

Applied Research Matching Fund (ARMF) Guidelines

FISCAL YEAR 2006 | July 1, 2005 to June 30, 2006

Established under Kansas statute: 74-8107

The ARMF fund is limited. Only companies and technologies that meet the investment criteria outlined in ARMF Guidelines are eligible. Successful investments generate jobs for Kansans and funds for KTEC to reinvest into other companies.

Objective

The Applied Research Matching Fund (ARMF) is designed to invest in early-stage Kansas companies that have **1)** innovative technologies, **2)** potential to create high-paying jobs, and **3)** opportunity to create wealth within the company and an ROI for Kansas.

Evaluation

The investment evaluation will be based on ARMF objectives and KTEC's assessment of each company for:

- A strong management team with the vision to utilize business and technical assistance when needed.
- An entrepreneurial spirit with the vision to utilize business and technical assistance when needed.
- Potentially unique or disruptive innovative growth technologies,
- Vision to build a company around the technology and develop prospects for full-scale market role-out.
- Desire to pursue and attract follow-on venture or angel funding.

Consideration

To be considered, **a company must complete the ARMF application form and submit it along with a business plan.** The company must demonstrate, through market research, that a considerable market exists and that the project has the potential to produce substantial results for the Kansas economy.

Contact

Prior to submitting any information, KTEC advises that the business contact a member of the KTEC Investment team or a KTEC Commercialization Center.

- Michele Weigand (mweigand@ktec.com), VP of Investments and Portfolio Mgmt.
- Sheila Meyer (smeyer@ktec.com), Investments Assistant

All can be reached at (785) 296-5272.

1 Investment Criteria

Only qualified companies will be considered for ARMF investment. Funding may be made to companies working alone or in collaboration with universities, business incubators, or other companies.

1.1 Kansas Economic Benefit

ARMF is intended to invest in companies that benefit the Kansas economy through jobs and wealth creation. The company must demonstrate to KTEC that the technology is innovative and that a considerable commercialization potential exists.

1.1.1 Return on Investment

ARMF invests in companies with the potential to generate a monetary return on investment. The timing of the investment return will vary depending on the type of business and negotiated terms.

1.1.2 Kansas Jobs

The state should benefit by increasing the tax base through Kansas jobs and higher-paying salaries.

1.1.3 Kansas Business Location

A portion of the business must be conducted in Kansas. In some cases, businesses may incorporate in other states while conducting the principal business in Kansas. Companies shall certify all state, federal and local licenses, regulatory requirements and qualifications are in order as needed.

1.1.4 Business Assistance

KTEC will give preference to companies seeking some form of business assistance.

1.2 Matching Requirements and Allowable Expenses

The company must match the ARMF investment with 150% of the amount of KTEC funding (60/40 split). The match requirement applies to any sized company and may include outside investors.

- The ARMF KTEC funds are for the development of the technology and not to be used for basic research or working capital.
- The company must commit matching funds before KTEC finalizes the investment.
- The company matching funds may be used for any purpose.
- KTEC will consider other company matching options on a case-by-case basis, but retroactive costs are not eligible.
- Neither the ARMF nor company matching funds may be used to pay earlier investors or prior debt.

Note: If a royalty investment is made, KTEC provides matching monies upon receipt of satisfactory progress reports and documentation of company expenditures.

1.3 Technology Innovation

The fund emphasizes technology innovation that is beyond the early research stage. This innovation must lead to marketable products or processes and revenue potential.

2 Investment and Review Process

The ARMF lifetime investment for any one company cannot exceed **\$125,000**. KTEC will seek a return on its investment through either a royalty agreement or convertible debentures. KTEC will only invest in **C corporations** or **Limited Liability Companies** when negotiating convertible debentures, and will consider **S Corporations**, C Corporations or Limited Liability Companies when completing royalty agreements.

KTEC staff and the ARMF Investment Committee review all investment opportunities. Business plans that pass an internal screening and due diligence process will be invited to present to the ARMF Investment Committee that convenes on a quarterly basis. Only investments recommended and approved by the Committee will be submitted to the KTEC Board of Directors for final approval and funding. Submitting a business plan does not guarantee funding. Average time from final Board approval to initial funding is typically one to two months.

2.1 Investment Terms

ARMF investments are structured in terms that facilitate success and generate an ROI for KTEC and the company. **ARMF considers each investment, set of terms and negotiation process unique.**

2.1.1 Equity

KTEC will consider equity financing in cases where a company has received a previous equity investment or has demonstrated a marketable valuation. Preference is given to preferred stock over common stock.

2.1.2 Convertible Debenture

Convertible debentures will be used when a company is considering a later equity round of funding. This debt and equity instrument allows the company and KTEC to begin an investment relationship while avoiding a premature valuation process.

2.1.3 Royalty

The company will pay the royalty on a regular basis starting with the first product sale. Royalty rates are competitive with the current economic development financing market and may vary depending on the risk level of the company and the negotiated terms.

For royalty investments, KTEC will provide monies upon receipt of satisfactory progress reports and documentation of company expenditures.

2.2 Due Diligence Review Process

A committee of business and technical experts evaluates each company's market potential and technology merits. The funding recommendation depends on the judgment of the Investment Committee and outside reviewers. The process is highly competitive.

- KTEC screens application and business plans for adherence to program intent, guidelines, investment opportunity, and budget. Business plans not passing this screening will not be considered.
- KTEC conducts independent market research and analysis and evaluates the commercial potential of the company, including technology, market strategy, financials, management background (including credit checks on principals of early-stage companies) and overall business potential.
- Independent reviewers may be used by KTEC to evaluate the technical merits of the products and/or the services of the company.
- KTEC's Investment Committee reviews the company business plan and all background material. This committee meets on a quarterly basis.
- The company makes a presentation to the Investment Committee at the quarterly meeting.
- The Investment Committee makes its funding recommendation to the KTEC Board of Directors for final approval.

2.3 Provisions of Funding

Once an investment is approved for funding, an investment or royalty agreement/contract will be negotiated and signed outlining the terms, responsibilities, and obligations of each party.

If a royalty agreement is structured, payments are made as expenses are incurred and milestones are met.

2.4 Reporting

KTEC will require that companies report status on a regular basis.

- The company is required to maintain records and accounts that properly document the source and use of all funding resources and subsequent product revenues and economic impact. Such records will be subject to audit by KTEC, who will conduct on-site or teleconference reviews as necessary to adequately monitor the project.
- Quarterly reports will be required detailing: (a) management discussion of accomplishments relative to established milestones and timeline, (b) budget summary and company financial position.
- Any significant delay in milestone progress, reporting, or the transfer of company matching funds will invoke an assessment by KTEC regarding project termination.
- Within 30 days following completion of the project, the company will provide a final report, with emphasis on technical accomplishment and forecasting commercialization.

In addition, all companies receiving an investment from KTEC will be requested to provide timely reporting and to participate in KTEC's annual economic impact survey.

3 Proprietary Information – Kansas Open Records Act (KORA)

KTEC is a quasi-state agency. KTEC, funded by the Economic Development Initiative Fund, reports to a Board of Directors appointed by the Kansas Governor, Kansas Legislature, and university presidents.

Any proprietary company financial information and intellectual property submitted to or discussed with KTEC is confidential and **not** subject to the Kansas Open Records Act. A list of exemptions can be found in **K.S.A. 45-221**.

- To ensure a strict confidential process, all confidential information (trade or business secrets as defined by Kansas law) should be clearly marked within the application. Such information will be held in strict confidence to the extent allowable by law.
- When KTEC does seek Board approval for funding, if trade secrets must be presented or discussed at a public KTEC Board or Committee meeting, the Board or Committee will enter a closed session to protect confidentiality.