



Audit Report



OIG-17-058

STATE SMALL BUSINESS CREDIT INITIATIVE

New Hampshire's Use of Federal Funds for the Borealis Granite Fund, LP

September 28, 2017

Office of
Inspector General

Department of the Treasury

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Abbreviations

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| Act | Small Business Jobs Act of 2010 |
| BGF | Borealis Granite Fund, LP |
| Borealis | Borealis Capital Partners III, LLC |
| DRED | New Hampshire Department of Resources and Economic Development |
| Fund | Venture Capital Fund |
| NHDBEA | New Hampshire Department of Business and Economic Affairs |
| NHBFA | New Hampshire Business Finance Authority |
| OIG | Office of Inspector General |
| SSBCI | State Small Business Credit Initiative |
| Treasury | Department of the Treasury |

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*The Department of the Treasury
Office of Inspector General*

September 28, 2017

Kipp Kranbuhl
Deputy Assistant Secretary for Small Business, Community
Development, and Housing

As part of our ongoing oversight of the Department of the Treasury's (Treasury) State Small Business Credit Initiative (SSBCI), authorized by the Small Business Jobs Act of 2010 (the Act),¹ we conducted audits of awards made to select States, Territories, and eligible Municipalities (hereinafter referred to as States) to support their capital access and small business credit programs. The purpose of these audits was to assess States' compliance with SSBCI program requirements and prohibitions to identify any reckless² or intentional³ misuse of funds. Regarding SSBCI funds awarded to the State of New Hampshire, our audit focused on the State's compliance with respect to funds invested in its venture capital program, the Venture Capital Fund (Fund).

In this report, we provide our assessment of the Fund's venture capital fund, Borealis Granite Fund, LP (BGF), which invested approximately \$1.3 million⁴ of SSBCI funds between January 22, 2013 and June 19, 2014. Appendix 1 provides more detail of our audit objective, scope, and methodology.

¹ Pub. L. 111-240, 124 Stat. 2568-2582 (September 27, 2010).

² Reckless misuse as defined by Treasury is a use of Allocated Funds that the Participating State or its administering entity/ies should have known was unauthorized or prohibited. A "reckless misuse of funds" is a highly unreasonable departure or willful disregard from the standards of ordinary care, and may be a single instance or a series of instances.

³ Intentional misuse as defined by Treasury is a use of Allocated Funds that the Participating State and/or its administering entity/ies knew was unauthorized or prohibited. An "intentional misuse of funds" may be a single instance or a series of instances.

⁴ Actual amount is \$1,347,258.

In brief, we found that BGF generally complied with the SSBCI program requirements and prohibitions governing venture capital programs. As such, we make no recommendation in this report.

As part of our reporting process, we provided the New Hampshire Department of Business and Economic Affairs (NHDBEA) management an opportunity to comment on a draft of this report. In its response, NHDBEA stated that it and the contract entity, the New Hampshire Business Finance Authority (NHBFA), agreed with the report in that all requisite rules and regulations were followed by the relevant entities. NHDBEA management's response, in its entirety, is included as appendix 2 to this report.

In its written response to this report, Treasury management stated it was pleased the report found that BGF generally complied with SSBCI program requirements. Treasury management's response, in its entirety, is included as appendix 3 to this report.

Background

SSBCI is a \$1.5 billion Treasury program that provides participating States funding to strengthen capital access programs and other credit support programs that provide financial assistance to small businesses and manufacturers. Capital access programs provide portfolio insurance for business loans based on a separate loan loss reserve fund for each participating financial institution. Other credit support programs include collateral support, loan participation, loan guarantee, credit support, and venture capital programs.

Loans and investments made with SSBCI funds must comply with the program requirements detailed in the Act, *SSBCI Policy Guidelines*, the *SSBCI National Standards for Compliance and Oversight*, and the *Allocation Agreement*. With respect to venture capital programs, investments must have at least 20 percent private capital at risk at the time the investments are made. Venture capital programs must target loans or investments with an average principal of \$5 million or less. The programs cannot extend credit for loans with principal amounts in excess of \$20 million nor participate in an investment instrument in which the resulting equity investment is in excess of \$20 million. Also, program

requirements prohibit the investment of SSBCI funds in related party interests. The Deputy Assistant Secretary for Small Business, Community Development, and Housing administers the SSBCI program. Details of the program are provided as appendix 4.

New Hampshire's Participation in SSBCI

The State of New Hampshire was awarded approximately \$13.2 million⁵ of SSBCI funds upon Treasury's approval of its participation in the program in July 2011. The *Allocation Agreement*, among other things, authorized the use of SSBCI funds for the following four State approved programs: Aid to Local Development Organizations, Capital Access Program, Collateral Shortfall Program, Loan Guarantee Reserves, and the Fund. As of December 31, 2016, Treasury disbursed all \$13.2 million to New Hampshire, which in turn, obligated or spent all of the SSBCI funds. The State designated the New Hampshire Department of Resources and Economic Development (DRED)⁶ to administer the approved State programs on behalf of the Office of the Governor.

Audit Results

Borealis Granite Fund, LP Generally Complied with SSBCI Program Requirements and Prohibitions

We found that BGF generally complied with SSBCI program requirements and prohibitions governing venture capital programs. DRED contracted with NHBFA, a public instrumentality,⁷ to administer its SSBCI programs. NHBFA entered into a limited partnership agreement with Borealis Capital Partners III, LLC (Borealis) to form BGF. As the limited partner, NHBFA was primarily responsible for making a capital contribution to BGF to invest in beneficiary companies. As the general partner, Borealis

⁵ Actual amount is \$13,168,350.

⁶ In July 2017, NHDBEA replaced DRED as administrator of New Hampshire's SSBCI programs.

⁷ According to the 2006 New Hampshire Statutes - Section 162-A:3, Authority Created, NHBFA is deemed to be a public instrumentality and the exercise by the authority of the powers conferred upon it by the legislature shall be deemed and held to be the performance of public and essential governmental functions of the State.

was responsible for, among other things, purchasing securities in beneficiary companies. As such, BGF made 11 investments totaling approximately \$1.3 million of SSBCI funds in 7 beneficiary companies between January 22, 2013 and June 19, 2014.

We tested all 11 investments and found that at least 20 percent private capital was at risk at the time the investments were made. Furthermore, the investments did not exceed the maximum dollar amount of \$20 million. Our testing did not identify any prohibited use of SSBCI funds or related party interests. As such, we make no recommendations.

* * * * *

We would like to extend our appreciation for the cooperation and courtesies extended to our staff during the audit. Major contributors to this report are listed in appendix 5. A distribution list for this report is provided as appendix 6. If you have any questions, please contact me at (202) 927-1011.

/s/

Theresa Cameron
Audit Director, Financial Assistance Programs

Pursuant to Section 3003 of the *Small Business Jobs Act of 2010* (the Act), we conducted audits of awards made to select States, Territories, and eligible Municipalities (hereinafter referred to as States) as part of our ongoing oversight of the Department of the Treasury's (Treasury) State Small Business Credit Initiative (SSBCI), authorized by the Act, to support their capital access and small business credit programs. The objective of these audits was to assess States' compliance with SSBCI program requirements and prohibitions to identify any reckless or intentional misuse of funds. Regarding SSBCI funds awarded to the State of New Hampshire, our audit focused on the State's compliance with respect to funds invested in its venture capital program, the Venture Capital Fund (Fund).

Of the \$13,168,350 in SSBCI funds allocated to New Hampshire, \$2,489,382 was invested in the Fund as of December 31, 2016. Of the amount invested, our audit scope comprised of 11 investments totaling \$1,347,258 made by the Borealis Granite Fund, LP (BGF) between January 22, 2013 and June 19, 2014. The remaining \$1,142,124 of SSBCI funds invested in the Fund after June 2014 were not within the scope of this audit, and therefore, not included in our testing.

To accomplish our objective, we performed the following steps.

- We reviewed the following documents:
 - Small Business Jobs Act of 2010 (Public Law 111-240; September 27, 2010);
 - *SSBCI National Standards for Compliance and Oversight* (May 15, 2012 and January 23, 2014);
 - *SSBCI Policy Guidelines* (October 21, 2011);
 - SSBCI Frequently Asked Questions;
 - SSBCI Fact Sheet;
 - *State of New Hampshire SSBCI Allocation Agreement for Participating States*;
 - *SSBCI Application* by the State of New Hampshire;
 - Borealis Granite Fund, LP limited partnership agreement;
 - Beneficiary capitalization tables and stock purchase agreements;
 - SSBCI Quarterly Reports;

- SSBCI Annual Reports (2012, 2013, and 2014); and
 - SSBCI Investee and Investor Certifications.
- We tested documentation supporting the 11 investments made by BGF to determine:
 - at least 20 percent capital was at risk for each investment;
 - each investment was not greater than \$20 million;
 - investee and investor certifications were obtained prior to the investment; and
 - no conflicts of interest existed between the investor and beneficiary company.
 - We also reviewed the Sex Offender Registry for New Hampshire to verify that no principal of the beneficiary companies was convicted of a sex offense against a minor (as such terms are defined in section 111 of the Sex Offender Registration and Notification Act (42 U.S.C. 16911)).
 - We interviewed key officials at New Hampshire Business Finance Authority and Treasury's SSBCI program office; and reviewed correspondence from BGF.

We conducted fieldwork at the Treasury Office of Inspector General office in Washington, D.C., between August 2014 and August 2017.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Appendix 2
New Hampshire Department of Business and Economic Affairs Management
Response



STATE OF NEW HAMPSHIRE
DEPARTMENT of BUSINESS and ECONOMIC AFFAIRS
DIVISION of ECONOMIC DEVELOPMENT

172 Pembroke Road Concord, New Hampshire 03301
Phone: 603-271-2341 www.nheconomy.com

September 12, 2017

U.S. Department of the Treasury
Office of Inspector General
Office of Audit
875 15th Street NW
Washington, DC 20005
Attention Theresa Cameron, Audit Director

Re: NH SSBCI Exit Interview

Dear Ms. Cameron:

On behalf of the State of New Hampshire, I would like to thank you for the opportunity to review the Office of Inspector General's (OIG) draft report entitled "Audit of New Hampshire's Use of Federal Funds for the Borealis Granite Fund, LP".

New Hampshire's Department of Business and Economic Affairs, as well as the contract entity, the New Hampshire Business Finance Authority, agrees with the report that states all requisite rules and regulations were followed by the relevant entities.

On behalf of the entire State of New Hampshire, I would like to thank the US Treasury for providing assistance and guidance during our deployment of SSBCI funds. The economic impact of this program has significantly contributed to our state's well-being, providing access to capital for scores of new and existing businesses. We look forward to continuing to use SSBCI funds to drive our state's growth in the future.

Kind regards,

A handwritten signature in black ink, appearing to read "Taylor Caswell".

Taylor Caswell
Commissioner
NH Department of Business and Economic Affairs

Cc: J. Key-Wallace, BFA

Appendix 3
Treasury Management Response



DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

September 22, 2017

Theresa Cameron
Department of the Treasury
Office of Inspector General
875 15th Street, NW
Washington, DC 20005

Dear Ms. Cameron:

Thank you for the opportunity to review the Office of the Inspector General's (OIG) draft report regarding New Hampshire's use of SSBCI funds in the Borealis Granite Fund, LP (the Report). This letter provides the official response of the Department of Treasury (Treasury). We are pleased with the Report's finding that the Borealis Granite Fund, LP generally complied with SSBCI program requirements.

It is our understanding that OIG transmitted a copy of the Report to New Hampshire program officials, and they provided you with a response.

Treasury appreciates our work together throughout the course of the SSBCI program.

Sincerely,

A handwritten signature in black ink, appearing to read "Kipp Kranbuhl".

Kipp Kranbuhl
Deputy Assistant Secretary for Small Business,
Community Development, and Housing

cc: Katherine Reilly, Office of General Counsel, Banking and Finance
Jeff Stout, Director of the State Small Business Credit Initiative

Under the State Small Business Credit Initiative (SSBCI), States were allocated funds based on formulas that measured the States' unemployment rates between 2007 and 2009. The Department of the Treasury (Treasury) disbursed SSBCI funds allocated to each participating State in three increments referred to as tranches. The first tranche was disbursed upon Treasury's approval for participation in the SSBCI program. Disbursements of the second and third tranches were dependent upon the participating State's certification that it had obligated, transferred, or spent at least 80 percent of the previous tranche and had complied with all applicable program requirements.

Each participating State was required to designate specific departments, agencies, or political subdivisions to administer the funding. The designated entity could distribute SSBCI funds to public and private institutions, which may include a subdivision of another State, a for-profit entity supervised by the State, or a non-profit entity supervised by the State. These entities were to use funds to make loans or provide credit access to small businesses.

Primary oversight of the use of SSBCI funds is the responsibility of each State's designated entity. To ensure that funds are properly controlled and expended, the Small Business Jobs Act of 2010 required that Treasury execute an Allocation Agreement with participants setting forth internal controls and compliance and reporting requirements before receiving SSBCI funds.

Appendix 5
Major Contributors to This Report

Nadine Forgenie, Audit Manager
Dennis Orsini, Auditor
Anne Ryer, Referencer

Department of the Treasury

Deputy Secretary
Deputy Assistant Secretary for Small Business, Community
Development, and Housing
Office of Strategic Planning and Performance Improvement
Office of the Deputy Chief Financial Officer, Risk and Control
Group

Office of Management and Budget

OIG Budget Examiner

New Hampshire Department of Business and Economic Affairs

Commissioner

United States Senate

Committee on Agriculture, Nutrition, and Forestry
Committee on Appropriations
Committee on Banking, Housing, and Urban Affairs
Committee on the Budget
Committee on Finance
Committee on Small Business and Entrepreneurship

United States House of Representatives

Committee on Agriculture
Committee on Appropriations
Committee on the Budget
Financial Services Committee
Small Business Committee
Committee on Ways and Means



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<http://www.treasury.gov/about/organizational-structure/ig/Pages/default.aspx>

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Gulf Coast Restoration Hotline – Call toll free: 1-855-584.GULF (4853)

Email: Hotline@oig.treas.gov

Submit a complaint using our online form:

<https://www.treasury.gov/about/organizational-structure/ig/Pages/OigOnlineHotlineForm.aspx>