Approved 04/06/87
Date

MINUTES OF THE HOUSE COMMITTEE ON ECONOMIC DEVELOPMENT.

The meeting was called to order by Phil Kline at
Chairperson

3:30 a.m./p.m. on Thursday, March 26, 1987 in room 423S of the Capitol.

All members were present except: Representatives Mainey and Sader (Excused)

Committee staff present:
Jim Wilson, Revisor
Lynn Holt, Research
Molly Mulloy, Secretary

Conferees appearing before the committee:

Senator David Kerr
David Barclay, Department of Commerce
Mark Burghart, Department of Revenue

Chairman Kline called the meeting to order and introduced Senator David Kerr.

Senator Kerr briefed the committee on both S.B. 67 and S.B. 243. He said S.B. 67 makes it possible for two major sources of investment capital to make use of tax credits which were passed last year. These sources are (1) out of state investors, since they have no Kansas tax liability and (2) parties who are presently untaxed by Kansas tax laws (such as profit sharing and pension funds, who have $1.3 billion to invest, not counting KPERS). Sen. Kerr added that as the law is presently written, it was highly unlikely these two sources would make use of it. Another change with S.B. 67 is that it allows investors who have no Kansas tax liability to transfer their credits to someone who does have a liability. A restriction is that the credit may only be transferred once and must be transferred in total.

Sen. Kerr said that S.B. 243 makes venture capital statutes more useable by (1)defining what a cash investment s (2) eliminating the carryback for tax credits (3) allowing the credit to be offset against total tax liability for a given year (4) enabling insurance companies to receive tax credits for investments in Kansas venture capital companies and (5) allowing investors to reserve tax credits if they enter binding investment contracts after the mandated $1.5 million threshold has been reached. In response to a committee question, Sen. Kerr clarified that S.B. 67 and S.B. 243 relate only to investments in private venture capital companies in Kansas, and not to Kansas Venture Capital, Inc. (the banking fund). He noted that the 25% tax credit was intended to stimulate investments in venture capital companies because of the "risky" nature of the investment.

The second proponent on the two bills was David Barclay of the Department of Commerce. He stated that he supports the bills because they encourage more people to invest in Kansas venture capital companies. Mr. Barclay stated that when you invest cash in a venture capital company, it's not the same as buying stock. It is actually less risky because the investor gets a 25% tax credit. He noted that when the Department of COmmerce certifies venture capital companies, they must have $1.5 million in cash investments in the company as the law now stands. But changes in S.B. 243 provide that part of the $1.5 million can include a binding agreement or pledge to invest at a future point.

Explaining the amendment beginning with line 0141, Mr. Barclay said the amendment allows venture capital companies to ask investors to make an equal investment in this calendar year and an equal amount in the next year. Under the current law, investors would just get credit for the first year's investment. Under the amended bill, investors would be allowed to get a tax credit based on their pledge for the second year. The advantage of this is that it encourages people to commit their money now. He added that such "staged investments" are standard industry practice. He noted that, on the other hand, this does not help the goal of investing cash in venture capital companies because of the cap of $6 million on available credit. Because of the cap, if people are allowed to earmark part of that cap on future committed funds, we will run out of tax credits and other venture capital companies will not be able to get started. Referring to a list of venture capital funds which are interested in qualifying their investors for the income tax credits (Attachment 1), he noted that the Department of Commerce has been approached by various companies and said that the estimated tax credits already exceed $10 million. He noted that if the "cap" were not there, the reservation of credit would not be a problem. In answer to questions from the committee, he stated that the $6 million figure for the cap had been an arbitrary figure at the time it was decided. Mr. Barclay also said that although the Department of Commerce supports both bills, they would prefer not to have reservation of credit.

Mark Burghart of the Department of Revenue was the last conferee on S.B. 67 and 243. He said that the Department of Revenue had no position on either bill. He added that initially, there were several concerns which were corrected by amendments made by the Senate. He commented that the Department of Revenue had asked for an amendment in S.B. 67, beginning with line 45, to help them keep track of credits. With S.B. 243, the Department of Revenue requested the stricken language in lines 71-97 and the additional language in lines 98-107.

After further questioning of the conferees by committee members, the hearing concluded. A handout prepared by David Barclay defining seed capital and venture capital companies was distributed to the committee (Attachment 2).

Minutes for meetings held on March 16, 17, 18 and at 12:30 on March 23 were approved.

The next meeting of the committee is scheduled for Monday, March 30. The meeting was adjourned at 4:35pm.

Date: 3/26/87 GUEST REGISTER

HOUSE

Committee on Economic Development

NAME	ORGANIZATION	ADDRESS
Stanley Sicilian	IPPBR-KU	Lawrence
MARK A. BURGHART	DEPT. OF REVENUE	TOPEKA
David Barclay	DOC	"
Jim Holt	Leg's Intern	"
James C. 'Pat' Thompson	Kansas Funds Management Group, Inc.	Box 1185 Hutchinson, Ks 67502
Sen. [illegible]	—	—
[illegible]	DEPT. OF COM. [illegible]	[illegible]

Possible Certifications for Tax Credits

The following information provides a listing of those venture capital funds which are interested in qualifying their investors for Kansas income tax credits.

Fund	Location	Date Expected	Expected Capitalization	Tax Credit
Kansas Venture Capital, Inc.	Topeka	4/87	$10,000,000[1]	$2,500,000
Capital Research Mgmt.Group[2]	Lawrence	12/86	$ 1,575,600	$ 393,900
R.A.B. Ventures, Inc	Overland Pk.	3/87	$ 2,000,000	$ 500,000
Kansas Capital Dev. Fund	Hutchinson	5/87	$ 6,000,000	$1,500,000
		5/88	$ 6,000,000	$1,500,000
Campbell-Becker #2	Lawrence	7/87	$ 5,000,000	$1,250,000
Central Systems Dev, Inc.	Wichita		$ 1,500,000	$ 375,000
Management Group	Wichita		$10,000,000	$2,500,000
Local Seed Capital Funds			unknown	unknown
TOTALS			$42,075,600	$10,518,900

1 Proposed legislation (1987 SB 70) would allow $1.5 million of current investment to be counted as new capitalization toward the $10 million required for State investment of $10 million. If it passes, this would mean that the tax credit would be 25 percent of $8.5 million or $2.125 million.

2 Certified as a Kansas venture capital company on December 9, 1986. This company was organized by Sam Campbell and Charles Becker of Lawrence.

Prepared by: Department of Commerce
3/3/87

Attachment 1
Barclay 2
3/26/87

STATE OF KANSAS

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Phone (913) 296-3481
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Mike Hayden, Governor

Harland E. Priddle, Secretary

M E M O R A N D U M

TO: House Economic Development Committee

FROM: David Barclay

RE: Seed Capital and Venture Capital Definitions

DATE: March 24, 1987

As requested, this memo describes the stages of a business' life and indicates when seed capital and venture capital are appropriate methods of financing. There are five stages listed. The first two -- pre-start and prototype development -- are appropriate for seed capital. Venture capital follows in the remaining stages.

Start-Up / Pre-Startup Stage

1. The business is not yet in operation.
2. The prototype is in blueprint form or is in the planning stage.
3. The business is at least three years from the break even point.
4. The business needs seed capital to build a prototype.
5. The management may be only the inventor.

Prototype Development Stage

1. A prototype is built but the business is not yet in operation.
2. The business is less than two years from a break even point.
3. Funds are needed to build productive capacity.

Commercialization Stage

1. The business is in operation.
2. The business will reach the break even point within a year.
3. Commercial interest has been generated in the product.
4. A management team is in place.
5. Funding is needed to fund losses, refine production and do marketing research.

Attachment 2
3/24/87

Expansion Stage

1. The business is at the break even point and ready to expand.
2. Funds are needed to purchase permanent working capital (i.e., inventory and receivables).
3. The company may encounter fast growth syndrome in which fast growth results in working capital shortages.

Acquisition Stage

1. The business has reached maturity.
2. The business is a candidate for purchase.