

DoD and SBA Approve First Set of Critical Technology SBICs

November 12, 2024

On October 22, 2024, [the Department of Defense \(DoD\) and the Small Business Administration \(SBA\) announced approval](#) of 13 inaugural small business investment company (SBIC) licensees and so-called green light approved investment funds pursuant to the Small Business Investment Company Critical Technology (SBICCT) Initiative. The DoD anticipates that this first cohort of investor fund participants will invest nearly \$3 billion in more than a thousand portfolio companies that operate in one or more of 14 “critical technology” areas that the DoD has identified and grouped into three categories:

- Seed areas of emerging opportunity – biotechnology, quantum science, future-generation wireless technology and advanced materials
- Effective adoption areas – trusted artificial intelligence (AI) and autonomy, integrated network systems of systems, microelectronics, space technology, renewable energy generation and storage, advanced computing and software, and human-machine interfaces
- Defense-specific areas – directed energy, hypersonics, and integrated sensing and cyber

The DoD and SBA jointly launched the SBICCT Initiative last year to increase private investment in critical technologies considered vital to domestic national and economic security, including at the component level and production processes. The initiative – run out of the DoD’s Office of Strategic Capital (OSC) and the SBA’s Office of Investment Innovation (OII) – issued an [Investment Policy Statement](#) stating that, “[b]y providing capital and technology sector guidance, the SBICCT Initiative aims to empower highly qualified investors to scale public-private partnered capital and catalyze investment in critical technology areas.”

The SBICCT Initiative leverages the SBA’s existing SBIC program authorities to provide low-cost capital guaranteed by the government to SBIC funds demonstrating an investment strategy whereby at least 60% of total capital deployments will be into markets aligned with the DoD’s identified critical technology areas.

Approval involves a formal application and a thorough underwriting and due diligence process, which includes technical, financial and national security considerations. Applicants must establish a track record of advancing early-stage companies and scaling emerging technologies.

Participating investors may include established venture capital investors with expertise in sectors related to the critical technology areas, family offices that have pursued venture or private equity early- or growth-stage critical technology investments, venture debt investors with fund backing and historical success in critical technology-related sectors, and potentially private growth equity investors with relevant experience. The investment funds participating in the SBICCT Initiative contemplate investing across a variety of asset classes – including direct lending, seed, venture, growth, fund of funds, buyout and special situations. Once the SBA administrator gives final approval for an applicant fund to begin raising private capital as an SBIC, the fund is considered a “green light approved” investor pre-qualified for an SBIC license and progresses toward final licensing, which is contingent upon final diligence. The SBA granted the first SBICCT Initiative license in early July 2024.

Licensed funds can obtain SBA-guaranteed loans of up to \$175 million each to enhance investment returns at the fund level. The DoD also will provide access to program-related support designed to help participating funds drive value in implementing their

investment strategies. Such support will include access to technical experts, cybersecurity offerings from the National Security Agency to help protect critical technologies, consideration for security clearances as necessary to enable the development of critical technologies, and cooperative research and development agreements (CRADAs) or similar agreements with the DoD to facilitate research, development and information sharing among the DoD, investment funds and portfolio companies.

Companies seeking to receive SBIC investments also must meet a variety of eligibility requirements on top of the industry focus for this particular initiative – including that the prospective portfolio company must be a small business and must not be a re-lender or re-investor, passive business or substantially foreign operation, among other things, as detailed in the applicable SBIC regulations (13 CFR, part 107).

The SBICCT Initiative targets identified gaps in access to capital and stands to help bolster the domestic industrial base. The overarching goals of the initiative include protecting the nation's competitive advantage on the global stage by strengthening supply chains and driving the development and commercialization of critical technologies.

This initiative complements similar, recent efforts by venture capital and private equity firms, outside of the SBIC program, to invest in defense tech and other national security-focused companies, as well as efforts by the government to provide viable domestic alternatives to foreign capital for US companies, thereby limiting foreign access to sensitive technologies. Indicative of the latter, in addition to the statutory and regulatory requirements of the SBIC program and the SBA that are applicable to all SBIC licensees and companies eligible for SBIC financing, the SBICCT Initiative imposes certain additional initiative-specific restrictions, such as:

1. SBICCT Initiative licensees may not raise capital from investors from countries that the Department of State has identified as being of particular concern. This currently includes Burma, the People's Republic of China, Cuba, Eritrea, Iran, the Democratic People's Republic of Korea, Nicaragua, Pakistan, Russia, Saudi Arabia, Tajikistan and Turkmenistan.
2. Citizens of countries of special concern cannot own, control, or be associated or affiliated with the licensee.
3. Licensees are prohibited from making investments into companies where individual citizens of or entities located in a country of special concern exercise ownership, control or influence, or hold a majority of the economic interest.

Nevertheless, because the term "critical technology" is a key concept in the Committee on Foreign Investment in the United States (CFIUS) regulations governing foreign investments in US businesses, investor participants should carefully assess the potential CFIUS implications of investments in portfolio companies with critical technology.

To date, more than 100 funds have expressed interest in the SBICCT Initiative. The program accepts applications during quarterly windows, and the next filing deadline is November 15, 2024.

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