

DIVERSE LEADERS VENTURE PROGRAM

Program Guidelines | December 2022



Table of Contents

Section I – General	1
A. Introduction	1
Section II – Eligibility	2
A. Use of Funds	2
B. Program Requirements	2
C. Program Structure	3
Section III – Application Process	4
A. Initial Application Requirements	4
B. Approval Process	4
C. Post Approval Process	5
D. Reporting Requirements	5
E. Sample Fund Term Sheet	7

Section I – General

A. Introduction

The Diverse Leaders Venture Program component of the Pennsylvania – SSBCI Program (PA- SSBCI) provides loans to venture capital general partners of diverse status having the wherewithal to invest in Pennsylvania small businesses. The loan will be matched by private funding that will create investments in small businesses led by individuals of diverse status that are in need of support and resources to expand and create jobs. For purposes of this program, diverse status is not limited to race or ethnicity but rather is broadly inclusive of membership in a variety of additional types of underserved populations, such as, for example, those based on geographic location or socioeconomic status.

PA-SSBCI was established with federal funding through the Federal State Small Business Credit Initiative (SSBCI), which was reauthorized by the American Rescue Plan Act of 2021 (ARPA) as a response to the economic effects of the COVID-19 pandemic. SSBCI is administered by the U.S. Department of the Treasury (Treasury). The funding includes a main capital allocation to support small businesses, an allocation for business enterprises owned and controlled by socially and economically disadvantaged individuals (SEDI-owned businesses), an incentive allocation for SEDI-owned businesses, and an allocation for very small businesses (VSBs).

Diverse Leaders Venture Program provides funding or capital to venture funds to address the financing needs of technology-oriented businesses by increasing the amount of risk capital available to such companies. Diverse Leaders Venture Program is for venture funds owned and controlled by general partners of diverse status that are targeting seed and later-stage capital investments in businesses owned and controlled by diverse status populations. Diverse Leaders Venture Program is administered by DCED under the direction of the Ben Franklin Technology Development Authority (“BFTDA”). The Diverse Leaders Venture Program is being established under 12 U.S.C. § 5701(12), as an Other Credit Service Provider (“OCSP”) program that uses public resources to promote private access to credit, and that meets certain eligibility criteria. In a SSBCI venture capital program, the “investor” can be an entity of the state; any private venture capital, seed-stage, or angel fund participating in an approved SSBCI program (but not individual investors in such a fund); or a special purpose vehicle or entity. The “investee” is the small business that is the end recipient of SSBCI funds, either directly or indirectly through a venture capital fund.

Section II – Eligibility

A. Use of Funds

The eligible applicants for the Diverse Leaders Venture Program can use funding to directly provide seed and later-stage capital for existing and emerging companies involved in the development and commercialization of technologically advanced products and processes.

B. Program Requirements

1. In order to apply for Diverse Leaders Venture Program funding, applicants must demonstrate their venture fund status as defined by 17 C.F.R. § 275.203(I)-1, which includes the following:
 - a. Represents to investors and potential investors that it pursues a venture capital strategy;
 - b. Immediately after acquisition of any asset, other than qualifying investments of short-term holdings, holds no more than 20% of the amount of the fund's aggregate capital contributions and uncalled committed capital in assets (other than short-term holdings) that are not qualifying investments, valued at cost or fair value, consistently applied by the investor;
 - c. Does not borrow, issue debt obligations, provide guarantees or otherwise incur leverage, in excess of 15% of the aggregate investor capital;
 - d. Only issues securities the terms of which do not provide a holder with any right, except in extraordinary circumstances, to withdraw, redeem or require the repurchase of such securities but may entitle holders to receive distributions made to all holders pro rata; and
 - e. Is not registered under Section 8 of the Investment Company Act of 1940 ("Act") and has not elected to be treated as a business development company pursuant to Section 54 of the Act.
2. Diverse Leaders Venture Program committed capital must be utilized as the anchor or initial investor in the fund being established.
3. Investments should target small technology-oriented businesses with high growth potential. Individual equity investments may not exceed \$20M in size, over the life of the investment. The \$20M limitation may not be avoided by dividing the investment into separate investments or creating separate instruments within an investment rounds.
4. Target businesses should demonstrate in some way that management is of diverse status. Participating venture funds must identify applicable companies prior to funding.
5. For purposes of Diverse Leaders Venture Program, participating venture funds:
 - a. Must invest entirely in Pennsylvania-located companies; or
 - b. There must be a reciprocal arrangement with other states agreeing to invest on pro-rata basis into said venture fund such that SSBCI funds will only be utilized by designated states in the given fund on a proportional basis.
6. Diverse Leaders Venture Program capital may not represent more than 20% of overall committed capital to any venture fund under consideration.
7. Diverse Leaders Venture Program funding is conditioned upon the applicant's meeting certain fundraising goals established at the time of approval. Only venture funds that evidence the ability to close on aggregate commitments of \$10M or more will be considered.

8. An additional goal of the Diverse Leaders Venture Program is to achieve a competitive rate of return on its total investment. As such, prospective venture funds must be prepared to demonstrate satisfactory prior returns.
9. The entity receiving Diverse Leaders Venture Program funding will comply with all reporting requirements described in Section II, D.3.
10. The comprehensive evaluation of each applicant will include the review of all the following factors:
 - a. The applicant's strategy fits the mission of PA-SSBCI and the Diverse Leaders Venture Program.
 - b. The capacity, skills and experience of the management team.
 - c. The current and historical performance of the applicant's investment portfolio.
 - d. The applicant's potential to sustain successful operations as a financial institution.
 - e. The terms and conditions are investor friendly and are considered industry standard.
11. Candidate venture fund managers must have exposure to the risk of their respective portfolio in a manner that is consistent with industry standards.
12. No assistance shall be awarded to an applicant under this program unless the applicant certifies that the applicant shall not discriminate against any employee or against any person seeking employment by reason of race, gender, creed, color, sexual orientation, gender identity or expression, or in violation of the Pennsylvania Human Relations Act, which prohibits discrimination on the basis of race, color, religious creed, ancestry, age, sex, national origin, handicap or disability, or in violation of any applicable federal laws.

C. Program Structure

1. Diverse Leaders Venture Program will be administered by the BFTDA via the Pennsylvania Department of Community and Economic Development ("DCED").
2. Funding is available in the form of loans. Applicants should note that, as such, the BFTDA will not participate as a traditional limited partner. A sample BFTDA loan term sheet which outlines requirements for the BFTDA's manner of participation is included in Section II herein.
3. Administrative Costs – Documented administrative costs necessary for administering the venture fund shall not exceed 1.7% of the loan amount. This amount may vary on a year-by-year basis; however, over the life of the venture fund, the percentage rate must average out to 1.7%. Any overage of this allowance must be repaid to the Commonwealth before the expiration of the loan agreement. The fund will be required to identify the services provided.
4. The BFTDA has historically authorized venture loan amounts ranging from \$1-5M, with most loans averaging \$2M. These amounts have been predicated on venture firm qualifications, strategy and ultimate total committed capital. It is envisioned that these historical allocation ranges will apply to the Diverse Leaders Venture Program.

Section III – Application Process

A. Initial Application Requirements

1. Applications may be filed at any time during the fiscal year with approval subject to availability of funding and BFTDA Board approval. Initial applications must include the following:
 - a. Private Placement Memorandum (PPM) pursuant to Reg. D or Reg. S of the Securities Act of 1933 (if available).
 - b. Written responses to **Appendix A** of the Fund Questionnaire A.
 - c. In some cases, a pre-packaged “due diligence binder” that the Fund provides may be accepted in lieu of **Appendix A**. Requests for this option should be addressed to the program manager.
2. **Submissions may be sent via email to:** dcervedventureinvest@pa.gov

If email is unavailable, hard copies may be delivered to:

PA Department of Community and Economic Development
BFTDA Venture Investment Program
Commonwealth Keystone Building
400 North Street, 4th Floor
Harrisburg, PA 17120-0225
(717) 787-4147

B. Approval Process

1. Staff will assist the applicant in the review process and will analyze all submitted documentation. Staff may involve employees of the DCED, consultants, analysts, and other professionals under contract to the DCED.
2. If DCED chooses to move forward, staff will issue an *Invitation to Apply* and the applicant will also be required to complete **Appendix B** of the Fund Questionnaire B.
3. The applicant will be requested to complete the [DCED Single Application for Assistance](#).
 - a. The Single Application for Assistance can be printed and/or completed online by accessing: dced.pa.gov/singleapp.
 - b. Copies of the Single Application kit may also be obtained by contacting the DCED Customer Service Center at 1-800-379-7448 or 717-787-3405 or e-mailing: dcervedventureinvest@pa.gov.
4. Applicants will be required to attach completed versions of **Appendix A, B and C** to the [Single Application for Assistance site](#).
5. If successfully vetted by staff, the application will be submitted to the BFTDA Board for review and approval. The BFTDA Board meets four times annually.
6. Applications may be rejected or deferred for, including but not limited to, any of the following reasons:
 - a. The applicant’s failure or refusal to provide pertinent information regarding the venture fund deemed essential by the BFTDA Board to adequately perform a due diligence review.

- b. The case for financial return is not convincing.
- c. The anticipated economic development benefit to the region or Pennsylvania is non-existent or negligible, or the level of proposed return is not commensurate with the requested loan amount.
- d. The applicant does not maintain a substantive presence within the Commonwealth of Pennsylvania.
- e. Sufficient resources are not available to the BFTDA to make an investment in the venture fund.
- f. Non-compliance with any requirements adopted by the BFTDA Board.

C. Post Approval Process

1. After BFTDA Board approval, staff will work with the investor to close and disburse the investment in accordance with approved terms.
2. Prior to closing, the investor must certify that it shall not discriminate against any employee or against any applicant for employment because of race, gender, creed, color, sexual orientation, gender identity or expression, or in violation of the Pennsylvania Human Relations Act, which prohibits discrimination on the basis of race, color, religious creed, ancestry, age, sex, national origin, handicap or disability, or in violation of any applicable federal laws. In addition, the applicant and its principals must be current in payment of all state and local taxes unless they have entered into a workout agreement satisfactory to the respective taxing authority and are in full compliance with the terms thereof.
3. Following disbursement of funds, staff will monitor the activities of the investor to ensure that the conditions of the Diverse Leaders Venture Program investment are being observed and met. Staff will advise the BFTDA Board of any substantive failure to perform by the investor. The BFTDA Board will have full authority to take all actions necessary to protect and preserve its investment, including but not limited to appropriate legal action when required.
4. The investor shall maintain full and accurate records with respect to its fund and shall ensure adequate control over the records of all related parties in the fund. Staff shall have access to such records and be able to inspect all relevant records at reasonable times and places. Upon request, the applicant must furnish all data, reports, contracts, documents and other information relevant to the fund, as may be requested in the investment documents.
5. If, subsequent to funding, it is determined that the application contained material misrepresentations, or funds were used for ineligible activities or activities not permitted under the terms of the approved financing, the investor will be in default and the BFTDA Board may demand immediate repayment of any and all funds advanced in connection with the investment. In addition, the matter may be referred to the appropriate authorities for criminal investigation.

D. Reporting Requirements

1. Investors must provide to DCED all reports and communication which are distributed to the investor's limited partners (ex: quarterly updates and financials, audited annual financial reports, etc.) as prescribed in the limited partnership agreement.
2. In addition, investors will provide the information requested in **Appendix D (1-2)**. These reports are to be returned to DCED for each calendar quarter of each year that the Diverse Leaders Venture Program investment remains active. These requested reports shall be furnished simultaneously with customary partnership reporting as outlined in the investment agreement.

3. Investors will be required to keep the Diverse Leaders Venture Program funds segregated, either through separate checking accounts or accounting systems that can maintain records of Diverse Leaders Venture Program funds.
4. Investors must also have the appropriate administrative and internal control systems in place to safeguard against waste, loss, unauthorized use or misappropriation of the Diverse Leaders Venture Program funds in accordance with the federal Uniform Administrative Requirements, Cost Principles and Audit Requirements (2 C.F.R. § 200).
5. Investors will also be required to comply with the audit requirements contained within subpart F.
6. The investor must maintain full and accurate records with respect to the project and must ensure adequate control over related parties in the project.
7. The Commonwealth will require access to such records, as well as the ability to inspect all work, invoices, materials, and other relevant records at reasonable times and places. Upon request of DCED, the investor must furnish all data, reports, contracts, documents, and other information relevant to each loan/investment.
8. Investors will be required to provide transaction level data in a timely manner to DCED. Failure to do so may result in the loss of future disbursements.

E. Sample Fund Term Sheet

FUND TERM SHEET

This term sheet summarizes the principal terms with respect to a potential loan to _____ by the BFTDA. The term sheet is intended solely as a basis for further discussion and is not intended to be and does not constitute a legally binding obligation. No legally binding obligation will be created until a final document is executed and delivered by both parties.

Lender BFTDA

Borrower _____, a _____
("Borrower")

Principal Amount \$[x] aggregate principal amount, anticipated to be Funded during the ____ quarter of ____.

Recourse The Loan will be non-recourse to the members of the Borrower with limited exceptions.

Maturity Approximately 10 years, or such later date as the Borrower may be liquidated.

Interest The lesser of (i) [x]% per annum or (ii) available cash flow, i.e., an amount equal to the amount that would have been distributed to Lender if, on a hypothetical basis, the loan amount had been a limited partnership interest in the Partnership.*

Certain Covenants The agreement governing the loan will contain covenants that, among other things, will:

- Require use of proceeds by Borrower to invest in _____ ("Partnership"), which will have received capital commitments of at least \$10M.

Repayment The loan may not be pre-paid such that prepayment would exceed the amount that would have been distributed to the Lender if, on a hypothetical basis, the loan amount had been a limited partnership interest in the Partnership. Nevertheless, the loan will be immediately repayable upon liquidation or sale of all or substantially all of the assets of the Borrower or the Partnership.

**Example: the Borrower raises total commitments of \$10M which includes a commitment of \$1M facilitated with the BFTDA's loan at 8% interest.*

Scenario 1

- If the fund were to distribute \$500,000 in year 1:
\$50K would be credited to the BFTDA and the entire amount would be characterized as interest.
- If the fund were to distribute \$800,000 in year 1:
\$80K would be credited to the BFTDA and the entire amount would be characterized as interest.
- If the fund were to distribute \$1,000,000 in year 1:
\$100K would be credited to the BFTDA of which \$80,000 would be characterized as interest and the remaining amount would be categorized as principal repayment.

Scenario 2

- If the fund were to distribute nothing in year 1 and \$500,000 in year 2:
The cash flow waterfall would be the same as Scenario 1-a (as stated above).
- If the fund were to distribute nothing in year 1 and \$800,000 in year 2:
The cash flow waterfall would be the same as Scenario 1-b (as stated above).
- If the fund were to distribute nothing in year 1 and \$1,000,000 in year 2:
\$100K would be credited to the BFTDA of which \$80,000 would be characterized as interest due for year 1 and \$20,000 would be interest due for year 2.