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Microsoft's Facebook stake influenced ConnectU case

by [Greg Sandoval](#)

SAN JOSE, Calif.--What is Facebook really worth?

One of the burning questions in the technology business during the past year also played a major role in the dispute between social networks ConnectU and Facebook, according to documents obtained by CNET News.com.

Some interesting details about Facebook's valuation were revealed in partially redacted court records released Wednesday by federal district judge James Ware. The documents were a transcript of a June 23 hearing in the [case, which Ware had closed to the public](#). The judge [released the redacted transcripts](#) after CNET Networks, parent company of News.com, objected to the closing and launched an effort to have relevant documents unsealed.

ConnectU, founded by brother Cameron and Tyler Winklevoss and Divya Narendra, filed suit against Facebook founder Mark Zuckerberg in 2004 and accused him of stealing their business plan. The two sides [reached a settlement](#), but ConnectU's side tried to pull out of the deal after alleging that Facebook fraudulently misrepresented the value of its stock. Ware disagreed and last week ordered that the settlement be enforced. That means Facebook is nearing the end of the ConnectU case.

But what the transcripts show was just how much Microsoft inadvertently influenced the proceedings.

Last fall, [Microsoft paid \\$240 million to acquire](#) a 1.6 percent share of Facebook. The day that news of the deal broke, headlines screamed that Facebook was worth \$15 billion based on Microsoft's investment.

Analysts said all along that the money Microsoft paid was more a reflection of the company's need to strengthen ties to Facebook than what Microsoft thought the company was really worth. Judging from the transcripts, the Microsoft money may have gotten ConnectU's founders seeing dollar signs. But it shouldn't have, according to statements made during the June 23 hearing by Facebook attorney Neel Chatterjee.

The value of Facebook shares

As part of the settlement, Facebook agreed to give ConnectU's four principals--Narendra, the brothers Winklevoss, and their father, Howard Winklevoss, who had invested in ConnectU--an undisclosed amount of cash and Facebook stock. In exchange, ConnectU's principals agreed to give Facebook all the stock they held in ConnectU. The settlement was essentially an acquisition.

In a statement to the court, a small portion of which was redacted, it's obvious that Chatterjee wanted to make clear that Microsoft's investment in Facebook had little in common with ConnectU's deal. The transcript indicates that ConnectU received common stock while Microsoft received preferred stock.

"ConnectU didn't get that and they knew they weren't getting that," Chatterjee said. "What Microsoft got out of the deal...are fundamentally different than what ConnectU is getting, or the principals of ConnectU, which was subject to the fair-market valuation."

Chatterjee pointed out that Facebook provided ConnectU with fair-market valuations it obtained when it considered using stock for other partnerships. But he also noted that if ConnectU wanted to know what Facebook was worth it could have obtained its own "independent appraisal," which it did not do before agreeing to the settlement.

Getting an accurate Facebook valuation was not why ConnectU had sought to challenge the settlement, said the company's attorney, David Barrett. ConnectU argued that the settlement was unenforceable for several reasons, the first being that Facebook withheld vital information.

"The point is that (Facebook's) duty is to disclose all material information," Barrett said, noting that Facebook is a privately held company but comes under security laws when selling shares. "If they decide to engage in a private trade of their stock, they do have to disclose material information."

Specifically, Barrett said that Facebook's board of directors obtained an evaluation of their company's worth following the Microsoft sale but before the settlement was reached. ConnectU claimed that Facebook never handed over that valuation. The transcript of the hearing didn't reveal the amount of Facebook's valuation.

But on Thursday, [*The New York Times*](#)' Brad Stone reported that in a transcript from a June 13 case management conference, that figure was revealed: "one-quarter of its apparent value based on Facebook's public press releases." That would put the price of Facebook at \$3.75 billion.

As Stone points out that valuing private companies is not exact and we'd have to wait until someone actually plunks down real money for Facebook in an acquisition or in a public offering of the company's stock. In any case, Chatterjee, Facebook's attorney, told the court he suspected that the reason ConnectU's founders had changed their mind about the settlement was because of a dispute with the company's former law firm, Quinn Emanuel. The reality of legal fees "was affecting the economics in some way they don't like," Chatterjee said.

Lawyers from Quinn Emanuel have filed a lien against ConnectU's settlement money, and appeared before Ware on Wednesday to request that he not release any of the company's funds until they got paid.

CNET News.com's Caroline McCarthy contributed to this report.

http://news.cnet.com/8301-10784_3-9983579-7.html