

**PE HUB Webinar:
How to Raise an SBIC Fund**

**The SBIC Licensing Process and
Doing Business with SBIC Funds**

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Welcoming Remarks



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McGuireWoods LLP - Firm Overview

- American Lawyer Top 100 firm
- More than 950 attorneys
- 17 U.S. offices

McGuireWoods LLP

Private Equity | Representative Work

- Portfolio Company Acquisitions and Investments
- Transaction Structure Advice and Recommendations
- Due Diligence Planning and Oversight
- Preparation, Review and Negotiation of all Acquisition, Financing, and Investment Agreements
- Fund Formation and Representation including all aspects of SBIC Regulatory Work

Today's Agenda

- Overview of SBIC Program
- Basics of the Debenture Program
- SBIC Fund Manager Qualifications / Licensing Process
- Transactions with SBIC Funds

Overview of the SBIC Program

- SBIC Program was created in 1958 pursuant to the Small Business Investment Act of 1958. The first Debenture SBIC was licensed in 1959.
- The Participating Securities Program was created in 1994 and the last PS SBIC was licensed in September 2004.
- There are 158 active Debenture SBIC Funds in FY 2012.
- Debenture SBIC Funds made 1,907 Financings to Small Businesses in FY 2012.
- 2012 McGuireWoods Private Equity and SBIC Debenture Report.

Basics of Debenture Program

- SBA provides leverage of 200% of private capital.
- SBA Debentures has a semi-annual interest-only payment.
- SBA Debentures have a 10 year maturity.
- Coupon Rate is approximately 200 bps over the 10 Year Treasuries.
 - Last Pooling was priced at 2.245% in September 2012.
- There are no prepayment penalties for repayment of SBA Debentures.
- SBA Debentures are unsecured and non-recourse to fund managers.

SBIC Fund Manager Qualifications

- Senior Level Investment Experience.
- Realized Track Record of Superior Returns.
- Approved Investment Strategy.
- Cohesive Management Team.
- Other Qualifications.

Timeline of Licensing Process

- Plan on a 6-9 Month Process.
- Non-Binding Indication of Interest from SBA CIO, Sam Boyd.
- Licensing Process can run concurrently with Fundraising Process.
- MAQ Submission.

Management Assessment Questionnaire

- The MAQ is the SBA's Gatekeeper's Form.
- MAQ: 2181, 2183 and Excel Spreadsheets.
 - Form 2181: Fund Information.
 - Form 2183: Principal Information.
 - Exhibit Fs: Track Record Information.
- Initial Review by SBA Gate Keeper: Scott Schaefer.
- Formal Presentation to SBIC Investment Committee.
- Issuance of "Green Light" Letter.

Formal SBIC License Application

- SBIC License Application:
 - Form 2181: Fund Information (Updated).
 - Form 2182: Additional Fund Information.
 - Form 2183: Principal Information and FBI Checks (Updated).
 - Exhibit Fs: Track Record Information (Updated).
 - Organizational Documents.
- Minimum Limited Partnership Commitments.
- SBIC Divisional Committee.
- SBA Agency Committee.
- Signed by SBA Administrator.

Formation of SBIC Limited Partnership

- Fund Structures.
 - Traditional Limited Partnership Fund.
 - Drop-Down Structure.
 - Side-by-Side Structure.
 - Foreign Investor Funds for ECI Issues.
 - Business Development Companies.
- General Partner is a Single Purpose Entity.
- Management Fee Issues.
- Carried Interest Issues.

Other Regulatory Issues

- On-Going Regulatory Oversight:
 - Quarterly and Annual Reports
 - Financing Reports
 - Annual Examinations
- Exemption from Fund Registration.
- Exemption from Volcker Rule Provisions.

CRA Credit Banks

- Special Status of SBIC Funds as a CRA Investment
 - Bank regulators should presume that any loan or investment in an SBIC Fund promotes economic development.
 - SBIC Funds must serve the broader geographic area containing the bank's assessment area.
- Federal regulators do not distinguish between direct and indirect investment. Indirectly investing in a community through an SBIC Fund therefore qualifies.

Transactional Issues

- What is a Small Business?
- Tangible Net Worth (excluding goodwill) of less than \$18 million **and** average after-tax income for the prior 2 years of less than \$6 million.
- **OR**
- Companies may still qualify if they meet certain size standards for their industry group which are based on the number of employees or gross revenues.
- A “Smaller Enterprise” must have a tangible net worth of less than \$6 million and average after-tax income for the prior 2 years of less than \$2 million.

Transactional Issues

- Cost of Money and Closing Fee Issues:
- 19% for Loans and 3% Closing Fee.
- 14% for Debt Securities and 5% Closing Fee.
- Overline Limitations:
- 10% of the Total Fund Size.
- SBA Forms (480, 652 and 1031).
- Right to Inspect / Standard Financial Disclosures and Covenants.

Transactional Issues

- Prohibited Transactions. SBIC Funds may not invest in the following:
 - Relenders or Re-investors (Banks/Factoring/Other PE Funds).
 - Project Finance.
 - Most Real Estate Projects.
 - Foreign Business.
 - Passive Businesses.

For more information, contact:



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Mr. Kromkowski has represented investment funds and portfolio companies in all types of private equity transactions from venture to mezzanine to buyout transactions. He also has extensive experience in counseling fund managers in all aspects of fund formation. He is among a small group of lawyers in the United States who have significant transactional and regulatory experience with Small Business Investment Companies (SBIC Funds).