S BOARD OF DIRECTORS AND THE NEGOTIATION AND EXECUTION OF A SATISFACTORY PURCHASE AGREEMENT AND RELATED DOCUMENTS.

VC1 LLP. _____

Agreed and accepted to on this day of <date>

<Company Name>

By:

Title

Post-financing capitalization (at maximum offering)

Class	Number	Percentage
Common Stock	1,000,000	32.14286%
Option pool	777,778	25%
Series A Preferred*	1,333,333	42.85714%
Total common share equivalents	3,111,111	100.00%

* Including conversion of bridge loan and warrants