



# Vermont Seed Capital Fund, LP

Investing in Entrepreneurs and Employers since May 2010

Annual Report to Limited Partners and State of Vermont Stakeholders  
**June 30, 2013**

VCET Capital Corporation  
General Partner and Fund Manager  
November 30, 2013

## **Fund Overview**

The Vermont Seed Capital Fund, LP launched for investing in May 2010. The for-profit Fund is managed by the VCET Capital Corporation, a wholly owned subsidiary of the non-profit Vermont Center for Emerging Technologies (VCET). VCET was selected as manager following a competitive bid process conducted by the Vermont Economic Development Authority (VEDA) in the fall of 2009.

The for-profit Fund is capitalized with \$5.1M, is professionally managed and designed as a revolving venture capital investor to support a select number of seed and early stage companies in Vermont.

Fund performance objectives include:

- Financial return commensurate with high risk investing in order to revolve the fund, after write-offs and expenses.
- Next generation job creation across Vermont.
- Capital leverage achieved for each \$1 invested by the Fund.
- Innovation ecosystem benefits (college technologies, internships, supply chain, cluster benefits, recruitment, natural resource utilization, green technologies, etc).

The Fund invests between \$50,000 and \$250,000 per transaction via a variety of debt and equity instruments. The Fund's manager, which is an entity, not an individual, makes investment recommendations for review and actions by the Fund's Investment Committee. The Fund seeks to support a select group of high opportunity businesses and high potential teams to meet the four principal Fund Objectives.

Because of a strategic relationship with VCET, portfolio firms also have access to substantive programs, facilities, partners, mentors and value-adding services at [www.vermonttechnologies.com](http://www.vermonttechnologies.com). VCET was named the #11 incubation program in the world by the UBI Index in 2013.

## **Fund Activity and Impact So Far**

The Vermont Seed Capital Fund, LP ("Fund") was created to provide early stage, high risk companies with risk capital to start and grow next generation employment opportunities. Prior to the Fund's capitalization in May 2010, Vermont was one of a handful of states without an early stage, state sponsored venture fund.

As of June 30, 2013, the Fund has invested in 12 companies for a total of \$1,884,544. This is comprised of \$1,774,544 in initial investments into 12 firms and \$110,000 in follow-on investments into 4 companies. Per company investments range from \$60,000 to \$250,000, with an average of \$157,045 invested per company.

The Fund has co-invested with accredited angel investors, angel investor groups and other institutional investors such as Fresh Tracks Capital, Launch Capital, Atlas Ventures .406 Ventures, Silicon Valley Bank, and Google Ventures. It is important to note that other accredited individual or institutional

investors or lenders are responsible for their own due diligence and investment decisions.

The Fund is required to report on total capital at the time of initial investment per company as a measure of capital leverage. Results to date have surpassed initial expectations of 2x leverage. Cumulative capital reported by companies totals \$21,510,194 for a capital leverage ratio of 11.4x the Fund's invested capital of \$1,884,544. The total capital investment secured by the 12 current portfolio companies at the time of the Fund's initial investments totals \$9,049,128. The Fund's leverage at time of initial investment was 5.1x.

As a standard practice, for each \$1 invested by the Fund, an additional +/- \$1 is held in reserve for follow-on growth financing, if it makes sense (and cents) to support further any one firm's situation. Not all firms who receive initial capital support, however, will receive follow-on funding. Since investing began in May 2010, the Fund expects to invest over 3 to 4 years into +/- 17 firms during its first capital revolve cycle. Investments are anticipated to not return capital until years 5-8 though there may be exceptions. Per company investment losses are likely to occur during the first 1-3 years post initial investment. For this high risk asset class, teams and products scale, meet milestones or fail generally during this period after initial investment.

Nationally on average, about 80% of all capital in this stage of a company's life is used for personnel (full, part-time & consultant). Most of the Fund's investment proceeds are used for employees, marketing & sales, product development and general working capital purposes.

The communities in which these first 12 startup employers have been supported are: White River Junction, Woodstock, Richmond, Burlington, Winooski, St. Johnsbury, S. Ryegate, Montpelier, Colchester, Middlebury, Barre, and Waitsfield. Additional remote workers are located around Vermont and in fact, across the globe.

Through proactive outreach, a strategic relationship with the VCET mentor and incubation program, and from an existing referral and sourcing network, the Fund's team has screened and reviewed an estimated 230 firms and entrepreneurs since inception. Capital seekers have come from across Vermont, the U.S., Quebec and elsewhere globally.

At any given time, the Fund is tracking 2-5 firms for investment consideration. The investment process from initial screening to closing can range from 8 weeks to 2 years, depending on the readiness of the business proposition, team, co-investors required for a sufficient round of finance and signals of market traction/demand for its products or services. The process averages about 2 - 5 months from start to closing. The Investment Committee meets monthly or more frequently as needed to review portfolio firm situations and new financings.

During fiscal year 2013 (ending June 30th), the Fund closed 2 initial company transactions into Rapid Focus Security LLC (d.b.a. Pwnie Express) in Berlin, VT and Northern Reliability, Inc. in Waitsfield, VT. Additionally, there was 1 follow-on financing into Green Mountain Digital during this period. An additional 3 follow-on investment requests from existing portfolio firms were either declined or deferred subject to certain performance milestones or conditions to be achieved.

During FY13, the Fund realized its first round of investment failures in 3 companies, 2 of which were disclosed in the FY12 Annual Report as subsequent events. Details on these firms and economic impacts are included later in this report. Each had been previously written down in whole or part as an unrealized loss, during the Fund's semi-annual portfolio review and valuation process.

During fiscal year 2013, the Fund got very "close" to initial investments in another 3 firms. However, for a variety of reasons ranging from price, references, alignment gaps, minimum co-investment lacking, deal structure, fund requirements, other terms and conditions, etc, these potential investments did not materialize. This is not uncommon for this kind of early stage investing. Often, these firms return for consideration again as we have seen occur with other portfolio firms.

## Subsequent Events

Subsequent to the Fund's June 30, 2013 year end thru November 30, 2013, the following warrant disclosure and sharing at this time:

- Rapid Focus Security (dba Pwnie Express) in August closed a \$5.1M Series A Preferred Stock offering led by Boston based venture firms .406 Ventures and Fairhaven Capital. In addition to converting its Convertible Note investment of \$200,000, the Fund contributed an additional \$100,000 as part of this financing.
- BuysideFX (formerly FXAligned) conducted a Series Seed 2 funding in July. The Fund contributed follow on investment of \$100,000 for this round of financing.
- The Fund invested \$50,000 into a Convertible Note offering by Campus Connector (dba GroupZoom) as part of a \$155,000 Notes offering. A new Series Seed Preferred Stock investment led by Fresh Tracks Capital occurred in November to provide additional capital to this fast growing group travel company. This company is the Fund's 13th initial investment. It's website is: <http://www.groupzoom.com/#about> . The company was founded by a Middlebury College student during his senior year.
- SemiProbe recruited a new CEO and current investors have provided fresh capital a via Convertible Note offering. The Fund invested \$72,917 into these Notes over two installments this Fall. The Fund originally invested \$250,000 in December 2010 as part of a \$900,000 financing of Series A Preferred stock and debt financing. The company makes semiconductor testing equipment and is based in Winooski.
- A \$100,000 investment commitment by the Fund into a local medical device company did not close in August. The Company chose to assign allocation to another existing investor.
- The Fund provided a Term Sheet to a company in the energy software sector after working with the team for the prior 9 months during company formation and early stages.
- Green Mountain Digital, Inc (Yonder App) closed a \$3.8M Series B Preferred Stock offering led by Monster Worldwide (monster.com). Please download and use the free Yonder.it app.
- VEDA Capital Investors contributed another \$57,450 of permanent capital into the Fund. The Fund's total initial capitalization is \$5,097,450, with VCET contributing \$1,000,000 of this total.
- As of November 30th, The Fund's total invested capital across 13 companies is: **\$2,207,462**
- Due to lower than modeled follow on investing in FY13, the Fund anticipates another 4 initial investments, up from 3, into Companies during this first capital revolve.

## **Fund Manager's Outlook into FY14**

Since investing began in May 2010, the Fund's principal milestones and activities so far have been to organize quickly and properly, complete the initial \$5.1M capitalization, make 13 initial investments into diverse companies so far, make 7 follow-on investments totaling \$383,000, provide oversight and support to 13 portfolio firms, limit realized losses to 3 companies to date, conduct annual Fund audits and reporting, prospect for high opportunity investments in support of Vermont's next generation of employers and manage towards fulfilling the Fund's four principal objectives around financial return, jobs, capital leverage and ecosystem benefits.

Given finite capital resources, statutory fund requirements and an increasingly active entrepreneurial sector in Vermont, the Fund must say "no thanks" or "not yet" much more frequently than "yes" to capital seekers. Fortunately, the Fund's team is able to assist entrepreneurs and firms even if an investment is not made via a relationship with the non-profit Vermont Center for Emerging Technologies (VCET) and its network of mentors, partner organizations, angel investors, venture capital firms and higher education institutions.

For the 4th consecutive year, an independent Audit was performed and without deficiency findings or any needs for corrective actions - this is another sound result in CPA parlance. Among other areas, the audit covered topics such as accounting, governance, conflict of interest policy, portfolio valuation, cash management and other internal processes and practices. Fund operating expenses were 3.15% which consists of a 2% annual management fee and certain direct professional services fees such as legal, insurance and audit.

Considerable efforts are undertaken in supporting portfolio firms in post-investment activities such as Board meetings, personnel recruitment, strategy, new customer prospecting, new financing and product/service sales, etc. The effort and time by the Fund's team is significant post investment. The Fund continues to leverage the VCET network of staff, partners, advisers, mentors, interns, co-investors and college networks to support and grow portfolio firms. To date, there have been no early Fund investment exits so far. Data from other Vermont Funds and nationally indicate a typical 7 year holding period until investment harvesting occurs.

As we look beyond the Fund's first 13 companies supported, the Fund anticipates making another 4 initial investments during the Fund's first revolve for a total of 17. Additionally, there will be more follow-on investment decisions to be made among the active portfolio. As determined by the Investment Committee, some portfolio companies may warrant additional funding, while others may not. The Fund still remains in the early years of its investing activities and anticipates further IRR losses largely from the J Curve effect until successful investment exits occur. For background, a Fund generally invests over the first 1-4 years. During this period, a Fund realizes cash return losses (negative IRR) given the investment outflows, write-offs and annual operating expenses. Following these early years, then the Fund anticipates harvesting investment returns beyond year 5. The Fund has an initial 10-year time horizon which is the industry norm.

In accordance with policies and accounting standards, the Fund continues to make estimated market value adjustments at mid-year and year-end, or on an as realized, interim basis. These adjustments can include unrealized gains or losses and any realized gains or losses among the Fund's varied investments.

As of this report date, 13 companies have received investment by the Fund, 3 have formally ceased operations and are realized losses in FY13 (True Body Products, eCorp English and Thermal Storage Solutions) and 10 portfolio companies are actively working hard to reach their operating milestones and achieving a sustainable business model. Without a doubt, we should continue to expect volatility in the estimated market valuations, the month-to-month highs and lows within specific portfolio firms and in the ratio of active companies to total companies. This uncertainty and volatility are typical of an early stage, high risk investment fund.

VCET Capital Corporation (the Fund Manager) would also like to acknowledge and thank the Seed Fund Advisory Board (SFAB) members for their efforts and assistance. The volunteer members are Jo Bradley, Robert Britt, Hinda Miller, Dr. John Evans and Jason Oleet. SFAB was established under the enabling statutes, met twice over this past year, receives confidential information on investments, receives the Fund's audit and are invited to the semi-annual portfolio review meetings with the Investment Committee. The Investment Committee members also attend the SFAB meetings.

Fund Investment decisions are made by a three member committee consisting of VCET Capital Corporation's David Bradbury and two independent Investment Committee members with deep early stage investing and fund operation experiences. James Robinson and Ken Merritt serve as volunteer investment committee members providing independent domain expertise and guidance. VCET's Andrew Stickney also plays an important role. The General Partner wishes to thank these professionals for their considerable volunteer time, expert skills and contribution to the Vermont Seed Capital Fund, and expert deliberation on these high risk, early stage investments. Investment Committee members follow a Conflict of Interest policy, which is available upon request.

Going forward, there remains strong continued interest by entrepreneurs from nearly all sectors seeking high risk capital. Given some transactions that did not close in 2013 as expected, we anticipate making an additional 3-4 initial company investments by end of FY14 from the first revolve.

As cautioned each year, early stage investing can be described as a "team contact sport" in that this stage is high risk, always dynamic, subject to inevitable losses, requires significant post investment support, and yet offers the greatest potential for high wage job growth, risk capital inflows and new wealth generation for employees, founders and Vermont as a whole. We remain fully engaged, proactive in outreach and active in investing into appropriate high risk opportunities, supporting entrepreneurs statewide and fulfilling the Fund's four principal performance objectives.

Thank you for your continued support.

Sincerely,

David Bradbury, President

## Vermont Seed Capital Fund. LP Impact Measures @ June 30, 2013

The Vermont Seed Capital Fund, LP is a \$5.1M for-profit, professionally managed, permanently revolving, early stage investment fund. Investors are the Vermont Center for Emerging Technologies (\$1M) and the Vermont Economic Development Authority (\$4.1M) as limited partners. The Fund Manager is the VCET Capital Corporation, a subsidiary of the non-profit Vermont Center for Emerging Technologies (VCET).

Four principal operating and investment objectives guide our investments over a 10-year Fund horizon: Financial Return, Capital Leverage, Jobs Impacted, and Innovation Ecosystem Benefits.

<p><b>Financial Return (IRR)<sup>1</sup></b></p> <p>Target IRR &gt; 20% Cumulative IRR -7.98%</p> <p>Absent an early year investment exits, positive IRR returns not anticipated until after year 5 and typical of the “J Curve” timing effect when investments start to return capital and gains to offset losses and expenses.</p>	<p><b>Jobs Impacted</b></p> <p>Target &gt; 150 (Permanent FTE) Actual 75 Cumulative<sup>2</sup> 202</p> <p>Early stage firms can be expected to experience employment volatility associated with capital, revenues earned, and cash flows over time.</p>
<p><b>Capital Leverage</b></p> <p>Total VSCF Investment (12) \$1,884,544 Total Capital Investment \$21,510,194 Leverage 11.4x</p> <p>As of November 30th, Fund has invested \$2,207,462</p>	<p><b>Innovation Ecosystem Benefits</b></p> <p>4 downtowns, multiple higher education licensees, multiple internships and hiring. A world class network of mentors, board members, domain experts, strategic partners and institutional venture investors are being utilized in support of portfolio firms. Momentum builds!</p>
<p><b>Total Revenue</b></p> <p>Actual (LTM<sup>3</sup>) \$7,371,031 Cumulative \$16,707,331</p>	<p><b>Total Payroll</b></p> <p>Actual (LTM<sup>3</sup>) \$3,875,369 Cumulative \$10,321,723</p>
<p><b>Vermont Coverage</b></p> <p>White River Junction, Richmond, Woodstock, Middlebury, Winooski, Burlington, Montpelier, Colchester, S. Ryegate, St. Johnsbury, Barre, Waitsfield</p>	<p><b>Investment Roadmap (first revolve)</b></p> <p>Target # Firms 17 Actual # Firms 12</p> <p>As of November 30th, Fund has invested into 13 firms.</p>

<sup>1</sup> IRR : Internal rate of return is the standard Fund financial performance measure of cash outflows and cash inflows adjusted for timing. Funds investing are typically negative in early years (1-5) and then anticipate positive returns in years 5-10 upon realized gains from remaining portfolio investments. This effect is also referred to as the J Curve in the venture fund industry.

<sup>2</sup> Job-years: This seeks to represent the cumulative Job years in portfolio companies as reported by firms annually.

<sup>3</sup> LTM: Last twelve months.

Vermont Seed Capital Fund, LP



**12**   
Investments



**Talent Cloud**



**\$22 Million Capital Raised**

**11.4X** Capital Leverage



**202**



Cumulative Job-Years

**\$17 Million Cumulative Revenue**



**\$10 Million Cumulative Payroll**





# PORTFOLIO COMPANIES @ JUNE 30, 2013



## Sound Innovations

Location	White River Junction, VT
Fund Investment	\$150,000
Date of Investment	5.18.10

**Description** Sound Innovations (SI) offers an Active Noise Reduction (ANR) technology platform for headsets, ear plugs and communication systems serving military, industrial, commercial and consumer markets.

**Use of Funds** Working Capital, Payroll, R&D, and S&M

**Status** Active



## Green Mountain Digital

Location	Woodstock, VT
Fund Investment	\$150,000 ; \$30,000 ; \$20,000
Date of Investment	9.22.10 ; 2.15.12 ; 3.6.13

**Description** Green Mountain Digital is an innovative digital media publisher and the mobile apps market leader in nature and wildlife. The company designs and publishes authoritative and comprehensive mobile applications that work to engage users with the natural world around them. Download Yonder.it today and Get Outdoors!

**Use of Funds** Working Capital, Content, IT, Payroll, Production and S&M

**Status** Active



## SemiProbe

Location	Winooski, VT
Fund Investment	\$250,000
Date of Investment	12.20.10

**Description** SemiProbe designs and manufactures the most innovative probing, inspection and test semiconductor solutions available today. Customers include the top foundries, research centers and corporations in the world.

**Use of Funds** Working capital, payroll, IT development, facility and S&M

**Status** Active



## Aprexis

Location	Montpelier, VT
Fund Investment	\$200,000
Date of Investment	1.25.11

**Description** Aprexis Health Solutions empowers pharmacist with tools to increase medication adherence among patients. The easy to use, web-based software revolutionizes delivery of personalized medication therapy management (MTM) and patient-centric clinical services while increasing revenues for pharmacies.

**Use of Funds** Working capital, payroll, SaaS platform, customer services, and business development.

**Status** Active



## Vtrim Online

Location	Middlebury, VT
Fund Investment	\$150,000 ; \$25,000
Date of Investment	9.6.11 ; 4.27.12

**Description** Vtrim Online offers healthy weight management programs based on research by Dr. Jean Harvey-Berino at the University of Vermont.

**Use of Funds** Working capital, personnel, sales, product development, and marketing

**Status** Active



## ElectroCell

Location	Colchester, VT
Fund Investment	\$99,544
Date of Investment	12.30.11

**Description** ElectroCell provides liquid waste treatment services to livestock farms, municipal wastewater treatment plants and industrial customers. Its bioelectric treatment uses precisely managed electrical pulses to open organic cells with breakthrough efficiency.

**Use of Funds** Working capital, personnel, pilot projects, equipment, and sales

**Status** **Active**



## BuysideFX

Location	Burlington, London, Boston
Fund Investment	\$100,000
Date of Investment	5.16.12

**Description** BuysideFX introduces 3rd party trading desk services for institutional investors in the world's biggest market, the \$4-5 trillion DAILY foreign exchange market.

**Use of Funds** Working capital, personnel, product development and business development

**Status** **Active**



## Pwnie Express

Location	Berlin, Austin, and Boston
Fund Investment	\$200,000
Date of Investment	10.11.12

**Description** Pwnie Express is the premier global provider of innovative, cost effective, rapid deployment penetration testing products. Their products have been incorporated into the cyber-security toolboxes of over one thousand security service providers, Fortune 500 companies and various federal agencies.

**Use of Funds** Working capital, personnel, product development and business development

**Status** **Active**



## Northern Reliability

Location	Waitsfield, VT
Fund Investment	\$150,000
Date of Investment	04.01.13

<b>Description</b>	As remote and back-up power experts, Northern Reliability offers premium stand-alone power systems providing solutions for customers needing a reliable energy source for their business or community, no matter the location or environment.
<b>Use of Funds</b>	Working capital, personnel, product development and business development
<b>Status</b>	<b>Active</b>

### Realized Losses:

During FY13, three of the Fund's twelve portfolio companies ceased operating for a variety of factors. These companies and teams worked tirelessly towards finding a sustainable business model. While these risk takers did not reach their lofty goals, the work and impacts of the employees, founders and investors nevertheless contributed to Vermont's start-up ecosystem.

### Summary Data (3 Firms)

Total Fund Investment:	\$360,000
Cumulative Capital Raised:	\$5,124,750
Leverage:	14.2
Cumulative Wages Paid:	\$1,255,738
Cumulative Revenues:	\$262,344

### True Body Products

Fund Investment	\$50,000 ; \$10,000
Date of Investment	Jul 9 2010 ; Aug 8 2011

### eCorp English

Fund Investment	\$200,000
Date of Investment	Oct 22 2010

### Thermal Storage Solutions

Fund Investment	\$75,000 ; \$25,000
Date of Investment	Feb 22 2011 ; Nov 7 2011

