

Prof. Dr. Joseph A. McCahery and Prof. Dr. Erik P.M. Vermeulen

Corporate Governance and Innovation

Venture Capital, Joint Ventures, and Family Businesses (PART I)



Setting the Theme

Part I:

Forms of Finance – Contractual Arrangements

Prof. Dr. J.A. McCahery

Part II:

Legal Infrastructure to Innovation

Prof. Dr. E.P.M. Vermeulen



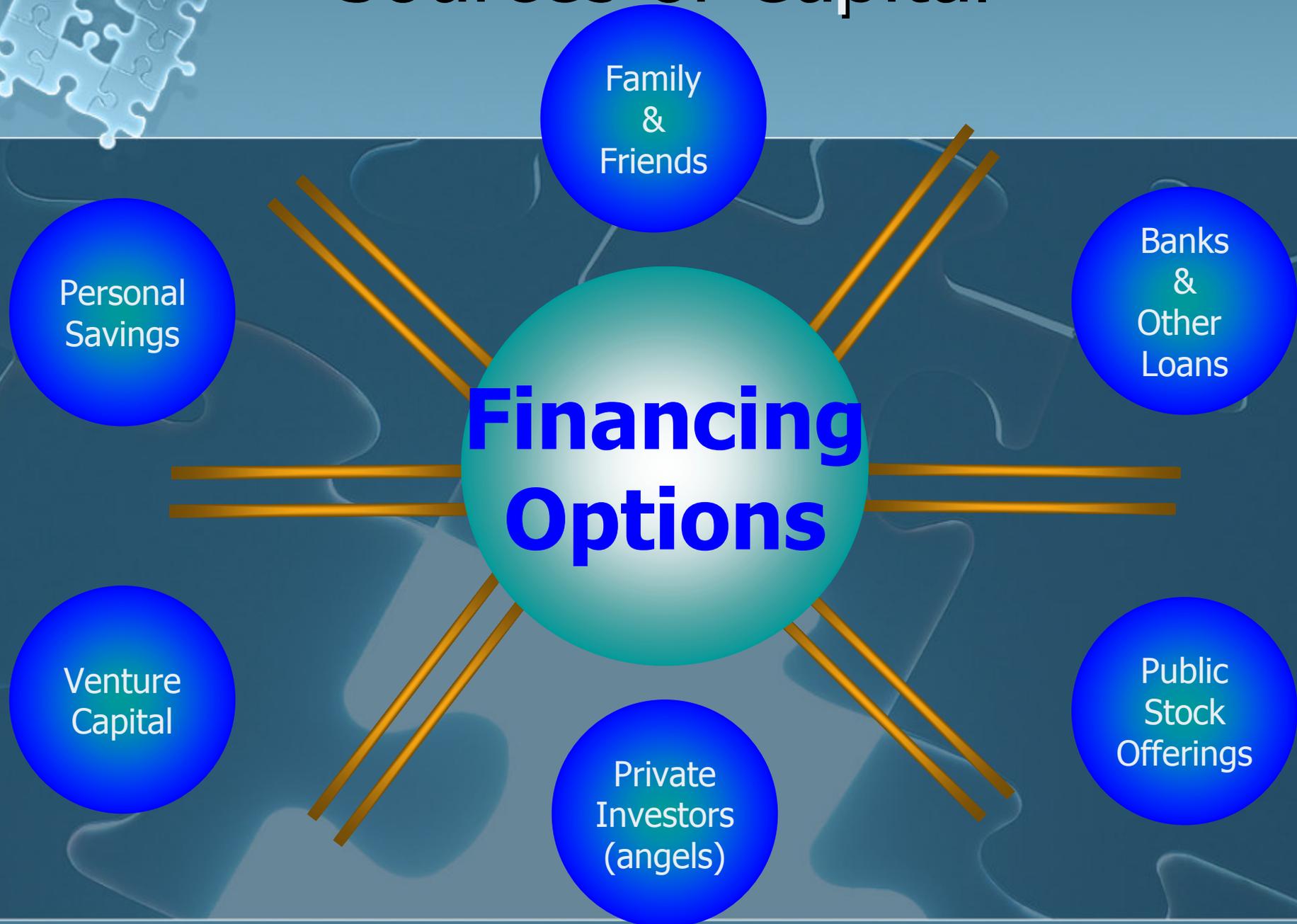
Part I: Financing Non-Listed Companies

***Creditor
Protection***

**Financing
Options**

***Investor
Protection***

Sources of Capital



Debt v. Equity

Innovative Start-ups?

Venture
Capital
=
EQUITY

Loans
=
DEBT

Investor

Ownership

Entrepreneur

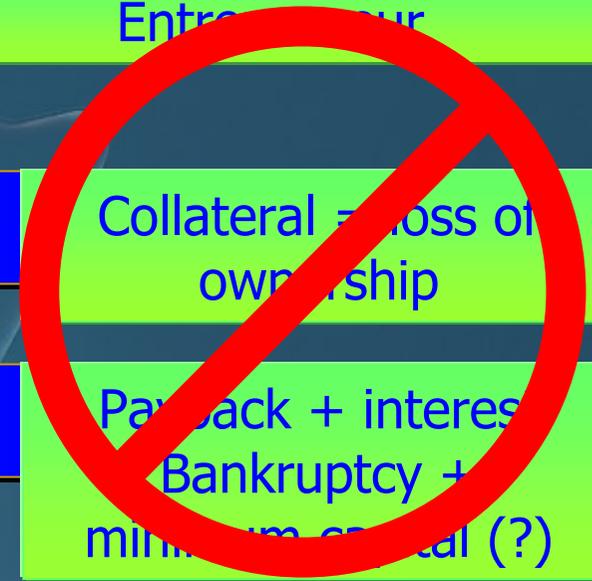
Investor needs legal (contractual) and non-legal (reputation) mechanisms in order to align investors and founders interest

Adverse Selection

Collateral = loss of ownership

Moral Hazard

Payback + interest
Bankruptcy + minimum capital (?)

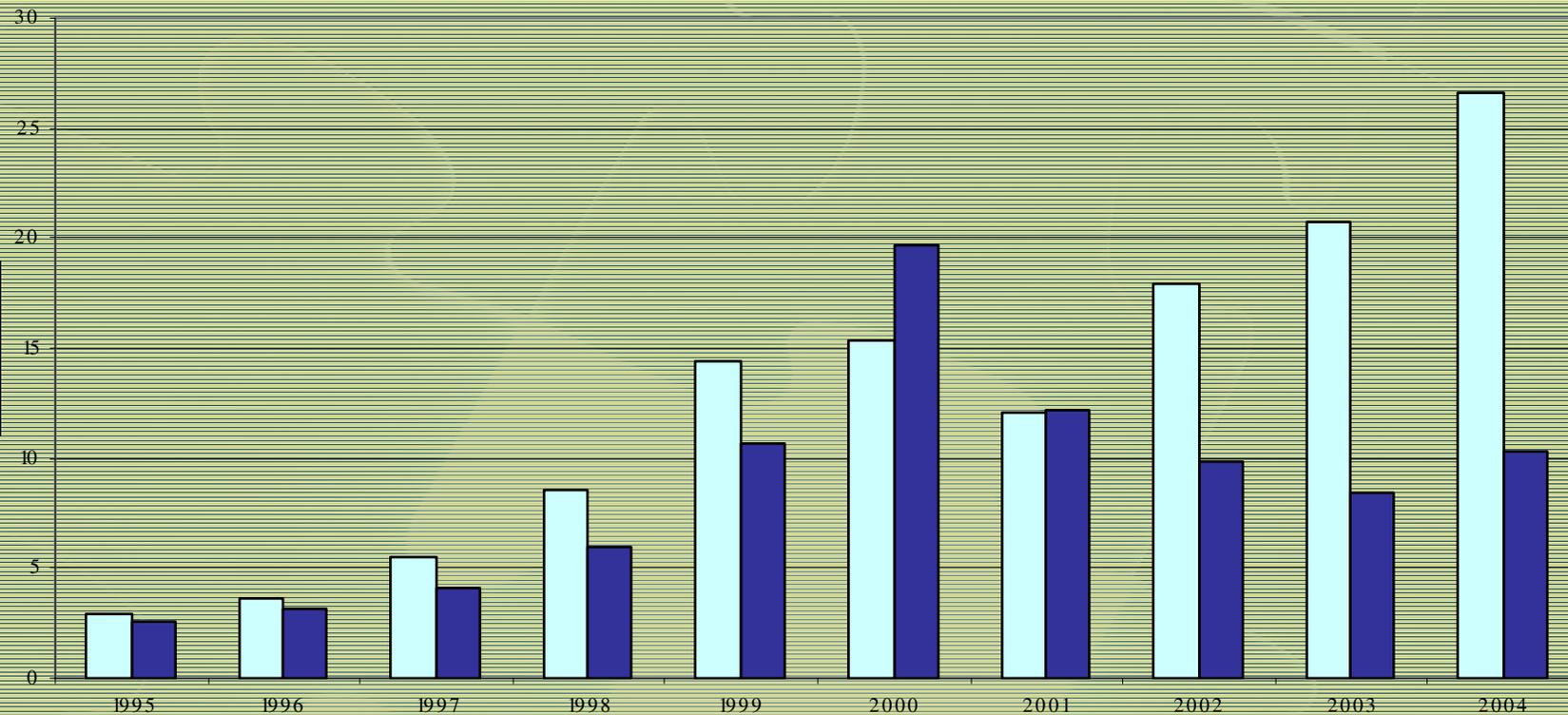




Risk Capital Invested

In Europe by stage 1995-2004

□ Buyout ■ Venture Capital

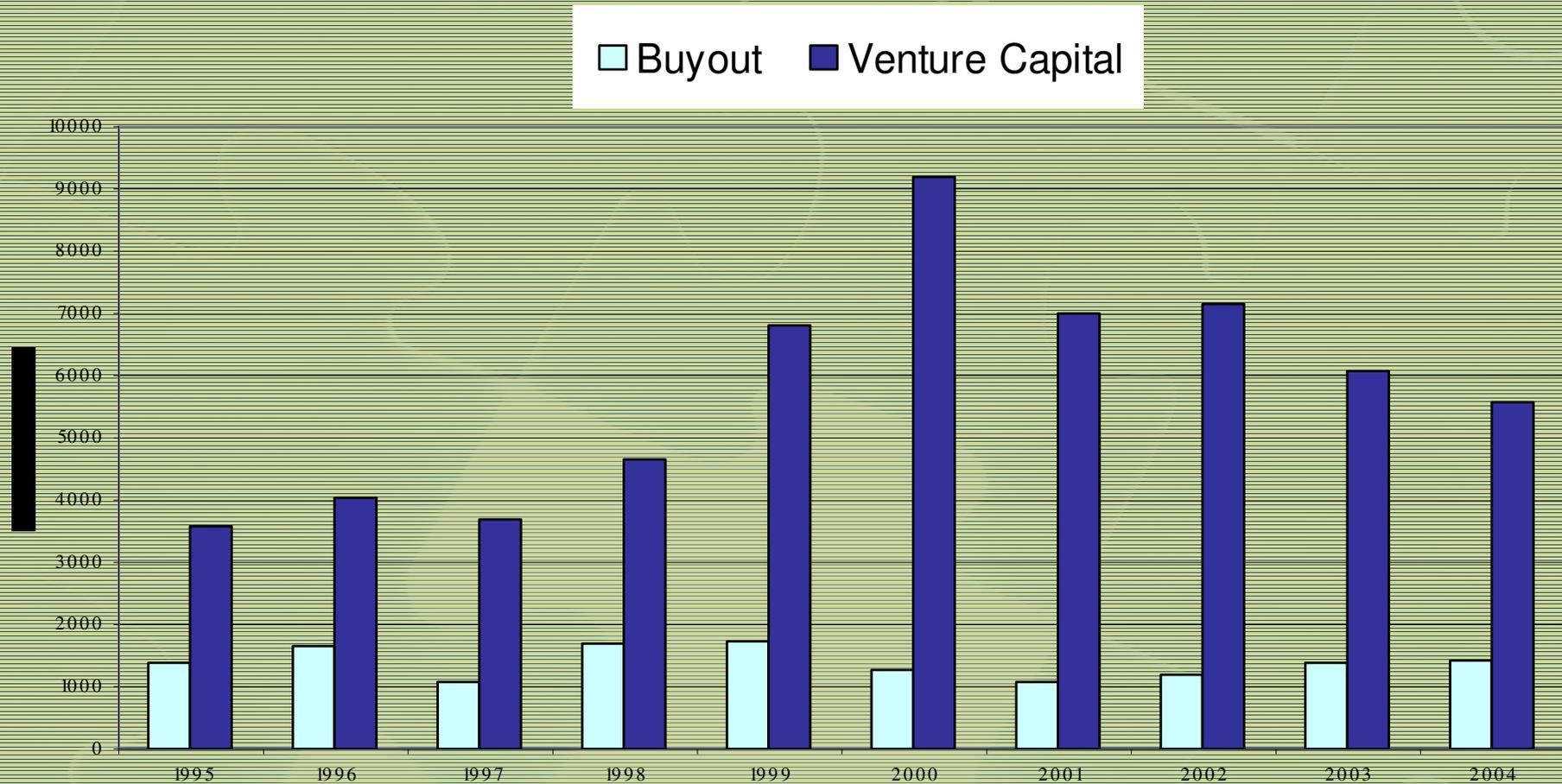


Source: CEFS/EVCA – Employment Contribution of Private Equity and Venture Capital in Europe – November 2005.



Number of Companies Invested In

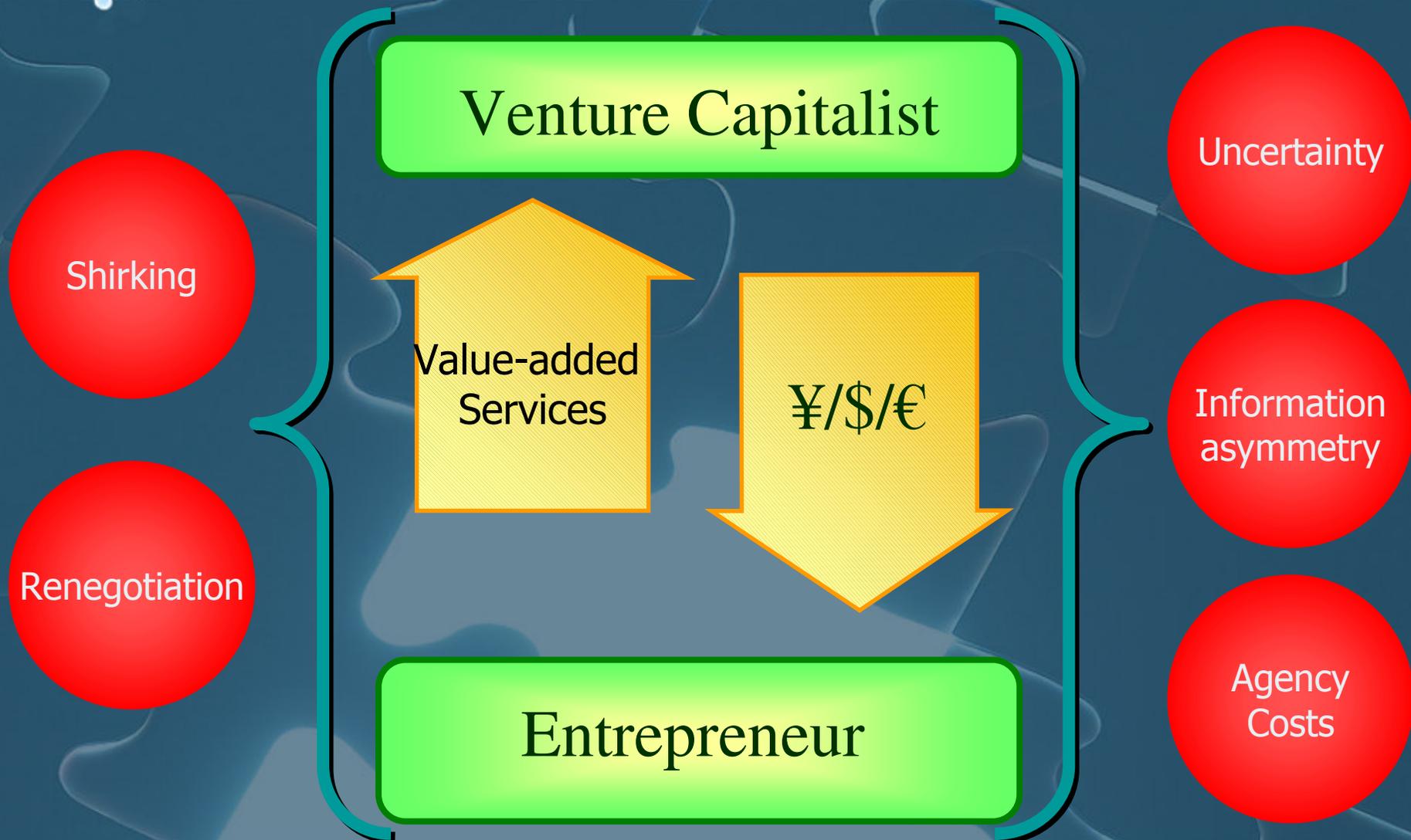
In Europe by stage 1995-2004



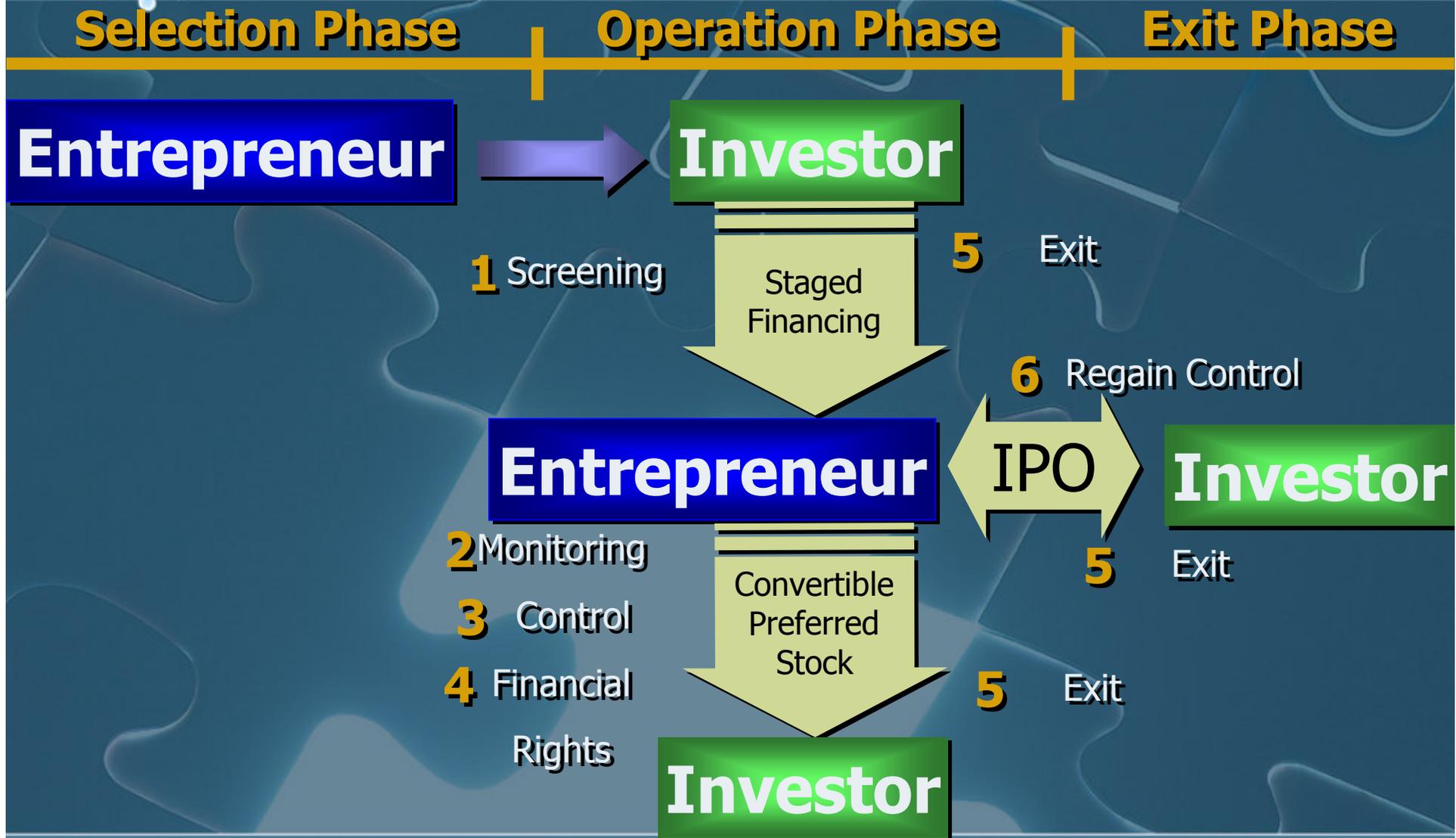
Source: CEFS/EVCA – Employment Contribution of Private Equity and Venture Capital in Europe – November 2005.



Double-sided Moral Hazard Problem

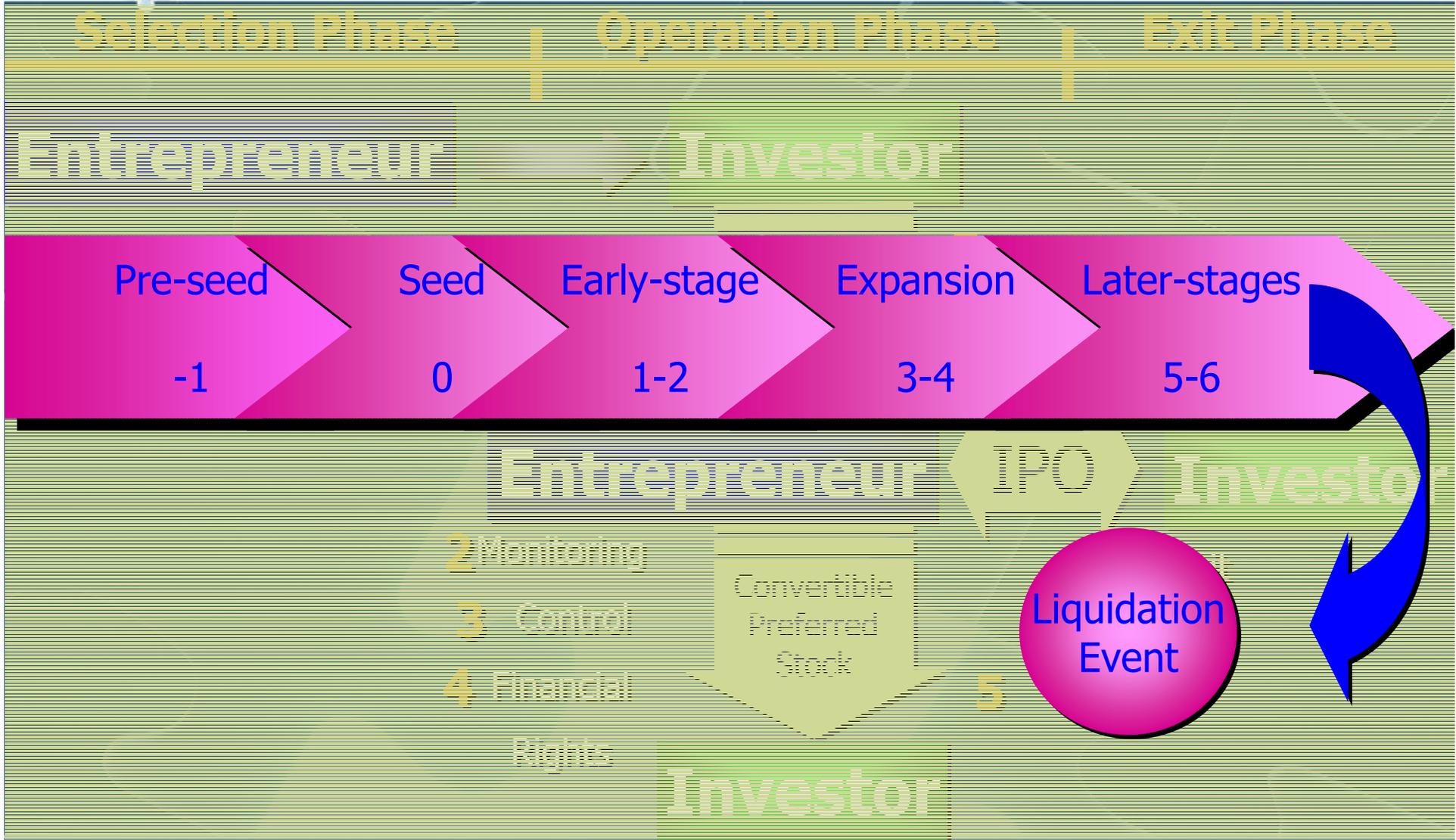


Venture Capital Architecture





Staged Capital



Term Sheet: Convertible Preferreds

Dividend Rights
Liquidation Pref.
Redemption
Conversion Rights
Antidilution
Voting Rights
Board Rep.
Protective Prov.
Info Rights
Rights of 1st Offer

MEMORANDUM OF TERMS FOR PRIVATE PLACEMENT OF
SERIES B PREFERRED STOCK OF
BIOTECH INCORPORATED



Exit Strategies

IPO

Trade Sale

Re-purchase

Reorganization

Liquidation

EXIT

Selection Phase

Creation Phase

Exit Phase

Entrepreneur

Investor

Staged Financing

Entrepreneur

Monitoring

Convertible Preferred Stock

Investor





Asset Securitization

OPTIMIZED

New Method of Financing
Strengthens the financial
infrastructure to enhance
the economy

SPV



Asset Securitization

ORIGINATOR

**Sale of
Assets**

SPV

**Sales of bonds or
commercial papers
with shares in return**

INVESTORS



Asset Securitization

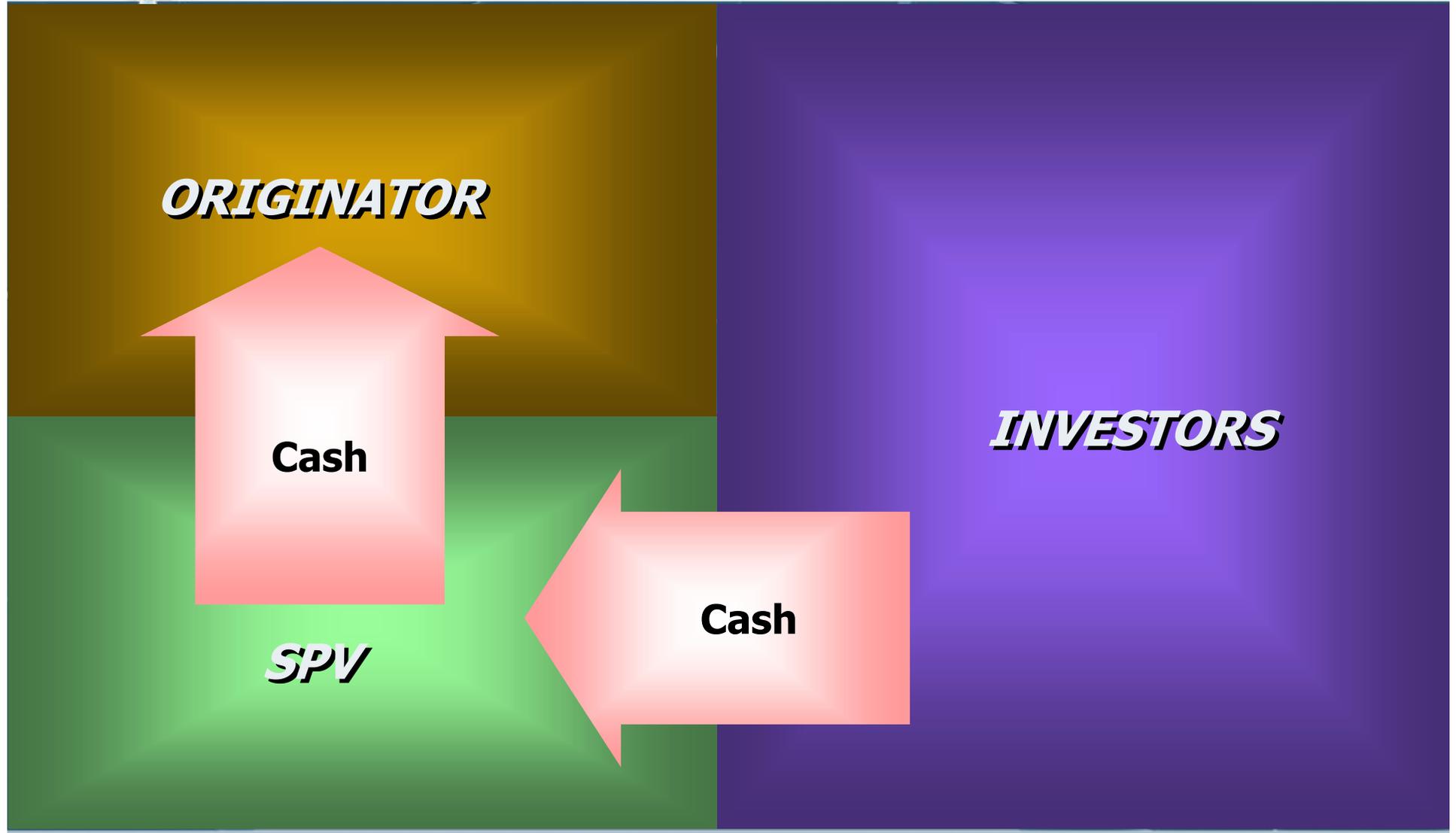
ORIGINATOR

Cash

SPV

Cash

INVESTORS





Advantages of Securitization

ORIGINATOR

On-going sale of
assets possible

No impact on
client relationship

Diversification of
funding sources

Off-balance sheet treatment

Cost efficient

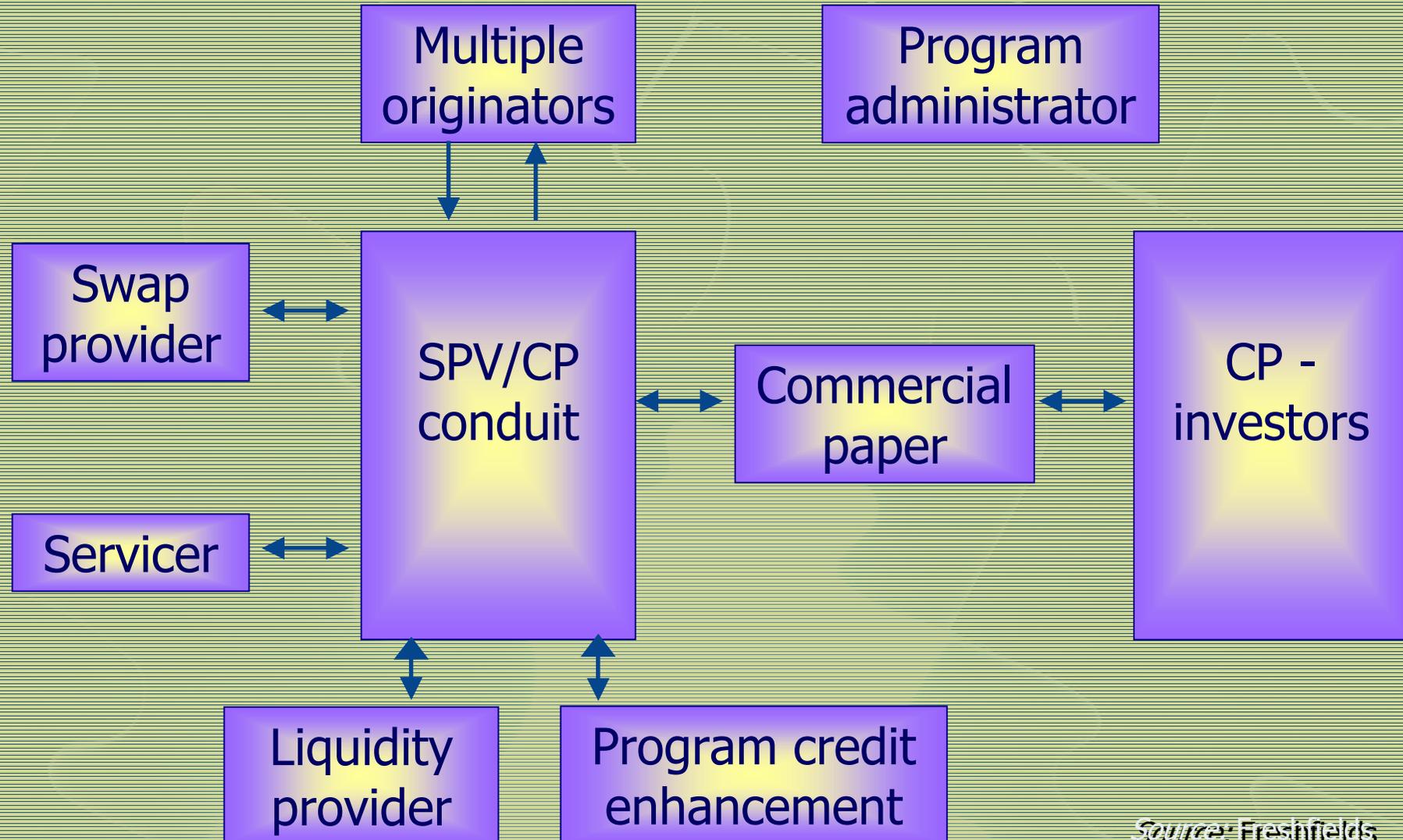
SPV

Asset/Liability Management

Increase of liquidity



Example





Conclusion

Debt

Asset-Backed
Securitization

Equity



Thank you!

j.a.mccahery@uva.nl

e.p.m.vermeulen@uvt.nl