



Memorandum

TO: COMMUNITY AND
ECONOMIC DEVELOPMENT
COMMITTEE

FROM: Paul Krutko

SUBJECT: CATALYST PROGRAM

DATE: April 18, 2007

On November 14, 2006, City Council authorized the City Manager to negotiate and execute an Investment Management Agreement with Pacific Community Management, Inc., Pacific Community Ventures' wholly owned subsidiary, to provide investment management services for the City's Economic Development Catalyst Program (EDCP). Pacific Community Ventures, a community development venture capital firm, was selected to manage the EDCP through an RFP process conducted earlier in 2006. The City executed the Investment Management Agreement with Pacific Community Management (PCM) in January 2007.

The City will provide up to \$3 million over the next four years to leverage substantial venture capital investment in private San Jose small businesses. PCM will match every City dollar invested through the EDCP with a minimum of \$5.70 from PCM and other co-investors. In addition to increasing the direct impact of City funds, the EDCP is anticipated to make equity investments that will enhance job creation, expand the local tax base, and facilitate the integration of other programs and services targeted to the small business community.

Although the City did not require a specific focus on hiring and training low- and moderate-income individuals, PCM's mission supports the identification of small businesses that will provide training, benefits, and profit-sharing opportunities for these employees. Over the 10-year term of the Agreement, PCM will recommend, perform due diligence, and facilitate investments in high potential small businesses with: (1) positive cash flow, (2) annual revenues of at least \$3 million, (3) a strong management team in place, and (4) a clear path toward growth and increased profitability. It is anticipated that the EDCP will be fully funded over the first 4 years of the Agreement with PCM.

The City met with PCM on April 17, 2007 to develop the EDCP Investment Plan for the next 12 months. At this meeting, OED staff and PCM discussed the contemplated level of program investment activity and the City's evaluation of PCM's investment management performance to date.

First EDCP Investment

For the inaugural EDCP investment, PCM has provided the City with an Investment Notice regarding a \$350,000 preferred stock investment in BenteK, a low-volume, high-complexity manufacturer whose services include engineering, design, and supply chain management. The leverage ratio for this investment is 6.7:1. Among the City's co-investors are JP Morgan's Bay

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Area Equity Fund, Fundamental Capital, and Medford Investments. The Bentek investment is a second-round infusion of capital to support the company in meeting its sales requirements for its second-best quarter ever.

OED staff, with the assistance of the City Attorney's Office and external counsel, reviewed the Investment Notice, the Securities Purchase Agreement, and the Investors' Rights Agreement, and subsequently provided a recommendation to the City Manager to move forward with a preferred stock investment in Bentek. The first EDCP investment is anticipated to close within the next two weeks.

PAUL KRUTKO
Chief Development Officer
City Manager's Office