

COMPLIANCE ASSESSMENT
RHODE ISLAND STATE SMALL BUSINESS CREDIT INITIATIVE
(SSBCI) PROGRAMS

August 14, 2013

Prepared by:



**Lyon Park
Associates**

Overview

The purpose of this compliance assessment is to document the extent to which Rhode Island's State Small Business Credit Initiative (SSBCI) programs comply with federal SSBCI requirements. Treasury approved Rhode Island's request to use its \$13,168,350 allocation to:

- Provide \$2,168,350 in additional funding for the Small Business Loan Fund, a pre-existing loan participation program operated by the non-profit Small Business Loan Fund Corporation (SBLFC);
- Make a \$9,000,000 investment in the Slater Technology Fund, administered by the non-profit Slater Fund, Inc., so that the fund may make direct equity investments in eligible small businesses; and
- Make a \$2,000,000 investment in the Betaspring Fund 100, administered by the for-profit Betaspring 100 Fund, LLC, so that the fund may make direct equity investments in eligible small businesses.

The federal SSBCI requirements are set forth in the Small Business Jobs Act of 2010; the SSBCI Policy Guidelines; the SSBCI National Standards for Compliance and Oversight; the SSBCI Frequently Asked Questions (FAQs); and Rhode Island's SSBCI Allocation Agreement, which incorporates Rhode Island's application by reference, as well as OMB Circular A-87 (Cost Principles for State, Local, and Tribal Governments). This report also seeks to provide general recommendations for process improvements to mitigate specific instances of non-compliance and to prevent such patterns of non-compliance from occurring in the future.

Lyon Park Associates conducted an on-site compliance assessment of Rhode Island's SSBCI programs from April 15, 2013, to April 19, 2013. During the course of this compliance assessment, Lyon Park Associates reviewed the files for:

- Both SSBCI-supported Small Business Loan Fund loans enrolled as of April 15, 2013;
- Fifteen investments in specific small businesses that were enrolled in the Betaspring Fund 100 using SSBCI funds and that closed on or before December 31, 2012 (out of 25 total);
- All six venture capital investments that were enrolled in Slater Technology Fund using SSBCI funds and that closed on or before December 31, 2012; and
- A judgmental sample of three direct administrative expenses charged by the Small Business Loan Fund Corporation against the SSBCI award through December 31, 2012.

Lyon Park Associates also reviewed the following materials provided by the Small Business Loan Fund Corporation:

- Rhode Island's SSBCI Allocation Agreement;
- Rhode Island's approved SSBCI Application;
- A risk assessment questionnaire¹ completed by the Small Business Loan Fund Corporation;
- A risk assessment questionnaire² completed by the Betaspring 100 Fund;
- A risk assessment questionnaire³ completed by the Slater Fund, Inc.;
- A detailed list of all administrative expenses charged against the SSBCI award;
- The Memorandum of Understanding (MOU) signed by the State of Rhode Island, represented by the Department of Administration (DOA); the Rhode Island Economic Development Corporation (RIEDC), a governmental agency charged with spearheading the state's economic development efforts; and SBLFC, a subsidiary of RIEDC;
- The Operating Agreement for Startup Investments, LLC, a Rhode Island limited liability company set up by the Betaspring Fund 100's managers to deploy SSBCI funds;
- A Reporting Agreement executed between SBLFC and Startup Investments, LLC;
- The Subscription Agreement requiring SBLFC to make an immediate \$1.4 million dollar investment in Startup Investments, LLC, with a subsequent investment of \$600,000 to be paid in November 2012; and
- The Grant Agreement between SBLFC and the Slater Technology Fund, Inc.

Lyon Park Associates found that Betaspring Fund 100 may have repeatedly committed serious violations of U.S. Treasury regulations. More isolated compliance issues were identified in the Slater Technology Fund program. Lyon Park Associates' findings for each program are described in detail below.

¹ The risk assessment questionnaire is a written survey especially created by Lyon Park Associates to identify potential compliance risks and shape the development of the audit procedures and the audit sample. Because the contract was not signed until two business days before Lyon Park Associates arrived for the on-site audit, Lyon Park Associates administered the questionnaire as an oral survey during the on-site assessment.

² Administered as an oral survey during the on-site assessment.

³ Administered as an oral survey during the on-site assessment.

Rhode Island Small Business Loan Fund

Methodology

Lyon Park Associates reviewed all two loans enrolled in the Rhode Island Small Business Loan Fund as of April 15, 2013.

In conducting this compliance assessment, Lyon Park Associates evaluated each of these loans (see Appendix A) to determine compliance with:

- The statutory requirement that the enrolled Other Credit Support Program (OCSP) loan not exceed \$20 million;
- The statutory requirement that lenders have “a significant amount of capital at risk,” as further elaborated in the SSBCI Policy Guidelines, which define a “significant amount” as 20 percent of the enrolled loan or investment;
- The statutory prohibition against the use of funds to make a loan to a “borrower that is a refinancing of a loan previously made to that borrower by the financial institution lender or an affiliate of the financial institution lender,” as further clarified in the SSBCI Policy Guidelines and the Frequently Asked Questions (FAQs) pertaining to refinancing;
- The use of proceeds prohibitions contained with the SSBCI Policy Guidelines, and reproduced in the borrower use of proceeds certification, that, among other things, prohibit the use of funds to purchase all or part of an ownership interest in a business and prohibit the use of funds for passive real estate investment, as further clarified by the Frequently Asked Questions (FAQs) pertaining to passive real estate investment; and
- The requirement to obtain (a) the borrower use of proceeds certification, (b) a lender use of proceeds certification signed by the lender making the private companion loan needed to comply with the 20 percent private capital at risk requirement ⁴, (c) a lender use of proceeds certification signed by SBLFC, (d) the borrower certification that none of its principals has been convicted of a sex offense against a minor, (e) a lender certification that none of its principals

⁴ The SSBCI National Standards for Compliance and Oversight clarify that “when a Participating State makes a direct loan or a companion loan under the approved direct loan or loan participation program, three use of proceeds forms must be executed: one by the borrower, one by the Participating State [in this case, SBLFC], and one by the lender making the companion loan.” However, in a July 10, 2013, email to SBLFC, Treasury SSBCI compliance officer Rick Oettinger offered a new interpretation of this requirement, stating that “the principal’s [i.e. borrower’s] private investment can count towards the 20% private capital at-risk. Only one set of certification/assurance needs to be obtained.”

has been convicted of a sex offense against a minor,⁵ signed by the lender making the private companion loan needed to comply with the 20 percent private capital at risk requirement , and (f) a lender certification signed by SBLFC, stating that none of its principals has been convicted of a sex offense against a minor. Although there were no findings pertaining to this program, Lyon Park Associates recommends that SBLFC develop an SSBCI compliance checklist, to include all borrower and lender certifications and evidence of private capital at risk. This checklist should specifically inquire whether the loan is to a real estate holding company (in which case, the checklist should require staff to indicate whether each and every requirement related to the FAQ on passive real estate investment is met) or for the purpose of paying off a prior debt (in which case, the checklist should require staff to indicate whether each and every requirement related to the FAQ on refinancing is met).

Betaspring Fund 100

Background

In Annex 1 of Rhode Island's SSBCI Allocation Agreement, Treasury and Rhode Island agreed that the state would use \$2,000,000 of its allocated funds to invest in the Betaspring Fund 100, administered by the for-profit Betaspring 100 Fund, LLC, so that the fund may make direct equity investments in eligible small businesses. Annex 1 identified Rhode Island's Department of Administration (DOA) as the state agency responsible for the implementation of Rhode Island's Approved State Programs and, as a result, required DOA to apply the provisions included in Articles IV and VI of the SSBCI Allocation Agreement to SBLFC, Slater Fund, Inc., and the Betaspring Fund 100. Articles IV and VI of the SSBCI Allocation Agreement either contain, or include by reference, all SSBCI compliance requirements.

On September 6, 2011, a Memorandum of Understanding (MOU) was signed by the State of Rhode Island, represented by DOA; the Rhode Island Economic Development Corporation (RIEDC), a governmental agency charged with spearheading the state's economic development efforts; and SBLFC, a subsidiary of RIEDC. In this MOU, DOA agreed to transfer all of the state's allocated funds to SBLFC, and SBLFC agreed to accept "full responsibility and accountability for all the requirements, duties, responsibilities and terms set forth in this Agreement, the Allocation Agreement, and the Act."

⁵ The SSBCI National Standards for Compliance and Oversight clarify that "the design of most direct loan programs, as well as loan participation programs based on companion loans rather than purchased participations, is such that lenders making companion loans must also provide the required sex offender certifications. If a Participating State believes that this requirement may not apply to its direct loan or loan participation program due to specific program-design considerations, the Participating State should contact Treasury for further consultation." In practice, whenever Treasury has been consulted, Treasury always finds that the private lender must sign the sex offender certification unless there is no subordination of collateral or priority of payment.

Although this MOU did not strictly comply with Treasury's requirement to apply the provisions of Articles IV and VI to SBLFC, it did bind SBLFC to the requirements contained therein. However, the language in Annex 1 of the SSBCI Allocation Agreement suggests that Treasury intended for DOA—not SBLFC—to directly oversee the activities of the Betaspring Fund 100 and the Slater Technology Fund.

On November 29, 2011, SBLFC and Betaspring Fund 100 executed an Operating Agreement for Startup Investments, LLC, a Rhode Island limited liability company set up by the Betaspring Fund 100's managers to deploy SSBCI funds. As shown in Schedule 1 of the Operating Agreement, SBLFC received 50,000 shares in Startup Investments, LLC, in return for a \$2 million contribution of SSBCI funds, while Betaspring Managers 100, LLC (an entity whose sole purpose is to employ the managers of the Betaspring Fund 100) received 50,000 shares in the company in exchange for \$10,000 and an in-kind donation of "services." A subsequent subscription agreement, dated December 23, 2012, required SBLFC to immediately provide \$1.4 million, with the remaining \$600,000 to be paid in November 2012.

In December 2011⁶, SBLFC executed a Reporting Agreement with Startup Investments, LLC. Under the heading "Applicable Laws and Agreements," this agreement included a statement that: "Startup warrants and represents that its activities under this Agreement and all activities conducted by it and the Fund under the Beta program shall to its knowledge and applying commercially reasonable efforts comply with in all material respects with the Allocation Agreement, the MOU, and all applicable Federal, state, and local government ordinances, laws and requirements including, but not limited to, the Act." The Rhode Island SSBCI Allocation Agreement was attached to the agreement as Exhibit A.

Section 8.2 of Rhode Island's SSBCI Allocation Agreement specifies that the "**Application, including any attachments, exhibits, appendices and supplements thereto** [emphasis added], any attachments, schedules, annexes, appendices and supplements to the Allocation Agreement, and said Allocation notice letter are incorporated in and made a part of this Agreement." Therefore, a key part of this compliance assessment was to determine whether the state and its subcontractors operated the Approved State Programs in accordance with Rhode Island's approved SSBCI application. In the portion of the approved application that described the Betaspring Fund 100, Rhode Island stated that "all SSBCI funds invested by Betaspring will be used for equity investment. All funds will represent a cash investment in the portfolio companies and will be shown as paid-in capital to the companies' balance sheets." The application also states that the fund will "make direct SSBCI investments in portfolio companies of about \$20,000 cash to fund company growth; [make] total investments averaging \$42,500 in SSBCI and private seed capital in each company; [and] obtaining [sic] and utilizing [sic] an additional \$8,000 to \$33,000 each in sponsorship services...." While the application makes it clear that investees will be graduates of Betaspring's affiliated accelerator, the application does not suggest that any funds will be used to fund the Betaspring Fund 100's operating expenses. The application does indicate that a

⁶ The exact date of the agreement is not known. The signed agreement provided to Lyon Park Associates did not have the date filled in. The first line of the agreement reads: "This Reporting Agreement (this "Agreement") is entered into as of this ___ day of December 2011...."

portion of the \$42,500 in seed capital “will be used to help pay for services including mentorship, legal counsel, incorporation filing, and other legal work necessary to complete the business model,” but it does not specify which entities will provide these services to the investees.

Methodology

Lyon Park Associates reviewed 15 of the 25 venture capital investments made by Startup Investments using SSBCI funds through December 31, 2012. In conducting this compliance assessment, Lyon Park Associates evaluated each of these investments (see Appendix B for a detailed list of all 15 investments, including any exceptions noted) to determine compliance with:

- The statutory requirement that the enrolled Other Credit Support Program loan (investment) not exceed \$20 million;
- The statutory requirement that lenders (investors) have “a significant amount of capital at risk,” as further elaborated in the SSBCI Policy Guidelines, which defines a “significant amount” as 20 percent of the enrolled loan or investment;
- The statutory requirement that that the Approved State Program “can demonstrate that, at a minimum, \$1 of public investment by the State program will cause and result in \$1 of new private credit”;
- The statutory prohibition against the use of funds to make a loan to a “borrower that is a refinancing of a loan previously made to that borrower by the financial institution lender or an affiliate of the financial institution lender,” as further clarified in the *SSBCI Policy Guidelines* and the Frequently Asked Questions (FAQs) pertaining to refinancing;
- The use of proceeds prohibitions contained with the *SSBCI Policy Guidelines*, and reproduced in the borrower use of proceeds certification, that, among other things, prohibit the use of funds to purchase all or part of an ownership interest in the business and prohibit the use of funds for passive real estate investment, as further clarified by the Frequently Asked Questions (FAQs) pertaining to passive real estate investment;
- The program design parameters set forth in Rhode Island’s approved SSBCI application, which are incorporated by reference into Rhode Island’s SSBCI Allocation Agreement;
- The requirement to report and document subsequent private financing, in accordance with Annex 7 of the Rhode Island SSBCI Allocation Agreement; and
- The requirement to obtain (a) the borrower use of proceeds certification, (b) the lender (investor) use of proceeds certification, (c) the borrower certification that none of its principals has been convicted of a sex offense against a minor, and (d) the lender (investor) certification that none of its principals has been convicted of a sex offense against a minor.

Findings

Startup Investments/Betaspring Fund 100 is not implementing the program in accordance with Rhode Island's approved SSBCI application

As stated above, Section 8.2 of Rhode Island's SSBCI Allocation Agreement specifies that the "***Application, including any attachments, exhibits, appendices and supplements thereto*** [emphasis added], any attachments, schedules, annexes, appendices and supplements to the Allocation Agreement, and said Allocation notice letter are incorporated in and made a part of this Agreement." Therefore, a key part of this compliance assessment was to determine whether the state and its subcontractors operated the Approved State Programs in accordance with Rhode Island's approved SSBCI application.

In the portion of the approved application that described the Betaspring Fund 100, Rhode Island stated that "all SSBCI funds invested by Betaspring will be used for equity investment. All funds will represent a cash investment in the portfolio companies and will be shown as paid-in capital to the companies' balance sheets." The application also states that the fund will "make direct SSBCI investments in portfolio companies of about \$20,000 cash to fund company growth; [make] total investments averaging \$42,500 in SSBCI and private seed capital in each company; [and] obtaining [sic] and utilizing [sic] an additional \$8,000 to \$33,000 each in sponsorship services...."

However, Lyon Park Associates found that, in practice, only \$394,395.50 of the \$1,352,508.07 in SSBCI funds "invested" in the first and second rounds—or 29 percent—were disbursed to portfolio companies in cash. This finding is based on a review of Startup Investments' cash transactions log, and a comparison of individual transactions listed in this log to individual subscription agreements. In every case, the stock purchase price listed in the subscription agreement matched the cash investment listed in the transaction log, so Lyon Park Associates believes that Startup Investments' transaction log provides an accurate record of the entity's use of SSBCI funds. The cash transaction log shows that Startup Investments used \$258,000 in SSBCI funds to purchase stock in the first round of SSBCI-supported investments. (See Appendix C for a list of first round investments; investments included in Lyon Park Associates' audit sample are shown in light green. Note that Startup Investments had no private funds available when these investments were made, as discussed in further detail in the next finding.) The accounting for the second round of SSBCI-supported investments is much more complicated, since cash investments for the second funding round were made out of an account that co-mingled SSBCI and private venture capital funds. In order to determine the true amount of SSBCI funds "used" to make cash investments in the second round, Lyon Park Associates first summed all of Startup Investments' cash investments in the second round (\$208,000) and then multiplied this amount by the share of second round funds attributable to SSBCI (65.57%). (See Appendix D for a list of second round investments; investments included in Lyon Park Associates' audit sample are shown in light green.)

The remaining 71 percent of the funds were used to pay the Betaspring Accelerator's operating expenses. According to Startup Investments' management, the entity determined the total amount of SSBCI funds "invested" by adding the amount of SSBCI funds disbursed to the investee as cash—which was generally a very small amount in the \$10,000 to \$20,000 range—to an estimate of the cost of providing ancillary mentorship services to these investees; Startup Investments calculated this estimate by aggregating all of the Betaspring Accelerator's operating costs for the most recent six-month period and dividing by the number of companies funded.

This appears to be problematic for several reasons. First, as stated above, this practice does not appear to be in keeping with the program description provided in Rhode Island's approved SSBCI application. The program description in the application indicates that each company will receive \$20,000 in cash from SSBCI funds, plus an additional \$22,500 in private seed capital, *plus* additional in-kind services. This statement appears to imply that these in-kind services will be paid for with non-SSBCI funds. While the application did elsewhere indicate, somewhat contradictorily, that a portion of the \$42,500 "will be used to help pay for services including mentorship, legal counsel, incorporation filing, and other legal work necessary to complete the business model," there was no indication to Treasury that these services would be provided by Betaspring staff, or that the funds to pay for these services would never actually pass through the investee. Second, this program design is clearly contrary to Congressional intent. Section 3002, part 12, of the Small Business Jobs Act of 2010, which created the State Small Business Credit Initiative, stipulated that, in order to be eligible for federal funding, an Other Credit Support Program had to "promote private access to credit." Furthermore, the Act limited administrative expenses to five percent of the first one-third of each state's allocation, and three percent of subsequent disbursements. Congress never intended for the program to fund business incubators or any other type of program with significant personnel expenses. Third, the Operating Agreement between SBLFC and Betaspring Fund 100 stated that the managers of Startup Investments would receive fifty percent of the initial shares of the company in exchange for \$10,000 and a donation of in-kind services. Therefore, the managers of Startup Investments are already adequately remunerated; they will have the opportunity to recoup the costs the accelerator is currently incurring at the time companies successfully exit.

In response to this finding, Startup Investments noted that the payment on behalf of portfolio companies for accelerator services is typically treated as "paid-in capital" on these companies' balance sheets, and therefore should be treated as a cash infusion.⁷ In addition, Startup Investments noted that Startup Investments in a separate legal entity from Betaspring Fund 100—which is the actual entity providing the mentorship, legal, and other services. However, Lyon Park Associates believes it is important to note that Startup Investments has no employees, and therefore could not provide such

⁷ Startup Investments did not have in its possession any portfolio company's balance sheet to demonstrate this, but its managers indicated this was typical industry practice.

services. Furthermore, the managers of Startup Investments are the same individuals as the managers of Betaspring Fund 100.

Startup Investments/Betaspring Fund 100 may not be in compliance with Treasury's requirements regarding 20 percent private capital at risk and 1:1 private leverage

Treasury requires that each and every loan or investment made with SSBCI funds have at least 20 percent private capital at risk, and Treasury requires that each Approved State Program (i.e. the Betaspring 100 Fund program as a whole) "can demonstrate that, at a minimum, \$1 of public investment by the State program will cause and result in \$1 of new private credit."

Venture capital programs demonstrate compliance with these requirements in one of two ways. They either a) require one or more private co-investors in each and every transaction, such that the private share of each transaction is at least 20 percent and such that at least 50 percent of capital in the overall portfolio is private at all times or b) require at least 50 percent of capital in a funding round to be private, so that each and every investment made with these pooled funds will automatically comply with the 20 percent private capital at risk and 1:1 private leverage requirements.

The Betaspring portion of Rhode Island's approved SSBCI application acknowledged Treasury's requirements regarding private capital at risk and 1:1 private program leverage and indicated that Betaspring would fully comply with these requirements. The application did not, however, clarify how Betaspring would demonstrate compliance with these requirements.

Since receiving SSBCI funds, Startup Investments has made two rounds of venture capital investments using SSBCI funds. The first set of venture capital investments was made in February and March 2012, shortly after the company received \$1.4 million in SSBCI funds from SBLFC. (See Appendix B for a list of the investments included in the audit sample.) A review of these files indicated that none of these investments were made alongside private co-investors, and the staff of Startup Investments confirmed that the company's policy was not to solicit private co-investors for individual transactions, but rather to pool SSBCI and private non-SSBCI into an account that could be used to make eligible investments.

Lyon Park Associates then reviewed Startup Investments cash transaction log to determine whether there were adequate private capital contributions to the first funding round to ensure that each transaction was fully compliant with the 20 percent private capital at risk requirements, and to ensure the portfolio as a whole was compliant with the 1:1 private leverage requirement. (See Appendix C for a list of all first round investments.) The cash transaction log showed, however, that **at the time each and every one of the SSBCI-funded transactions was made, there were no private funds in the account.** Startup Investments' staff indicated that there had been private capital invested in the first funding round *prior to the receipt of SSBCI funds*, but that all of these private funds had already been spent by the time SSBCI arrived; investments made prior to the receipt of SSBCI funds were funded entirely with

private capital, and investments made after the receipt of SSBCI funds were funded entirely with SSBCI funds.

Startup Investments made a second round of investments in August and September 2012. (See Appendix D for a list of all second round investments.) The amount of cash invested in this round totaled \$208,000, according to Startup Investments' cash transaction log, and Lyon Park Associates verified the accuracy of this figure by comparing selected individual subscription agreements with the cash transaction log. Startup Investments' management indicated that, in this second round of investments, it satisfied the private capital at risk requirement by pooling private limited partners' funds with SSBCI funds, and then making qualified investments out of these pooled funds. Based on Startup Investments' own accounting for SSBCI funds, as documented in the cash transaction log, 65.57 percent of this amount, or \$136,395, is attributable to SSBCI funds.

However, verifying the relative proportions of SSBCI and private funds in each deal turned out to be quite complicated. Unlike most venture capital programs, Startup Investments began making second round investments before all private capital calls had been received, so the level of private funds in the co-mingled account fluctuated each day depending on the timing of individual investment closings, as well as the timing of the receipt of individual capital calls. Lyon Park therefore used Startup Investments' cash transactions log, along with the August and September 2012 statements from the bank account holding the entity's co-mingled SSBCI and private funds, to reconstruct the daily availability of private funds (see Appendix E). Although Startup Investments did their accounting in such a way as to "fund" a large share of their operating expenses out of SSBCI funds, Lyon Park Associates considered each expenditure to represent a reduction in private fund availability, since Lyon Park Associates believes these expenses should have been paid for out of private funds.

Lyon Park Associates then used this reconstructed daily private funds balance to determine whether Startup Investments had sufficient private funds available to make each of these second round investments, at the time the investments were made, assuming that each investment was funded, in equal proportion, by SSBCI and non-SSBCI private funds. (Although Startup Investments' cash transaction log indicates that the entity attributed, on average, 65.57 percent of the funds invested to SSBCI funds, using SSBCI funds in this proportion would violate SSBCI's requirement that the portfolio as a whole maintain 1:1 private leverage at all times.) Based on this analysis (see Appendix F), Lyon Park Associates concluded that Startup Investments had sufficient private capital available to fund ten of the 13 SSBCI-supported second round investments. At the time the remaining investments were made, insufficient private funds remained in the account.

Startup Investments contends that, regardless of the amount of private funds in their account at any given time, all of the investments enrolled in the SSBCI-supported program did indeed have 20 percent capital "at risk," since private investors in the funding round share proportionally in the loss or gain of the portfolio as a whole. It is unclear whether such an interpretation comports with Treasury's current guidance, which appears to have been drafted with the working assumption that a funding round would close prior to the enrollment of SSBCI-supported investments, so that each investment would be funded

out of a fixed pool of funds, such that each and every investment would have the same proportion of private and SSBCI funds.

Startup Investments/Betaspring Fund 100 did not complete the required investor use of proceeds certification at the time the investments were made

Of the 15 transaction files reviewed during the on-site compliance assessment, none contained the required investor use of proceeds certification. In lieu of the *investor* use of proceeds certification, Betaspring had signed the *investee* use of proceeds certification. The language for the investor use of proceeds form and the investee use of proceeds form is completely different. However, upon receipt of Lyon Park Associates' draft compliance assessment, which noted this issue, Startup Investments/Betaspring 100 subsequently executed the required investor use of proceeds certification.

All other required certifications were on file at the time of the on-site compliance assessment.

Startup Investments/Betaspring Fund 100 failed to provide adequate documentation of subsequent private financing

Rhode Island's 2012 SSBCI Annual Report indicated that several of Betaspring's SSBCI-supported investments had attracted subsequent private financing. However, there was no documentation in the files to support this claim. Startup Investments staff provided a copy of Betaspring's reporting to investors as evidence; however, this report did not include any details regarding the source of this subsequent private financing. Startup Investments staff also indicated that their only means of tracking subsequent private financing is to ask investees to self-report; however, they do not require investees to provide any sort of documentation to substantiate self-reported subsequent private financing.

In response to this finding, Startup Investments indicated that it will collect this documentation by the end of 2013.

Startup Investments/Betaspring Fund 100 invested in companies that were not located in the State of Rhode Island

Of the 15 investments reviewed by Lyon Park Associates, only 12 of the companies receiving funds were located in the State of Rhode Island at the time the investment decision was made. Autobike was located in Michigan, and Startup Investment's records even indicated that this company subsequently received SSBCI funding from the State of Michigan. Kay McGowan, Inc., was located in New York City, and Gbooking—which was not reported on Rhode Island's SSBCI Annual Report but was, in fact, funded with SSBCI monies—is located in Israel.

In response to this finding, Startup Investments/Betaspring Fund 100 noted that all of these companies were required to be in Rhode Island during the 12-week accelerator "boot camp." Additionally, Startup Investments/Betaspring Fund 100 stated that Gbooking initially intended to remain in the United States, but subsequently realized that its market was abroad, and Kay McGowan Inc. remained in Rhode Island

following the conclusion of "boot camp." Lyon Park Associates was able to verify that Kay McGowan Inc. is currently headquartered in Rhode Island.

Recommendations

In light of these findings, Lyon Park Associates recommends that SBLFC:

- Immediately contact Treasury to determine a) whether the program can apportion Betaspring Fund 100's operating expenses among portfolio companies, and count each portfolio company's share of these operating expenses as part of the SSBCI "investment" in the company, and b) whether investments made at the time all private funds had already been expended can be considered compliant with Treasury's private capital at risk requirement if private investors bear more than 20 percent of the risk of loss in the portfolio as a whole. SBLFC should clearly state that the first round investments were made after the date of Rhode Island's SSBCI Allocation Agreement but before the date funds were transferred from SBLFC to Startup Investments; in the case of the second round of investments, the funding round remained open while investments were being closed, such that the relative proportion of SSBCI and private funds in the round fluctuated on a nearly daily basis. Following the receipt of Treasury's opinion on these two issues, SBLFC should provide U.S. Treasury with a list of ineligible investments that must be un-enrolled from the Approved State Program.
- Require Startup Investments to obtain sufficient documentation for any subsequent private financing associated with any of the investments that remain enrolled.
- Request that the State of Rhode Island determine whether it is appropriate to terminate the Betaspring Fund 100 Program. If the state does not wish to terminate the program, Lyon Park Associates recommends that (a) Startup Investments be required to maintain a segregated account for SSBCI funds, and to only withdraw funds from this account to fund the federal share of eligible cash investments in Rhode Island-based companies, and (b) SBLFC vet each and every Betaspring Fund 100 investment prior to closing to ensure compliance with all SSBCI eligibility requirements.

Slater Technology Fund

Background

In Annex 1 of Rhode Island's SSBCI Allocation Agreement, Treasury and Rhode Island agreed that the state would use \$9,000,000 of its allocated funds to invest in the Slater Technology Fund, which is administered by the non-profit Slater Fund Inc., so that the fund may make direct equity investments in eligible small businesses. Annex 1 identified Rhode Island's Department of Administration (DOA) as the state agency responsible for the implementation of Rhode Island's Approved State Programs and, as a result, required DOA to apply the provisions included in Articles IV and VI of the SSBCI Allocation Agreement to SBLFC, Slater Fund, Inc., and the Betaspring Fund 100. Articles IV and VI of the SSBCI Allocation Agreement either contain, or include by reference, all SSBCI compliance requirements.

On September 6, 2011, a Memorandum of Understanding (MOU) was signed by the State of Rhode Island, represented by DOA; the Rhode Island Economic Development Corporation (RIEDC), a governmental agency charged with spearheading the state's economic development efforts; and SBLFC, a subsidiary of RIEDC. In this MOU, DOA agreed to transfer all of the state's allocated funds to SBLFC, and SBLFC agreed to accept "full responsibility and accountability for all the requirements, duties, responsibilities and terms set forth in this Agreement, the Allocation Agreement, and the Act." Although this MOU did not strictly comply with Treasury's requirement to apply the provisions of Articles IV and VI to SBLFC, it did bind SBLFC to the requirements contained therein. However, the language in Annex 1 of the SSBCI Allocation Agreement suggests that Treasury intended for DOA—not SBLFC—to directly oversee the activities of the Betaspring Fund 100 and the Slater Technology Fund.

On January 26, 2012, SBLFC and the Slater Technology Fund, Inc. executed a Grant Agreement, which specified that SBLFC would immediately transfer \$1,500,000 to the Slater Technology Fund ("Slater"), with subsequent disbursements of \$3,143,466 and \$4,356,533.40 to be made upon the remittance of the state's second and third tranche, respectively, to SBLFC. Under the Grant Agreement, Slater acknowledged that "the Grants may only be used for investment purposes and may not be used for administrative expenses, management fees or other non-investment expenses." Under the heading "Applicable Laws and Agreements," this agreement included a statement that: "Slater warrants and represents that its activities under this Agreement and all activities conducted by it under the Slater program shall to its knowledge and applying commercially reasonable efforts comply with in all material respects with the Allocation Agreement, the MOU, and all applicable Federal, state, and local government ordinances, laws and requirements including, but not limited to, the Act." The Rhode Island SSBCI Allocation Agreement was attached to the agreement as Exhibit A.

Methodology

Lyon Park Associates reviewed all six venture capital investments made by the Sater Technology Fund using SSBCI funds through December 31, 2012. In conducting this compliance assessment, Lyon Park Associates evaluated each of these investments (see Appendix G for a detailed list of all six investments, including any exceptions noted) to determine compliance with:

- The statutory requirement that the enrolled Other Credit Support Program loan (investment) not exceed \$20 million;
- The statutory requirement that lenders (investors) have “a significant amount of capital at risk,” as further elaborated in the *SSBCI Policy Guidelines*, which defines a “significant amount” as 20 percent of the enrolled loan or investment;
- The statutory requirement that the Approved State Program “can demonstrate that, at a minimum, \$1 of public investment by the State program will cause and result in \$1 of new private credit”;
- The statutory prohibition against the use of funds to make a loan to a “borrower that is a refinancing of a loan previously made to that borrower by the financial institution lender or an affiliate of the financial institution lender,” as further clarified in the *SSBCI Policy Guidelines* and the Frequently Asked Questions (FAQs) pertaining to refinancing;
- The use of proceeds prohibitions contained with the *SSBCI Policy Guidelines*, and reproduced in the borrower use of proceeds certification, that, among other things, prohibit the use of funds to purchase all or part of an ownership interest in the business and prohibit the use of funds for passive real estate investment, as further clarified by the Frequently Asked Questions (FAQs) pertaining to passive real estate investment;
- The program design parameters set forth in Rhode Island’s approved SSBCI application, which are incorporated by reference into the Rhode Island SSBCI Allocation Agreement;
- The requirement to report and document subsequent private financing, in accordance with Annex 7 of the Rhode Island SSBCI Allocation Agreement; and
- The requirement to obtain (a) the borrower use of proceeds certification, (b) the lender (investor) use of proceeds certification, (c) the borrower certification that none of its principals has been convicted of a sex offense against a minor, and (d) the lender (investor) certification that none of its principals has been convicted of a sex offense against a minor.

Findings

One-half of Slater's investments did not comply with Treasury's requirements regarding private capital at risk at the time they were made

Treasury requires that each and every loan or investment made with SSBCI funds have at least 20 percent private capital at risk, and Treasury requires that each Approved State Program (i.e. the Slater program as a whole) "can demonstrate that, at a minimum, \$1 of public investment by the State program will cause and result in \$1 of new private credit."

Venture capital programs demonstrate compliance with these requirements in one of two ways. They either a) require one or more private co-investors in each and every transaction, such that the private share of each transaction is at least 20 percent and such that the private share of the portfolio is at least 50 percent at all times or b) require at least 50 percent of capital in a funding round to be private, so that each and every investment made with these pooled funds would automatically comply with the 20 percent private capital at risk and 1:1 private leverage requirements.

The Slater portion of Rhode Island's approved SSBCI application acknowledged Treasury's requirements regarding private capital at risk and 1:1 private program leverage. The application did not, however, clarify whether Slater would demonstrate compliance by requiring one or more private co-investors with each transaction, or by pooling SSBCI and non-SSBCI private funds and then making investments using these pooled funds.

During Lyon Park Associates' on-site review of Slater's investment files, Lyon Park Associates determined that three of the six investments demonstrated compliance with the private capital at risk requirement. For these three investments (Mnemosyne Pharmaceuticals, Inc., MoFuse, and Illuminoss Medical, Inc.), Slater's investment was structured as a stock purchase as part of a larger funding round, with private co-investors contributing well in excess of 20 percent capital at risk.

A fourth investment, to Vcharge, was structured as a convertible note alongside equity investments by private co-investors, but Lyon Park Associates believes that the Treasury Office of Inspector General may not consider the transaction compliant with the private capital at risk requirements. Slater provided Lyon Park Associates with the following documentation:

- A December 17, 2010, stock purchase agreement with an attached exhibit indicating that Slater had made a \$250,000 investment in Vcharge (using non-SSBCI funds) as part of a \$1,932,000 Series A funding round;
- A June 30, 2012, convertible note from Slater for \$250,000 (using SSBCI funds) that would later allow Slater to convert the loan to Series A stock;
- An undated revised exhibit, which was not attached to any revised stock purchase agreement, showing Slater investment of \$250,000 and total investment of \$2,452,000; and

- An “ownership ledger” showing all Series A investors in Vcharge, as of February 12, 2013, along with the amounts and dates of their investments.

Although the documentation provided did indicate that the vast majority of the Series A funding was from private sources, only \$10,000 of the private financing was invested after Sater issued the \$250,000 convertible note using SSBCI funds on June 30, 2012. The remaining private financing was provided well in advance of this convertible note; \$10,000 was invested on June 1, 2012, with all other financing occurring in February 2012 or earlier. This is admittedly an area with considerable ambiguity; Lyon Park Associates believes that Treasury program staff have not issued any specific guidance regarding the timing of co-investments, and that the Treasury Office of Inspector General has not yet conducted an audit of a venture capital program with funding rounds that remain open for so long. However, Lyon Park Associates believes that the Treasury Office of Inspector General may not consider the Series A investment as a single “transaction” for the purpose of determining whether the individual transaction had 20 percent capital at risk. Treasury does not allow lending programs to count loans that closed more than a few days before the SSBCI-supported loan towards private capital at risk. In addition, the 1:1 private leverage requirement is based on a requirement in the Act that the Approved State Program “can demonstrate that, at a minimum, \$1 of public investment by the State program will **cause** and **result** [emphasis added] in \$1 of new private credit.” For private capital to count towards the 1:1 private leverage requirement, therefore, one must be able to firmly establish a nexus between the public investment and the private investment; it is difficult to demonstrate such a nexus if the private investment occurred first and therefore did not serve as an kind of inducement for private investors to participate. It is less clear whether private capital used to demonstrate compliance with the 20 percent capital at risk requirement must also demonstrate that it was caused by, or resulted from, the public investment.

In response to this finding, Sater indicated that, while its SSBCI-supported investment did not occur until June, it had made the funding commitment much earlier. To support this claim, Sater provided a copy of its Investment Committee’s April 9, 2012, meeting minutes approving the investment. However, as noted above, this approval occurred after all but \$20,000 in private funds had been committed.

A fifth investment, to Lucidux, did not have any private co-investors. This investment was made solely with SSBCI funds in direct contravention of SSBCI requirements. During the on-site assessment and in subsequent conversations, Sater management indicated that Sater intended to transfer funds from its “recovery account”—which holds the income Sater has made from successful exits—to its SSBCI funds account in an amount equal to at least 20 percent of this investment. In this manner, Sater believed it would be retroactively compliant with the 20 percent capital at risk requirement. It is not clear, however, whether Treasury will consider recovery account funds to be “private,” since they are from income earned as a result of state-funded operations, or whether Treasury will consider this investment eligible if it was non-compliant at the time the transaction was made.

Lyon Park Associates reviewed the monthly statements of Sater’s recovery funds account and determined that, at the time the Lucidux investment was made, there were sufficient funds in the

recovery account to fund 20 percent of more of this transaction. Furthermore, on July 12, 2013, following the receipt of Lyon Park Associates' draft compliance assessment, Slater transferred \$50,000 (or 20 percent of its \$250,000 investment in Lucidux) from its recovery account to its SSBCI funds account in order to retroactively comply with the private capital at risk requirement. Therefore, Lyon Park Associates believes Slater can make a relatively good case that it made an accounting mistake, which was subsequently rectified through a transfer of funds from the recovery account to the SSBCI funds account.

The sixth and last investment that Lyon Park Associates reviewed, to VoltServer, did not have any private investors. This transaction was funded solely by Slater, in two tranches ***pursuant to two separate promissory notes***, such that the initial June 22, 2012, payment of \$100,000 was made solely with SSBCI funds, and the subsequent October 31, 2012, payment of \$150,000 was paid out of Slater's operating account. While 60 percent of the combined \$250,000 investment was made with Slater's non-SSBCI funds, the source of the operating account funds is unclear, and therefore these funds may not be "private." In addition, Lyon Park Associates believes that Treasury may interpret this investment to be comprised of two separate transactions; if this is the case, the first transaction did not have 20 percent private capital at risk at the time the investment was made.

On July 12, 2013, Slater transferred \$70,000 from its SSBCI account and \$80,000 from its recovery account to its operating account, in order to "reimburse" its operating account for the second payment to VoltServer. While it appears that Slater did so in order to ensure that "private" recovery account funds were retroactively part of this transaction, this transfer did not address the inadequate private capital at risk in the first disbursement to VoltServer. It is also unclear whether Treasury guidelines permit program managers to increase the amount of SSBCI support for a transaction ***after a transaction is enrolled***; this transfer, in effect, increased the amount of SSBCI support for the combined \$250,000 transaction from \$100,000 to \$170,000.

Slater improperly used SSBCI funds to make two investments that were not enrolled in the SSBCI program

In the course of reviewing Slater's reconciliation of its operating, recovery, and SSBCI accounts, and the transfers that occurred as a result of Lyon Park Associates' preliminary findings, Lyon Park Associates discovered that Slater made two investments using SSBCI funds that were not included in Rhode Island's 2012 SSBCI Annual Report. These investments did not appear on the investment list provided to Lyon Park Associates prior to the on-site compliance assessment, and do not appear to have ever been enrolled in the program. Therefore, Lyon Park Associates has determined that Slater improperly used funds from its SSBCI account to make a \$250,000 investment in ProThera Biologics on August 28, 2013, and a \$10,000 investment in Enhanced Energy Group on November 16, 2012.

On July 12, 2013, Slater transferred \$260,000 from its operating account to its SSBCI account in order to reimburse the SSBCI account for these two SSBCI-ineligible investments.

Sater did not complete the required investor sex offender certification at the time the investments were made

Treasury requires that the following be obtained for each transaction: (a) the borrower use of proceeds certification, (b) the lender (investor) use of proceeds certification, and (c) the borrower certification that none of its principals has been convicted of a sex offense against a minor. Treasury also requires that either: (a) each transaction file contain a newly executed lender (investor) certification that none of its principals has been convicted of a sex offense against a minor or (b) the state (or its designated administering entity) obtain a one-time lender (investor) sex offender certification and execute a written agreement with the lender or investor (which may be part of a larger lender, or investor, participation agreement) that creates a positive requirement to notify the Participating State if and when an event occurs that renders the prior certifications obsolete.

Of the six transaction files reviewed during the on-site compliance assessment, none contained the required investor sex offender certification. Although Sater provided a copy of a one-time investor sex offender certification that it believed covered all of its investments, the grant agreement executed by SBLFC and Sater did not contain the required positive requirement to notify the Participating State if and when an event occurs that renders the prior certifications obsolete. Therefore, Sater was not compliant with the investor sex offender certification requirement as of April 2013, when the on-site compliance assessment was conducted.

However, upon receipt of Lyon Park Associates' draft compliance assessment, which noted this issue, Sater subsequently executed the required investor use of proceeds certification.

All other required certifications were on file at the time of the on-site compliance assessment.

Recommendations

In light of these findings, Lyon Park Associates recommends that SBLFC:

- Request guidance from Treasury regarding whether private funds committed to a company prior to an SSBCI-supported investment may be counted as private investment for the purpose of determining whether the investment complies with Treasury's private capital at risk requirement. If Treasury responds in the negative, un-enroll the Vcharge investment from the Approved State Program following Treasury's newly adopted procedures.
- Provide Treasury with an explanation of the private capital at risk issues identified in the course of this compliance assessment, as well as a cover memorandum from Sater describing the reconciling transactions that were made.
- Require Sater to immediately begin completing a compliance checklist prior to each SSBCI-funded investment closing. This compliance checklist would require Sater to describe, in detail, the way in which it is satisfying the 20 percent capital at risk requirement and 1:1 private

leverage requirement. If Slater indicates that there are private co-investors, it should attach a copy of a stock purchase agreement indicating simultaneous investment by private investors. If Slater is the only investor, Slater should attach documentation that demonstrates that sufficient funds were transferred from its recovery funds account to its SSBCI funds account immediately prior to its investment in the firm. The compliance checklist should also require Slater to attach all four certifications. Lyon Park Associates recommends that Slater be required to send this checklist, and the accompanying documentation, to SBLFC for approval prior to making the investment.

- Request that Slater's attorney render a legal opinion whether the recovery account funds are "private funds." If Slater's attorney cannot or will not furnish such an opinion, Slater should immediately cease making SSBCI-supported investments without private co-investors.

Administrative Expenses⁸

Lyon Park Associates reviewed a judgmental sample of 3 direct administrative expenses charged against the SSBCI award by SBLFC. (See Appendix H.) In conducting this compliance assessment, Lyon Park Associates evaluated each transaction against four criteria:

- **Allowability.** OMB Circular A-87 sets forth a lengthy list of the factors affecting the allowability of costs. Chief among these are the stipulation that the costs "be necessary and reasonable for the proper and efficient performance and administration of Federal awards" and "conform to any limitations or exclusions set forth in these principles, Federal laws, terms and conditions of the Federal Award, or other governing regulations as to types or amounts of cost items." The latter stipulation encompasses the limitations and exclusions set forth in Attachment B of the circular, "Selected Items of Cost," which provides further details regarding the allowability of specific cost categories. Although the list of allowability factors also encompasses allocability, reasonability, and the adequacy of documentation, Lyon Park Associates considered these as separate criteria for the purposes of this compliance assessment. Therefore, Lyon Park Associates considered an administrative expense as allowable if it (a) was necessary for the

⁸ Section 4.2 of Rhode Island's *SSBCI Allocation Agreement* requires the state to pay allowable costs in accordance with the cost principles set forth in *OMB Circular A-87 (Cost Principles for State, Local, and Indian Tribal Governments)*. Section 3(b) of *OMB Circular A-87's* Attachment A states: "All sub awards are subject to those Federal cost principles applicable to the particular organization concerned. Thus, [...] if a sub award is to some other non-profit organization, *Circular A-122, "Cost Principles for Non Profit Organizations"* shall apply." Although SBLFC is a non-profit organization and would generally be held to the standards of *Circular A-122* rather than *Circular A-87*, Annex 1 of Rhode Island's *SSBCI Allocation Agreement* is written in such a way as to imply that DOA should hold SBLFC to the standards of *Circular A-87*. For this reason, the compliance assessment focused on SBLFC's adherence to the cost principles set forth in *Circular A-87* rather than *Circular A-122*. That said, these circulars contain quite similar requirements.

proper performance and administration of the SSBCI award and (b) was not in a cost category specifically excluded by Attachment B of OMB Circular A-87.

- **Allocability.** OMB Circular A-87 states that “a cost is allocable to a particular cost objective”—in this case, the SSBCI award—“if the goods or services involved are chargeable or assignable to such cost objective in accordance with the relative benefits received.” In determining whether a cost was allocable to the SSBCI award, Lyon Park Associates determined (a) whether the expense funded a good or service that directly and solely benefitted Rhode Island’s SSBCI programs and (b) whether the written documentation provided was adequate to support such a determination.
- **Reasonability.** OMB Circular A-87 states that “a cost is reasonable if, in its nature and amount, it does not exceed that which would be incurred by a prudent person under the circumstances prevailing at the time the decision was made to incur the cost.” Among other factors, OMB Circular A-87 directs agencies to consider sound business practices and market prices for comparable goods and services. Lyon Park Associates primarily relied on these factors when determining the reasonability of a particular administrative expense.
- **Adequate documentation.** OMB Circular A-87 does not provide any general guidance regarding what constitutes “adequate” documentation. However, Attachment B of the circular does provide guidance regarding particular documentation for selected cost categories. Lyon Park Associates evaluated the documentation provided in light of any documentation requirements specific to that particular cost category, if any; if Attachment B did not specify any particular documentation requirements for a given cost category, Lyon Park Associates followed best practice and compared the amount recorded with standard supporting documentation such as receipts, invoices, credit card statements, requisition requests, and internal authorization memoranda. When determining whether an expense was adequately documented, Lyon Park Associates considered only whether the amount charged could be substantiated.

Of the three direct administrative expenses reviewed, Lyon Park Associates determined that all three were allowable, allocable to the SSBCI award, reasonable, and adequately documented.

Appendix A: Loans Enrolled in the Rhode Island Small Business Loan Fund Program

Lender Name	Closing Date	Borrower	Business Name	Private Financing	SSBCI Loan Amount	Primary Business Activity	Use of SSBCI Funds	Borrower Use of Proceeds Certification	Borrower Sex Offender Certification	Lender Use of Proceeds Certification	Lender Sex Offender Certification
Bank Newport	12/8/2011	Kelly Gemma LLC d/b/a Ocean State Psychotherapy	Ocean State Psychotherapy	\$350K of Newport Bank financing for purchase of business, \$125K loan and \$87.5K SBA loan to Gemma Realty Investment LLC	\$50,000	psychotherapy	"working capital to ensure a smooth financial transition from current ownership to new ownership"	yes	yes	yes	yes
Webster Bank	2/14/2012	NMC Acquisition Corp.	National Marker Company	Webster Bank \$500K LOC (assumption of \$0 balance prior LOC), \$350K equipment purchase line (assumption of \$0 balance prior LOC), \$600K equipment SBA 504; OSBDA \$480K equipment 504; BDCRI \$1.5M; seller note \$500K; equity \$350K;	\$250,000	manufacturer of safety identification markers	working capital	yes	yes	yes	yes



Appendix B: Audit Sample: Betaspring Fund 100 Program

Investee	Investee location	Date of investment	Cash investment	Non-cash investment (in-kind services) as reported by Betaspring	Total Amount	Good or service produced by business	Investee use of proceeds cert?	Investee sex offender cert?	Investor use of proceeds cert?	Investor sex offender cert?	If subsequent private financing was listed on the annual report, is it properly documented?	Other issues/ comments
Agile QR (listed as 121Nexus on SSBCI Annual Report)	RI	2/7/2012	\$14,000.00	\$34,102.72	\$ 48,102.72	Digital media	Yes, but not dated	Yes, but not dated	Yes, but provided after draft compliance assessment	Yes, but not dated	N/A	
Kay McGowan, Inc. (listed as ACuratedWorld on SSBCI Annual Report)	NY	2/22/2012	\$10,000.00	\$34,102.72	\$ 44,102.72	Online sales of handicrafts	Yes, but not dated	Yes, but not dated	Yes, but provided after draft compliance assessment	Yes, but not dated	N/A	
AutoBike	MI (even received loan from MI)	8/28/2012	\$16,000.00	\$44,384.62	\$ 60,384.62	Bicycles	Yes	Yes	Yes, but provided after draft compliance assessment	Yes	Also reported in Betaspring Fund 100 Investor Update Feb. 2013; Betaspring did not receive substantiating documentation other than email from investee	



Investee	Investee location	Date of investment	Cash investment	Non-cash investment (in-kind services) as reported by Betaspring	Total Amount	Good or service produced by business	Investee use of proceeds cert?	Investee sex offender cert?	Investor use of proceeds cert?	Investor sex offender cert?	If subsequent private financing was listed on the annual report, is it properly documented?	Other issues/ comments
Autoshag	RI	3/8/2012	\$ 10,000.00	\$34,102.72	\$ 44,102.72	Web-based purchasing platform for used cars	Yes	Yes	Yes, but provided after draft compliance assessment	Yes	N/A	
Consano (listed in SSBCI Annual Report as CareThread)	RI	2/10/2012	\$20,000.00	\$34,102.72	\$ 54,102.72	Web solutions for hospital teams Web platform for searching and comparing consumer services	Yes	Yes	Yes, but provided after draft compliance assessment	Yes	Also reported in Betaspring Fund 100 Investor Update Feb. 2013; Betaspring did not receive substantiating documentation other than email from investee	Investor Report indicates company changed name from Consano to CareThread
Gbooking	Israel	2/22/2012	\$20,000.00	\$34,102.72	\$ 54,102.72	Online learning solutions	Yes	Yes	Yes, but provided after draft compliance assessment	Yes	N/A	Not listed on Annual Report at all
LessonWriter	RI	NOT DATED	\$20,000.00	\$34,102.72	\$ 54,102.72		Yes	Yes	Yes, but provided after draft compliance assessment	Yes	N/A	



Investee	Investee location	Date of investment	Cash investment	Non-cash investment (in-kind services) as reported by Betaspring	Total Amount	Good or service produced by business	Investee use of proceeds cert?	Investee sex offender cert?	Investor use of proceeds cert?	Investor sex offender cert?	If subsequent private financing was listed on the annual report, is it properly documented?	Other issues/ comments
Mercury Print and Mail Co. (listed in SSBCI Annual Report as MarketHound; Betaspring is in the process of executing new documents with MarketHound name; MarketHound is subsidiary)	RI	2/13/2012	\$20,000.00	\$34,102.72	\$54,102.72	Marketing program management tool	Yes	Yes	Yes, but provided after draft compliance assessment	Yes	N/a	Spin-out of another business; manager of Betaspring was formerly board member of company; subscription agreement is Mercury Print and Mail (parent company)
MoveableCode	RI	2/9/2012	\$20,000.00	\$34,102.72	\$54,102.72	Mobile entertainment	Yes	Yes	Yes, but provided after draft compliance assessment	Yes	Also reported in Betaspring Fund 100 Investor Update Feb. 2013; Betaspring did not receive substantiating documentation other than email from investee	



Investee	Investee location	Date of investment	Cash investment	Non-cash investment (in-kind services) as reported by Betaspring	Total Amount	Good or service produced by business	Investee use of proceeds cert?	Investee sex offender cert?	Investor use of proceeds cert?	Investor sex offender cert?	If subsequent private financing was listed on the annual report, is it properly documented?	Other issues/ comments
Pennant	RI	8/16/2012	\$12,000.00	\$44,384.62	\$ 56,384.62	Ad creation tool	Yes	Yes	Yes, but provided after draft compliance assessment	Yes	N/A	
Prepmatic	RI	2/23/2012	\$14,000.00	\$34,102.72	\$ 48,102.72	Exam prep tool	Yes	Yes	Yes, but provided after draft compliance assessment	Yes	Also reported in Betaspring Fund 100 Investor Update Feb. 2013; Betaspring did not receive substantiating documentation other than email from investee	
Recoverd	RI	2/22/2012	\$14,000.00	\$34,102.72	\$ 48,102.72	Purchasing platform for colleges/universities	Yes	Yes	Yes, but provided after draft compliance assessment	Yes	N/A	
Splitwise	RI	2/22/2012	\$20,000.00	\$34,102.72	\$ 54,102.72	Web-based tools to fairly split bills	Yes	Yes	Yes, but provided after draft compliance assessment	Yes	Also reported in Betaspring Fund 100 Investor Update Feb. 2013; Betaspring did not receive substantiating documentation other than email from investee	



Investee	Investee location	Date of investment	Cash investment	Non-cash investment (in-kind services) as reported by Betaspring	Total Amount	Good or service produced by business	Investee use of proceeds cert?	Investee sex offender cert?	Investor use of proceeds cert?	Investor sex offender cert?	if subsequent private financing was listed on the annual report, is it properly documented?	Other issues/ comments
Sproutel	RI	2/23/2012	\$14,000.00	\$34,102.72	\$ 48,102.72	Toys that teach compliant behaviors to chronically ill children	Yes	Yes	Yes, but provided after draft compliance assessment	Yes	Also reported in Betaspring Fund 100 Investor Update Feb. 2013; Betaspring did not receive substantiating documentation other than email from investee	
WorldBrain	RI	9/13/2012	\$16,000.00	\$44,384.62	\$ 60,384.62	Web platform	Yes	Yes	Yes, but provided after draft compliance assessment	Yes	N/A	



Appendix C: Startup Investments' (Betaspriing Fund 100's) First Round Investments

Date	Investee	Cash investment-- SSBCI funds	"Services" investment--SSBCI funds
2/7/2012	121Nexus (Agile)	\$14,000.00	\$34,102.72
2/9/2012	MoveableCode	\$20,000.00	\$34,102.72
2/10/2012	CareThread (Consano)	\$20,000.00	\$34,102.72
2/13/2012	Markethound	\$20,000.00	\$34,102.72
2/17/2012	Socialping	\$15,000.00	\$34,102.72
2/22/2012	Recovend	\$14,000.00	\$34,102.72
2/22/2012	Splitwise	\$20,000.00	\$34,102.72
2/22/2012	A Curated World (Kay McGowan)	\$10,000.00	\$34,102.72
2/22/2012	GBooking	\$20,000.00	\$34,102.72
2/23/2012	Prepmatic	\$14,000.00	\$34,102.72
2/23/2012	Sproutel	\$14,000.00	\$34,102.72
2/23/2012	Thryve	\$14,000.00	\$34,102.72
2/23/2012	ThumbsUp	\$14,000.00	\$34,102.72
2/28/2012	LessonWriter	\$20,000.00	\$34,102.72
3/1/2012	JumpOffCampus	\$14,000.00	\$34,102.72
3/1/2012	Moveable Code	\$5,000.00	\$34,102.72
3/8/2012	Autoshag	\$10,000.00	\$34,102.72
		\$258,000.00	\$579,746.22



Appendix D: Startup Investments' (Betaspriing Fund 100's) Second Round Investments

Investment date	Investee	Total cash investment	Services "investment"	Total "investment"	SSBCI dollars	Private dollars	Total dollars
8/14/2012	Rentul	\$12,000.00	\$44,384.62	\$56,384.62	\$36,973.47	\$19,411.15	\$56,384.62
8/16/2012	Pennant	\$12,000.00	\$44,384.62	\$56,384.62	\$36,973.47	\$19,411.15	\$56,384.62
8/28/2012	AutoBike	\$16,000.00	\$44,384.62	\$60,384.62	\$39,597.17	\$20,787.44	\$60,384.62
8/28/2012	Rootless	\$20,000.00	\$44,384.62	\$64,384.62	\$42,220.17	\$22,164.44	\$64,384.62
8/28/2012	Scholfly	\$20,000.00	\$44,384.62	\$64,384.62	\$42,220.17	\$22,164.44	\$64,384.62
8/29/2012	TennisHub	\$12,000.00	\$44,384.62	\$56,384.62	\$36,974.18	\$19,410.44	\$56,384.62
8/30/2012	iOrganics	\$20,000.00	\$44,384.62	\$64,384.62	\$42,220.17	\$22,164.44	\$64,384.62
8/31/2012	HealthID Profile	\$16,000.00	\$44,384.62	\$60,384.62	\$39,597.17	\$20,787.44	\$60,384.62
9/1/2012	Umbie Health	\$16,000.00	\$44,384.62	\$60,384.62	\$39,597.17	\$20,787.44	\$60,384.62
9/5/2012	TouchVu	\$12,000.00	\$44,384.62	\$56,384.62	\$36,974.18	\$19,410.44	\$56,384.62
9/6/2012	Crunchbutton	\$20,000.00	\$44,384.62	\$64,384.62	\$42,220.17	\$22,164.44	\$64,384.62
9/13/2012	WorldBrain	\$16,000.00	\$44,384.62	\$60,384.62	\$39,597.17	\$20,787.44	\$60,384.62
9/22/2012	Kuratur	\$16,000.00	\$44,384.62	\$60,384.62	\$39,597.17	\$20,787.44	\$60,384.62
		\$208,000.00	\$577,000.00	\$785,000.00	\$514,761.86	\$270,238.14	\$785,000.00

2nd round--Proportion of funding from SSBCI	65.57%
2nd round--Total "cash" investment	\$208,000.00
2nd round--"Cash" investment from SSBCI funds	\$136,395.50
Plus first round SSBCI cash investment	\$258,000.00
Total SSBCI cash investment	\$394,395.50



Appendix E: Movement of Private Funds In and Out of Startup Investments' (Betaspriing Fund 100's) Co-mingled SSBICI and Private Funds Account

Date	Event	Addition to private funds available	Reduction in private funds available	Net balance of private funds (excludes investment closings)
5/18/2012	Receipt of funds from Collette Travel Service	\$50,000.00		\$50,000.00
5/18/2012	Bank service fee		-\$15.00	\$49,985.00
5/29/2012	Receipt of funds from Mike Lapsley	\$7,500.00		\$57,485.00
5/29/2012	Bank service fee		-\$15.00	\$57,470.00
6/1/2012	Organizational expense		-\$250.00	\$57,220.00
6/11/2012	Services payment		\$50,000.00	\$7,220.00
6/12/2012	Organizational expenses		-\$2,164.00	\$5,056.00
6/21/2012	Bank service fee		-\$15.00	\$5,041.00
6/21/2012	Organizational expenses		\$40,020.20	-\$34,979.20
6/21/2012	Receipt of funds from Angus Davis Ocean State Opportunities Fund LP	\$18,750.00		-\$16,229.20
6/28/2012	Receipt of funds from Cherrystone Beta LLC <i>(note: accountant's log shows a total of \$58,800, but amount on investor list only total \$54,900)</i>	\$54,900.00		\$38,670.80
6/28/2012	Receipt of funds from EA Investors LLC	\$25,500.00		\$64,170.80
6/28/2012	Organizational expenses		-\$256.25	\$63,914.55



Date	Event	Addition to private funds available	Reduction in private funds available	Net balance of private funds (excludes investment closings)
7/26/2012	Services payment		\$50,000.00	\$13,914.55
8/7/2012	Receipt of funds from Coryndon Luxmore	\$4,500.00		\$18,414.55
8/7/2012	Receipt of funds from Angel Street Capital	\$15,000.00		\$33,414.55
8/9/2012	Services payment		\$50,000.00	-\$16,585.45
8/14/2012	Receipt of funds from Paul G. Arpin Estate	\$140,000.00		\$123,414.55
8/20/2012	Wire fee		-\$15.00	\$123,399.55
8/23/2012	Services payment		\$50,000.00	\$73,399.55
9/6/2012	Services payment		\$50,000.00	\$23,399.55
9/14/2012	In branch withdrawal		-\$4,000.00	\$19,399.55
9/27/2012	Services payment		\$100,000.00	-\$80,600.45

Note: Betaspring's August bank statement showed an additional withdrawal of \$204,000 on 8/21/2012 that is not listed above. This payment, coded "debit memo," was a lump sum withdrawal for the cash payments to investees, according to Betaspring. Because the availability of funds calculation lists each payment to investees separately, to avoid double counting, this payment is not included here.



Appendix F: Availability of Private Funds for Second Round Investments, Assuming 50% Private Share in Each Investment

Investment date	Total private funds available	Investee	Total cash investment	Required 50% private share
8/14/2012	\$ 123,414.55	Rentul	\$12,000.00	\$6,000.00
8/16/2012	\$ 117,414.55	Pennant	\$12,000.00	\$6,000.00
8/28/2012	\$61,399.55	AutoBike	\$16,000.00	\$8,000.00
8/28/2012	\$53,399.55	Rootless	\$20,000.00	\$10,000.00
8/28/2012	\$43,399.55	Scholarly	\$20,000.00	\$10,000.00
8/29/2012	\$33,399.55	TennisHub	\$12,000.00	\$6,000.00
8/30/2012	\$27,399.55	iOrganics	\$20,000.00	\$10,000.00
8/31/2012	\$17,399.55	HealthID Profile	\$16,000.00	\$8,000.00
9/1/2012	\$9,399.55	Umbie Health	\$16,000.00	\$8,000.00
9/5/2012	\$1,399.55	TouchVu	\$12,000.00	\$6,000.00
9/6/2012		Crunchbutton	\$20,000.00	\$10,000.00
9/13/2012		WorldBrain	\$16,000.00	\$8,000.00
9/22/2012		Kuratur	\$16,000.00	\$8,000.00
			\$208,000.00	



Appendix G: SSBCI-supported Slater Technology Fund Investments, through December 31, 2012

Investee Name	Date of investment	Was Slater the sole investor?	SSBCI investment	Private amount from co-investors	20% capital at risk?	Investee use of proceeds cert?	Investee sex offender cert?	Investor use of proceeds cert?	Investor sex offender cert?	If subsequent private financing was listed on the annual report, is it properly documented?	Other issues/ comments
Mnemosyne Pharmaceuticals, Inc.	2/1/2012	No	\$500,000.00	\$ 2,000,000.00	yes	yes	yes	yes	yes--blanket cert for all investments; BUT no clause in MOU	N/A	Certs signed in January and February 2013; Schedule of Purchasers shows AccessBridgeGap LLC purchasing 3,898,641 shares @ 51.3 cents/share and Slater purchasing 974,660 shares; amounts to \$2M private, \$500K Slater (SSBCI) Structured as a \$130,000 convertible note; promissory note states "the note is one of several Convertible Promissory Notes with an aggregate principal amount of up to \$750,000, issued by the Borrower pursuant to a Note Purchase Agreement dated March 30, 2012..."; Exhibit A to purchase agreement contains list of other investors
MoFuse	6/22/2012	No	\$130,000.00	\$ 393,013.00	yes	yes	yes	yes	yes--blanket cert for all investments; BUT no clause in MOU	N/A	



Investee Name	Date of investment	Was Slater the sole investor?	SSBCI investment	Private amount from co-investors	20% capital at risk?	Investee use of proceeds cert?	Investee sex offender cert?	Investor use of proceeds cert?	Investor sex offender cert?	If subsequent private financing was listed on the annual report, is it properly documented?	Other issues/ comments
Lucidux	6/30/2012	Yes	\$250,000.00	\$	Not at the time investment was made	yes	yes	yes	yes	N/A	Structured as \$250,000 promissory note--\$100K up front, plus three \$50K milestone payments (all paid); 100% paid from Slater Administrative account, although sufficient funds were in Recovery account at the time
VoltServer	10/31/2012	Yes	\$250,000.00	\$	Not at the time the investment was made	yes	yes	yes	yes	yes	Structured as \$150,000 promissory note; there is an earlier 06/29/2012 promissory note in the file for \$100,000; 100% paid from Slater Administrative account, although sufficient funds were in Recovery account at the time



Investee Name	Date of investment	Was Slater the sole investor?	SSBCI investment	Private amount from co-investors	20% capital at risk?	Investee use of proceeds cert?	Investee sex offender cert?	Investor use of proceeds cert?	Investor sex offender cert?	If subsequent private financing was listed on the annual report, is it properly documented?	Other issues/ comments
Vcharge	6/30/2012	No	\$250,000.00	\$ 10,000.00	Unclear— timing issue	yes	yes	yes	yes	N/A	Other issues/ comments Structured as a \$250,000 convertible promissory note, shares will convert at \$1/share; ownership ledger shows only attracted \$10,000 in private Series A investment after convertible note issued
Illuminoss Medical, Inc.	9/26/2012	No	\$500,000.00	\$13,500,000.00	yes	yes	yes	yes	yes	yes	Structured as Series C1 Preferred Stock Purchase; \$0.3834 per share--SSBCI initial closing of \$250K, milestone closing of \$250K



Appendix H: Representative Sample of Administrative Expenses Charged by SBLFC against the SSBCI Award

Date	Payee	Description	Amount	Description of documentation provided	Documented (i.e. receipt or invoice substantiates amount)?	Allowable?	Allocable?	Reasonable?	Suggested action
1/31/2012	Moses & Afonso Ltd	legal service	\$ 4,756.00	Copy of check, copy of law firm bill	Yes	yes	yes	yes	none
1/31/2012	Partridge Snow & Hahn LTD	Yes	\$20,616.50	Copy of check, copy of law firm bill	Yes	yes	yes	yes	none
10/31/2012	Betaspring	Reimbursement to Owen Johnson for costs incurred in his travel to the SSBCI Conference Oct 1-2	\$ 1,276.50	Copy of check to Betaspring; copy of hotel, airfare, taxi, and restaurant receipts	Yes	yes	yes	yes	none

