The Players

CAMERON (L) & TYLER (R) WINKLEVOSS
DIYA NARENDRA, CONNECTU FOUNDERS
MARK ZUCKERBERG, FACEBOOK CEO

November 2003

- The Winklevoss twins and Narendra were seniors at Harvard University
- Building a social networking website called HarvardConnections.com
- Had paid programmer Victor Gao a total of $400 to implement the site
- Gao quit
- They asked him to brief a replacement, Harvard sophomore Mark Zuckerberg

Mark Zuckerberg

- In November 2003, Zuckerberg was already infamous
- He had created a site at Harvard called Facemash.com
- It displayed pictures of pairs of Harvard students and asked users to pick the more attractive one
- Zuckerberg hacked into dormitory servers to obtain pictures of students
- The site was WILDLY popular
- In four hours, over 22,000 votes were recorded.
- The average voter evaluated 48 pairs of faces
- Facemash also maintained a ranked list of the prettiest people at Harvard
Mark Zuckerberg

- Harvard was not happy about Facemash.com
- Zuckerberg was disciplined internally for
  - breaching security
  - violating copyrights, and
  - violating individual privacy
- But he knew how to build a popular website
- On Nov. 30, Winklevoss asked him to be an equity partner in HarvardConnections.com, to be called ConnectU
- He agreed to finish the site in return for a piece of the company

Zuckerberg’s Facemash (re-creation)

Harvard students often compete in the classroom, but for at least a few hours this weekend, only one thing helped them make the grade—their looks.

Just over a month after two Harvard alumni competed in the Miss America Pageant, a website created by Mark Zuckerberg, ‘06 gave students a chance to rate their peers using ID photos taken from online House Facebooks.

“We’re we let in for our looks? No. Will we be judged on them? Yes,” proclaimed the site, which Zuckerberg has now taken offline.

Zuckerberg, a computer science concentrator, said he created the site—www.facemash.com—by hacking into House online Facebooks and combining ID photos onto his website, allowing viewers to vote for the “hotter” of two randomly chosen photos and rate the looks of students in a particular House against fellow-residents.

Mark Zuckerberg

- Winklevoss and Zuckerberg met three times
- Winklevoss sent him all their code
- They exchanged 52 emails
- At first, Zuckerberg was enthusiastic: “I read over all the stuff you sent and it seems like it shouldn’t take too long to implement, so we can talk about that after I get all the basic functionality up tomorrow night.”
- After one week, progress stopped
- Zuckerberg claimed he was busy
- He kept promising the code, but never delivered ANY CODE AT ALL
Mark Zuckerberg

- Meanwhile, MZ was developing his own site, thefacebook.com
- On January 8, 2004, MZ confirmed to Winklevoss he would deliver the finished code for ConnectU
- But on January 11, 2004, MZ registered the domain thefacebook.com
- January 14, 2004: last meeting between MZ and Winklevoss. No hint of any problem other than delay
- February 9: Winklevoss read in the Harvard Crimson about MZ’s new site, thefacebook.com
- The relationship ended. The feud began.

Harvard Crimson Announcement

What Was Zuckerberg Doing?

- MZ’s emails and instant messages during the November-January development period have surfaced
- On December 7, one week after agreeing to work with Winklevoss, MZ sent his partner Eduardo Saverin this message:
  “they made a mistake haha. They asked me to make it for them. So I’m like delaying it so it won’t be ready until after the facebook thing comes out.”
- Other messages are too obscene to be included here
- MZ also hacked the existing ConectU site to make it less useful

ConnectU v. Facebook

- ConnectU sued Facebook and Zuckerberg in July 2007 in Massachusetts.
- Allegations:
  - Zuckerberg intentionally hampered the development of ConnectU while working there
  - Facebook infringes ConnectU’s copyrights
  - Facebook misappropriated ConnectU’s trade secrets
- A hearing was held in July 2007. The judge was unimpressed with ConnectU’s case and allowed it time to collect supporting evidence
ConnectU v. Facebook

- A mediation was held in February 2008
- At the mediation, representations were made about the value of Facebook stock and a settlement term sheet was drafted
- The Court found that a settlement had been reached and ordered enforcement of the term sheet

Facebook v. ConnectU

- ConnectU provided a tool that enabled Facebook users to provide ConnectU with their login credentials, which ConnectU then used to grab data from Facebook’s servers.
- The California Penal Code provides for action against anyone who “knowingly accesses and without permission takes, copies, or makes use of any data from a computer, computer system, or computer network.”
- In May 2007, Facebook sued ConnectU in Federal court in California
- This case also settled

The Settlement

- The settlement covered both cases
- The Winklevoss received USD 65,000,000:
  - USD 20,000,000 in cash
  - USD 45,000,000 in common stock
- How many shares?
- Facebook said it had just sold some shares to Microsoft for about USD 35.90
- The Winklevoss received 45,000,000/35.90 = 1,253,000 shares of Facebook

Revoking the Settlement

- After the settlement was finalized, the Winklevoss learned that Microsoft had received preferred stock
- Facebook employees who got common stock were told it was worth $8.88, not $35.90
- The Winklevoss should have received about 5,000,000 shares, not 1,253,000
- They sued to overturn the settlement
Securities Law

- U.S. Securities and Exchange Commission Rule 10b-5
  “Employment of Manipulative and Deceptive Practices”
- “It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange, …
  (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading … in connection with the purchase or sale of any security
- Winklevoss allege violation of 10b-5

Revoking the Settlement

- The first court denied their claim on the basis that
  – (1) settlements are favored in the law
  – (2) Rule 10b-5 does not apply to settlement negotiations
- The case is now on appeal to the Ninth Circuit Court of Appeals in California
- Oral argument was heard on Jan. 11, 2011; no decision yet. A U.S. Supreme Court appeal seems certain

Revoking the Settlement

- In October 2010 Facebook stock split 5-1.
- Winklevoss now have 6,265,000 shares
- On Feb. 18, 2011, some Facebook shares changed hands at USD 37.00, giving Facebook a valuation of 83 billion
- The Winklevoss now hold USD 252 million:
  – USD 20 million in cash
  – USD 232 million in stock
- They should have had $20 + 925 = 945 million if the stock had been valued properly in 2008

Revoking the Settlement

- The public seems to think the Winklevoss are trying to get $945 million instead of $252 million
- Seems greedy
- That is NOT the outcome they want
- They want the settlement voided –
  – They have to give back the cash and stock (which are in escrow)
  – They must start from ZERO and continue with the original lawsuit
- What would YOU do?
facebook financing

- June 2004. Initial investment of $500,000 for 7% of the company by Peter Thiel, a founder of PayPal
- 2005. USD 13 million from Accel partners, 27.5 million from Greylock Partners
- October 2007. Microsoft: 240 million
- November 2007. Li Ka-shing: 60 million
- March 2008. Li Ka-shing: another 60 million
- September 2009. First positive cashflow
- January 2011. Goldman Sachs: 450 million, committed to raise 1.5 billion more

facebook growth

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Facebook Growth
(Millions of users)

By Ben Foster @benphoster

Google v. Facebook

Unique Visitors

Data: comScore (Worldwide data; Google includes Google-branded sites, such as Google.com, Google.nl, etc.).

SOURCE: SILICON ALLEY INSIDER
Why Is Google Having Trouble?

- Facebook is still a “ground floor” opportunity. Much smaller (1/12 in employees) – more chance to shine
- One in five Facebook employees came from Google!
- Facebook stock is appreciating fast; Google is stable
- Facebook is perceived as the hottest employer in technology
- Facebook captures more eye-minutes per month than any site
- Facebook has room to grow with new applications: messaging, payments, groups, games, etc.
- Google is essential but non-social