

Business Angel Co Investment Fund

Information Note 1

The Business Angel Co Investment Fund (CoFund) has been made possible because of a successful bid to the UK Government's Regional Growth Fund. The fund will make £50m available to invest alongside Business Angel networks or syndicates (hereafter both referred to as "Syndicates") into eligible SMEs. The bid was approved, subject to due diligence, on 12 April 2011 and could be operational by the autumn. Every effort is being made to bring this date forward and in the meantime interested Syndicates can register their interest to receive updates by sending an email with their contact details to cofund@capitalforenterprise.gov.uk.

The fund will operate by investing alongside and on the same terms as Syndicates. This note contains details of the type of investment that can be supported and the roles of the respective partners.

The fund will not be open to approaches from individual businesses. Businesses seeking investment should first look for an investment Syndicate. More information on Business Angels, Syndicates and Networks can be found on the British Business Angels Association website www.bbaa.org.uk.

What type of deal will the fund invest in?

Syndicates should be looking for the CoFund to provide funding of between £50,000 and £1m in investment rounds ranging from £200,000 upwards into eligible SMEs¹ (Subject to any EU State aid requirements and review in the light of experience). The size of the investment needs to be significant enough to properly fund the business and to allow for the cost of proper due diligence and legal advice. The investment will need to be a new investment for the Syndicate, rather than supporting an existing investment, which will help to ensure that the Syndicate and the CoFund's objectives are broadly aligned. The CoFund will, to the extent possible, follow the terms of the Syndicate including the structure and price of any investment. Once invested the CoFund will be able to make follow on investments alongside Syndicates in to companies that are already within its portfolio.

How does the relationship with the Syndicate work?

In order to keep bureaucracy to a minimum and to allow full access to the fund from all syndicates, the criteria for becoming a partner syndicate will simply be to have an investment paper approved by the fund investment committee. At that stage the syndicate will need to agree that the CoFund will see all future opportunities (although it will not be obliged to invest) and the syndicate will also have to agree to provide the CoFund with monitoring information. This information will include a requirement to make a recommendation in relation to future investment or exit activity.

¹ There will be some RGF specific restrictions which have not yet been finalised.

Where the CoFund chooses to invest, a one off fee of 2.5% of the amount invested will be payable to the syndicate manager. This is the same level of fee that is paid to partners of the Scottish Co-Investment fund and is considered reasonable as a payment for the investment monitoring and reporting activities that the syndicate is then required to carry out on behalf of the CoFund. The syndicate will be able to collect an arrangement fee from the investee company on the CoFund contribution and primarily this should be used to pay costs (e.g. legal fees). These fees will have to be transparent in the investment paper and the Investment Committee will be able to reject a proposal if they feel that fees and charges are too high. The CoFund will expect to share in any monitoring or other fees charged to the investee company on the same basis as other syndicate members. The one off fee will be kept under review and some partners may want to accept a reduced fee to be allowed, for example, a larger share of carried interest (a success related payment).

Some syndicate managers take a carried interest payment on successful investments. Although the overarching principle is to invest on the same basis as private investors the bid partners and investment committee will want to ensure that any carry is reasonable and may want to restrict to a certain percentage as a maximum.

What are the different roles and responsibilities within the CoFund structure?

Bid Partners

The bid to the Regional Growth Fund was led by a consortium of private sector partners with support from Capital for Enterprise. The Bid Partners were:

- Braveheart Investment Group
- Hotspur Capital Partners
- Octopus Ventures
- Oxford Investment Opportunity Network (OION)
- Venrex Investment Management

The Bid Partners have no preferential access to CoFund investment but have been involved in its development and representatives of each organisation will be asked to form an Advisory Board to oversee the fund's progress.

Syndicates

Syndicates will need to be sufficiently formally constituted for someone to be able to sign the necessary commitments to become partners of the CoFund.

Syndicates will be responsible for sourcing investments, carrying out appropriate due diligence and producing the investment paper for the CoFund's investment committee. This activity largely reflect the way syndicates already operate but in some cases it may involve syndicate leads taking on a more active role. Research indicates that this more active role is consistent with more effective investment.

Investment Committee

The Investment Committee (IC) of the fund will be independent of the other bid parties with its secretariat functions performed by CfEL. The IC will be tasked with taking a sensible private investor view on the proposals it sees and will specifically not be charged with acting as a commercial fund's investment committee. The question the IC will be required to answer with each investment will be "Is it reasonable for an individual syndicate member to invest their own money into this deal?" in answering the question the IC will have regard to the structuring of the investment and the level of due diligence that has been carried out.

It is possible that the IC might ask the syndicate lead to present their investment paper but otherwise the paper will be submitted via CfEL.

Investment committee members will be remunerated but at a modest level. CfEL will manage the appointment of IC members on behalf of the Advisory Board.

CfEL

CfEL will provide the day to day fund administration services and the secretariat for the Investment Committee and Advisory Board. CfEL will pre-screen proposals to ensure that the investment papers are 'complete' and show evidence of due diligence having been carried out. CfEL will provide feedback to syndicates on any papers that are rejected.

The fund administration will include checking that any geographic or state aid restrictions are met and anti-money laundering checks are performed as well as providing (aggregate) reporting to Government against the agreed targets for the fund.

CfEL are not intended to operate the CoFund on the same basis as for its other funds operations where it carries out primary due diligence and will lead on the structuring of deals. The fund will be largely passive and CfEL's role will reflect this.

Further information notes will be issued as the fund develops.

CfEL

12 April 2011