

Kentucky Innovation Fund Thesis

May, 2019

The KY Innovation Fund represents the relaunch of the Kentucky Enterprise Fund. At the direction of KY Innovation in the Cabinet for Economic Development, the Commonwealth Commercialization Center (C3) will be charged with the administration of the investment programs set forth by the Kentucky Innovation Act. As defined in the Kentucky Innovation Act, these programs are as follows:

- The Kentucky Enterprise Fund – an investment vehicle established with the purpose of enabling small or medium-size, Kentucky-based companies to undertake feasibility, concept development, research and development, or commercialization work in partnership with colleges and universities in the Commonwealth.
- The Kentucky Rural Innovation Fund – an investment vehicle established with the purpose of enabling small, rural Kentucky-based firms to undertake research and development, and entrepreneurial innovation work in partnership with postsecondary institutions in the Commonwealth.
- The Kentucky Commercialization Fund – an investment vehicle established to provide funding for the development and commercialization of promising technologies at and emerging from colleges and universities in the Commonwealth.

Legislation states that funds were allocated to these initiatives with the belief that the general welfare and material well-being of the citizens of the Commonwealth depends on immediate action to develop a strong, entrepreneurial economy characterized by knowledge, innovation, and speed and that it is in the best interest of the Commonwealth to promote research, innovation, and high-technology enterprises that utilize the higher-order skills of an educated workforce. Within C3, the KY Innovation Fund will work to achieve these aims through combined administration of all three of the programs described above. These programs will function in accordance to the guidelines provided in the Kentucky Innovation Act. Those guidelines are as follows:

- The Kentucky Enterprise Fund – The Kentucky Enterprise Fund shall make financial assistance available to qualified companies in accordance with the following guidelines:
 - Grants or warrants of up to **\$30,000** for companies exploring the feasibility of technology commercialization.
 - Funding of up to **\$250,000** for companies in the concept development phase of technology commercialization.
 - Funding of up to **\$500,000** for companies in post-initialization but before full commercialization.
 - Funding of up to **\$750,000** for companies with high growth potential and a clear path to commercialization.
- The Kentucky Rural Innovation Fund – Project funding in the Kentucky Rural Innovation Fund will be guided by the following parameters:
 - Award funds shall be used as seed funding
 - The amount of a fund award to a qualified company shall not exceed **\$50,000** each year for a two years, equal to a maximum of **\$100,000**.
- The Kentucky Commercialization Fund – Project funding in the Kentucky Commercialization Fund program will follow these guidelines:
 - The maximum amount of funding for a project award under the Kentucky Commercialization Fund shall not exceed **\$75,000** each year up to two years, equal to a maximum of **\$150,000**.

- The University of Kentucky and the University of Louisville shall be awarded together no more than 70% of fund awards.

These are the statutory guidelines as they currently stand, however, they are subject to change based upon adjustments advised by the Kentucky Cabinet for Economic Development and KY Innovation during the upcoming legislative session.

The day-to-day operations of the KY Innovation Fund will be managed by a dedicated staff comprised of a Fund Manager and up to two Associate/Analyst positions. These members of the KEF team will be responsible for community outreach, relationship management, investment due diligence and the general operations of the Innovation Fund.

In order to reinforce the fidelity of the investment process, the Innovation Fund will also contract with a to-be-determined third-party professional advisory. This group will assist in the diligence process and make investment recommendations based upon investments they feel have the greatest potential to achieve the desired return of the Fund while effectively meeting the requirements set forth in the Kentucky Innovation Act.

For further assurance that investments are being made with appropriate diligence and in alignment with state strategy and public benefit, all investment recommendations will be vetted and approved by the C3 investment committee, which consists of professionals from both the public and private sectors with a history of investing in and/or managing innovation driven enterprises.

Investments made by the KY Innovation Fund will come in three forms – direct equity investments, fund of funds investments, and grants/warrants.

- Direct equity investments will be made based on the investment recommendations originated through the Innovation Fund investment process described above. Furthermore, in order to create appropriate separation between the state government and investment decisions made by the Fund, a portion of funds will be dedicated to a “rules-based” co-investment strategy. This will be structured such that the C3 establishes relationships with various investment funds/groups throughout the state and dedicates a portion of its capital to invest alongside those funds/groups based on pre-determined rules.
- As with direct equity investments, fund of funds investments will be based on the investment recommendations originated through the C3 investment process. This strategy will aid in providing the Innovation Fund with broad diversification early in the life of the fund, and will also work to support the Commonwealth’s existing pools of capital. This strategy also aims to provide additional separation between the Commonwealth and the companies that receive Innovation Fund investments. The CED and KY Innovation’s desired outcome for the Fund is to provide broad support for Kentucky’s entrepreneurial ecosystem, not to pick and choose corporate winners.
- Grants or warrants will be made available to companies in the earliest stages of the commercialization process. The flexibility of this type of funding will be approached as an investment in developing a commercialization driven culture in Kentucky.

Per the statutory guidelines, the KY Innovation Fund may receive state appropriations, gifts, grants, federal funds, revolving funds, and any other funds both public and private. Any income earned from the investments along with the unencumbered balances in the fund shall not lapse, and shall be deemed a trust and agency account and made available solely for the purposes and benefits of the Innovation program. This revolution of funds allows for the Innovation Fund administrators to take a long-term view, with the goal of supporting substantial and sustainable growth in Kentucky’s entrepreneurial ecosystem.