Appalachian Angel Capital Fund Formation RFP

Formation of New Angel Capital Funds in Appalachia

Open Date:	April 23, 2012
Webinar Dates:	May 14, 2012 May 15, 2012
Proposal Due Date:	June 15, 2012
Announcement Date:	July 13, 2012

Award: Two types of awards are available:

I. Technical assistance will be provided by RAIN Source Capital to local entities to support new angel fund formation or to improve the performance of an existing angel fund/network. Up to four applicants will be selected for this support.
II. Direct grant support will be provided to qualified local organizations to support the formation of a new angel fund. Up to $30,000 of direct grant support will be provided to one qualified applicant in this round.

Summary
ARC has contracted with RAIN Source Capital to provide technical assistance to selected entities that demonstrate the ability to convene a group of angel investors[1] in their area to form new angel capital funds in Appalachia. To be successful, entities will need to demonstrate their ability to:

- convene a group of angel investors who have the interest, the risk tolerance, and the appetite to invest in local and regional early-stage companies;
- partner with organizations who can generate a flow of deals with appropriate growth potential that would be attractive to a group of angel investors.
- identify the capacity, either internally or through partner organizations, to support the due diligence, monitoring of portfolio companies, and provision of ongoing angel fund administrative support.

To assist applicants with their response to this RFP, ARC and RAIN Source Capital will host webinars that will outline the key elements of the application and outline the angel fund creation process and the ongoing support needed (see the section "Angel Fund Formation Workplan" on page 7).

Selected applicants are anticipated to raise over $1 million each in local investment capital for early-stage and/or expanding companies. Upon formation of a fund, the angel investors typically self-finance the fund's ongoing activities, and, if appropriate, provide reimbursement of start-up support, enabling continued support for other entities to form new additional angel funds in Appalachia.

BACKGROUND

Appalachian Regional Commission

The Appalachian Regional Commission (ARC) is a federal-state partnership established in 1965 by the Appalachian Regional Development Act to promote economic and community development of the Appalachian Region. The Act, as amended in 2008, defines the Region as 420 counties comprising all of West Virginia and

[1] Angel investors for this purpose must meet the "Accredited Investor" standards as defined by the U.S. Securities and Exchange Commission: http://www.sec.gov/rules/final/2011/33-9287.pdf

parts of Alabama, Georgia, Kentucky, Maryland, Mississippi, New York, North Carolina, Ohio, Pennsylvania, South Carolina, Tennessee, and Virginia—an area of 205,000 square miles and about 25 million people. To promote local planning and implementation of ARC initiatives, the Commission works with 73 local development districts (LDDs) comprising groups of counties within each of the 13 states. The Commission has 14 members: the governors of the 13 Appalachian states and a federal co-chair, who is appointed by the president.

For almost 50 years, the Commission has assisted a wide range of programs in the Region, including highway corridors; community water and sewer facilities, telecommunication, and other physical infrastructure; health, education, and human resource development; economic development programs; local capacity building; and leadership development.

ARC Capital Policy Initiative

ARC has determined that access to capital and credit is one of the major factors limiting business creation, expansion, and growth in the Appalachian Region. This has been an historic problem in the Region relative to many other parts of the country. ARC studies done in 1998 by Mt. Auburn Associates and in 2007 by the National Community Reinvestment Coalition found that:

- There was a significant gap in the availability of equity capital relative to other areas of the country. For example, just 1.3% of professionally managed venture capital is invested in Appalachia annually.[2]
- Established small businesses in the Region—and particularly small firms with fewer than 10 employees—had insufficient financing to expand. For example, lenders using the SBA 7a program made 15% fewer loans in Appalachia as compared to the nation, while 7a loans in ARC-designated economically distressed counties were just one-third the national average.[3]
- Non-metropolitan and distressed counties had considerably smaller shares of bank assets, which resulted in these communities receiving less community development financing.
- Of the $26 billion in New Markets Tax Credit allocations provided to low-income communities across the nation, just $290 million in allocations (1.1%) went to 11 funds located in Appalachia (4.4% of all funds capitalized nationwide). Appalachia made up about 8% of the U.S. population in 2009, while 45% of Appalachia by geography is eligible to participate in the New Markets program.[4]

These challenges have only been intensified by the severe recession and by longer-term trends that have been increasingly driving economic activity and population into larger metropolitan areas. In addition, Appalachia and other rural regions have also been hurt by the ongoing consolidation and related changes taking place in the banking industry. Larger banks have been consolidating in major cities and urban regions, and there are fewer community banks, particularly in smaller towns and rural areas. These trends have been building for many years but have been accelerated by the current economic downturn. This is particularly noteworthy as the presence of banks, bank branches, and bank capital positively correlates with increased business lending in rural Appalachian communities (National Community Reinvestment Coalition study, 2007).

To address these challenges, in 2010 ARC convened an Appalachian Capital Policy Initiative Advisory Committee comprising representatives from banks, development lenders, state government, venture funds, and federal financial regulators. This advisory group has provided oversight and direction for the development of strategic options to address the Region's capital and credit challenges.

The Appalachian Capital Policy Initiative has four objectives:

1. To expand bank lending for business expansion and growth;
2. To attract new sources of equity investment into the Region from private corporations, pension funds, national financial institutions, philanthropic institutions, and intermediaries;
3. To build the capacity of development loan funds (community development financial institutions, or CDFIs) and other providers of capital to expand into underserved communities;

[2] National Venture Capital Association, PricewaterhouseCoopers/Money Tree Report, 2011.
[3] U.S. Small Business Administration, 2003.
[4] U.S. Department of the Treasury, CDFI Fund, CIIS data, September 2011.

4. To increase the volume and quality of deal flow and financeable transactions by strengthening the entrepreneurial ecosystem.

To accomplish these objectives, ARC has developed a multi-faceted strategy that seeks to: influence policy; educate key constituencies and enlist their support and participation; develop and expand programs that deliver capital to business; and attract new sources of capital to the Region. A number of programmatic efforts are currently under way through the Appalachian Capital Policy Initiative, including the development and expansion of angel investment funds to provide new sources of financing for growing enterprises. For information on ARC-funded activities in this program area, visit: www.arc.gov/entrepreneurship

Angel Investing in the United States

Angel investors are an important source of capital for growing firms. The Center for Venture Research estimates that U.S. angel investors provided $20.1 billion in approximately 61,900 deals (about 35,000 small businesses) in 2010. Many of the investments were in start-up or very-early-stage companies. The best available estimates are that over 265,000 people have made an angel investment in the last two years (including accredited and non-accredited investors). Many more people could become angels—based on a net worth of $1 million or more, the potential number of angel investors is 4 million.

Between 10,000 and 15,000 angels are believed to belong to angel groups in the United States. The average angel group has 42 investor members and invested a total of $1.9 million in seven deals in 2007. According to the Angel Capital Association and the National Association of Seed and Venture Funds, the Appalachian Region has 15 angel funds, leaving significant areas underserved by this important source of capital.

RAIN Source Capital

RAIN Source Capital is an industry leader that has efficiently and effectively guided communities through angel fund creation and capitalization. It has:

- Formed 24 RAIN angel funds in rural and underserved communities
- Raised $20+ million committed capital within these funds
- Identified 450 angels/accredited investors within their network of funds
- Invested in 80+ portfolio firms.

A total of $150 million has been invested by RAIN angel funds, members, and VC's, and five communities are currently planning new RAIN angel funds.

Through its proprietary process, RAIN Source Capital guides interested parties in assessing the feasibility of an angel investment fund in their community. As appropriate, RAIN Source guides groups through the three-phase process to design, fundraise for, and organize a formal angel investment fund.

An experienced manager of angel investment funds, RAIN Source Capital is under contract with ARC to provide the selected entities the technical assistance to form an angel fund(s). Entities will apply to ARC to receive technical assistance to form an angel fund. RAIN Source Capital will provide in-person, on-site technical support for the formation of these funds, to include: meeting with the key angel investor/leaders to discuss fund structuring options; fundraising support to capitalize the fund; and management of the organizational meeting of the angel fund. RAIN Source Capital may be retained by the local angel fund to manage ongoing activities, or the angel fund could be managed locally.

More information on RAIN Source Capital is available at www.rainsourcecapital.com

PROPOSAL SUBMISSION: ANGEL FUND FORMATION PROPOSAL

Proposals may be submitted for either of two types of awards:

I. Technical assistance will be provided by RAIN Source Capital to local entities to support new angel fund formation or to improve the performance of an existing angel fund/network. Up to four applicants will be selected for this support.

II. Direct grant support will be provided to qualified local organizations to support the formation of a new angel fund. Up to $30,000 in direct grant support will be provided to one qualified applicant in this round. Direct grant support may be used for a range of eligible costs, including personnel, travel, and contractual expenses, and other related costs.

   Note: To successfully apply for direct grant support, the applicant must be able to demonstrate a track record of forming and successfully managing angel investment funds.

The proposal submission should not exceed five pages, with other pages appended as supplemental material, and should include the following information:

1. Briefly describe the lead applicant's organization, and indicate the award for which the application is being submitted: I. Technical Assistance or II. Direct Grant Support. *(One-page summary)*
    a. Describe the organization's mission, program, operations, and governance. Emphasize previous programs targeting entrepreneurs, investors, or financial institutions, and associated outcomes.
    b. Identify relevant background, qualifications, and experience of the organization(s) and personnel who will be convening or supporting the proposed angel fund. Information should include direct experience with the specific subject-matter area and relevant references. As appropriate, include resumes of project personnel in an appendix, not to be considered within the five-page proposal submission limitation.

2. Define the opportunity and the need for local, angel capital.
    a. Define the geographic area to be served by the proposed angel fund. A map may be included in the appendix.
    b. Describe the need for local, angel capital within the target geography.
    c. Describe the entrepreneurial support systems operating in the target geography. Identify partner organizations that can serve as mentors and advisors to entrepreneurs, and generate deal flow appropriate to the angel fund (e.g. accelerators, colleges, etc.).

3. Demonstrate the ability of the applicant and partners to convene angel investors. As part of the angel fund formation process, the applicant will need to:
    a. Convene a group of 15 to 25 prospective angels who meet the SEC "Accredited Investor" definition[1] to attend an angel fund informational meeting. These high-net-worth individuals must have an appetite to invest in early-stage companies, demonstrate the risk tolerance for early-stage investing, and be willing to mentor entrepreneurs. Please describe the applicant's relationships with these investors and how they have been, or will be, identified. This activity will be undertaken as part of the angel fund formation workplan (see page 7).
    b. Identify from this group of angel investors two to five individual champions who are willing to play a lead role in supporting the process required to form an angel fund and who are willing to lead fundraising activities, using their personal network and the applicant's network. This activity will be undertaken as part of the angel fund formation workplan (see page 7). Please note whether individual champions have already been identified or solicited.
    c. If applicant is applying for the Direct Grant Support (II), outline experience in forming and managing an angel fund. Include the year and amount the fund(s) was capitalized, number of members, targeted geography of fund, number and types of investments made to date, exits, and results.

4. Demonstrate the ability to convene and collaborate with local resources to support the angel fund activities (when established).
    a. Identify professional service providers and/or nonprofit agencies that can support the activities of the fund. The activities of these partners could include deal flow sourcing, due diligence guidance, valuation, and administrative support such as meeting logistics, bookkeeping, taxes, and related support.
    b. Outline how the partner organizations have collaborated in the past, and the outcomes from previous partnerships. If this is a first-time collaboration, please outline a framework of how the entities plan to collaborate for a proposed angel fund.

Proposals are due by 5:00 p.m. EDT on June 15, 2012.

Please send proposals electronically in **one** PDF file to the Appalachian Regional Commission at angelfunds@arc.gov

Proposal Evaluation
ARC will select communities to form angel funds through a competitive grant process based on:
- The completeness of the required information and the likelihood of success.
- An articulated need for angel capital resources within the existing entrepreneurial ecosystem.
- The ability to convene a group of accredited investors.
- Credibility within the community and demonstrated ability to convene partner resources.

ARC anticipates that recipients will be selected by July 13, 2012.

Informational Webinars
Questions about this RFP and angel fund formation and operation will be address at the following scheduled informational webinars:

Monday, May 14: 1:30 p.m.–3:30 p.m. EDT
Tuesday, May 15: 1:30 p.m.–3:30 p.m. EDT

To register for a webinar, send an email with your name and organization contact information to: angelfunds@arc.gov . Confirmation of your participation in the webinar will be provided to all registrants.

ADDITIONAL RESOURCES

Associations

Angel Capital Association
www.angelcapitalassociation.org

National Association of Seed and Venture Funds
www.nasvf.org

Publications

Benjamin, Gerald A. and Margulis, Joel B. *The Angel Investor's Handbook: How to Profit from Early-Stage Investing*. New York: Bloomberg, 2001.

Shane, Scott A. *The Importance of Angel Investing in Financing the Growth of Entrepreneurial Ventures*. An Office of Advocacy Working Paper, U.S. Small Business Administration, 2008. Available online at http://www.sba.gov/content/archived-economic-research-working-papers

ANGEL FUND FORMATION WORKPLAN

RAIN Source Capital will work with successful applicants to develop a workplan for angel fund formation that accommodates unique local conditions. A workplan template is below provided as an outline for the angel fund formation process and will be reviewed in the scheduled webinars.

RAIN Source Capital will provide technical support to successful applicants for implementation of each phase of the workplan.

Phase I: Feasibility and Design—90 Days

A. Initial meeting
   Identify and convene angel investors
   - Outcome: Communicate overview of process, identify leadership group and members, schedule next steps.
B. Initial fund design meeting with angel leadership group
   Member assessment, fund design worksheet
   - Outcome: introduce fund design, identify investor prospects, identify next steps.
C. Follow-up meeting with angel leadership group
   Discuss draft fund design and solicitation of interest
   - Outcome: Finalize fund design, finalize investor prospects, identify next steps.
D. Repeat as necessary!

Phase II: Fundraising—60 days

A. Initial fundraising meeting with leadership group
   Draft of legal documents
   - Outcome: review documents, identify investors, outline fundraising schedule
B. Repeat if necessary
C. Final fundraising meeting with RAIN leadership group
   Approve legal documents
   - Outcome: finalize documents, finalize investors, finalize fundraising schedule
D. Fundraising kick-off meeting with full membership
   Review legal documents, membership tracking sheet
   - Outcome: collect contribution agreements, checks for deposits in escrow
E. Weekly meetings if necessary

Phase III: First Organizational Meeting

A. Initial organizational meeting
   Resolutions, legal documents, service agreements, proxies, banking info
   - Outcome: Execute closing documents, execute service contracts, pass resolutions
   - Introduce and orient members to investing process and technology
   - Organize committees, collect membership contributions