

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 Tuesday, March 31, 1987 in room 423S of the Capitol.

All members were present except: Chronister, Hassler and Miller (All Excused)

Committee staff present:

Jim Wilson, Revisor
Lynn Holt, Research
Molly Mulloy, Secretary

Conferees appearing before the committee:

Dr. Charles Kreider, Institute for Public Policy and Business Research, KU
David Barclay, Dept. of Commerce

S.B. 69

Chairman Kline called the meeting to order and introduced Dr. Chuck Kreider, who answered committee questions on this bill. He explained that the reference to having public funds in a senior position (line 57) means they have less risk than private funds, and that because the risk is lower, the rate of return is lower for public funds.

After further discussion, Rep. Heinemann moved to amend S.B. 69 by changing the word "shall" to "may" in line 61 so that the rate of return is negotiable. Rep. Weimer seconded the motion and the motion carried. Rep. Heinemann moved and Rep. Aylward seconded to pass the bill favorably, as amended. Motion carried.

S.B. 243

Rep. Gjerstad distributed three handouts: balloon amendments to S.B. 243 (Attachment 1), copies of p. 56 of the Economic Development Commission Report (Attachment 2) and a description of Decertification Procedures (Attachment 3). She said the amendments had been suggested by the Department of Commerce and explained them to the committee. Referring to Attachment 1, Rep. Gjerstad said the balloon on page 1 clarifies whether it's a high risk loan or type of near equity. On page 2, the Department of Commerce proposes to strike the definition of cash investment because venture investors traditionally deal strickly with cash. She said it's a policy question as to whether we want to have cash invested in venture capital companies or to permit some kind of debt instrument. She said the balloon on page 4 (deleting lines 0141-0155) involves another policy questions as to whether we want to give a credit for cash investment and give up the ability to have perhaps more cash available this year. Referring to the last page of the balloon and the handout on Decertification Procedures, Rep. Gjerstad said that currenrently there are four ways to be decertified, and that after the seventh year, investors do not have to repay credits. The Department of Commerce wanted to have language to clarify this. Rep. Gjerstand called on David Barclay, of the Department of Commerce, to address the committee.

Mr. Barclay said that the Decertification Procedures (Attachment 3) page is meant to be a conceptual amendment to S.B. 243, to be included with the bill. He said this referes to the last two pages on Attachment 1, which are from the same Act that S.B. 243 addresses, and relates to decertification procedures in the last section of the Act. He said that this conceptual amendment simply makes clear what the existing policy is because from reading the Act, the policy is not clear.

Rep. Gjerstad moved, and Rep. Aylward seconded, that the amendments be adopted. The motion carried. Rep. Aylward moved, and Rep. Moonaw seconded, that the bill be passed favorably, as amended. The motion carried.

S.B. 209

Rep. Leach moved for an amendment which would leave the bill intact except for divid-ing the second \$100,000 in the bill according to the following formula: \$25,000 to the Board of Agriculture's Marketing Division, \$25,000 to the Department of Commerce Trade Division and \$50,000 in the General Fund in tax years 1988 and again in 1989.

CONTINUATION SHEET

MINUTES OF THE HOUSE COMMITTEE ON ECONOMIC DEVELOPMENT,
room 423S, Statehouse, at 3:30 a.m./p.m. on Tuesday, March 31, 1987.

In 1990, he would return \$75,000 to the commissions and \$25,000 to the general fund. Rep. Mead seconded this motion. After further committee discussion, Rep. Hoy moved, and Rep. Baker seconded, to table the bill. The motion failed. On Rep. Leach's motion to amend the bill, the motion carried. Rep. Leach moved to pass the bill favorably, as amended. Rep. Teagarden seconded, and the motion carried.

S.B. 138

Rep. Foster moved, and Rep. Teagarden seconded, to pass the bill favorably. Rep. Baker offered a substitute motion to amend lines 62 and 63 by changing the number of days from 90 to 30 and the percent of qualified electors from 5% to 3%. Rep. Gjerstad seconded the motion. On a request to divide the motion, the substitute motion to change the days from 90 to 30 failed. On the motion to change the percent from 5% to 3%, the motion failed. On the original motion to pass the bill favorably, the motion carried.

The meeting adjourned at 4:45pm. At this time, no further meeting of the committee is scheduled.

SENATE BILL No. 243

By Committee on Economic Development

2-12

0018 AN ACT amending the Kansas venture capital company act;
0019 concerning income tax credits for investments in certified
0020 Kansas venture capital companies; amending K.S.A. 1986
0021 Supp. 74-8303, 74-8304 and 74-8306 and repealing the exist-
0022 ing sections.

0023 *Be it enacted by the Legislature of the State of Kansas:*

0024 Section 1. K.S.A. 1986 Supp. 74-8303 is hereby amended to
0025 read as follows: 74-8303. For the purposes of this act, the fol-
0026 lowing terms shall have the meanings provided herein, unless
0027 the context clearly indicates otherwise:

0028 (a) "Department" means the department of commerce;,
0029 (b) "equity" means all forms of equity such as common stock,
0030 preferred stock with or without voting rights and without regard
0031 to seniority of equity position, ~~forms of subordinate or convert-~~
0032 ~~ible debt, or both,~~ with warrants or other means of equity
0033 conversion attached, or any other means of financing which meet
0034 generally accepted national standards for venture capital invest-
0035 ment in the United States;;

0036 (c) "Kansas business" means any small business owned by a
0037 Kansas resident, any partnership, association or corporation
0038 domiciled in Kansas, or any corporation, even if a wholly owned
0039 subsidiary of a foreign corporation, that does business primarily
0040 in Kansas or does substantially all of its production in Kansas;;

0041 (d) "Kansas venture capital company" means any for-profit
0042 partnership or corporation that has as its primary business activ-
0043 ity the investment of funds in return for equity in ventures that
0044 are in need of capital for expansion, new product development or
0045 similar business purposes and that may be certified by the
0046 secretary as meeting the criteria of this act and thus eligible for

or forms of unsecured,

ATTACHMENT
L8/12/87

0047 the tax credit provided in this act;

0048 (e) "secretary" means the secretary of the department of
0049 commerce;

0050 (f) "cash investment" means money or its equivalent in con-
0051 sideration for:

0052 (1) An equity interest, such as a general or limited partner-
0053 ship interest, common or preferred stock with or without voting
0054 rights and without regard to seniority position, forms of subor-
0055 dinate or convertible debt, or both, with warrants or other
0056 means of equity conversion attached; or

0057 (2) a debt instrument, such as a note or debenture, which is
0058 unsecured, subordinated to the general creditors of the debtor,
0059 and requires no payments of principal (other than principal
0060 payments required to be made out of any future profits of such
0061 debtor) for at least a seven-year period after commencement of
0062 its term.

0063 Sec. 2. K.S.A. 1986 Supp. 74-8304 is hereby amended to read
0064 as follows: 74-8304. (a) There shall be allowed as a credit against
0065 the tax imposed by the Kansas income tax act on the Kansas
0066 taxable income of a taxpayer *and against the tax imposed by*
0067 *K.S.A. 40-2801, and amendments thereto, on insurance compa-*
0068 *nies for a cash investment in a certified Kansas venture capital*
0069 *company in an amount equal to 25% of such taxpayer's cash*
0070 *investment in any such company in the taxable year in which*
0071 *such investment is made and the taxable years following such*
0072 *taxable year until the total amount of the credit is used. In any*
0073 *one taxable year, the amount of such total credit allowable for*
0074 *deduction from the taxpayer's tax liability shall not exceed 25%*
0075 *of the total amount of such credit, and, in no case, may such*
0076 *amount exceed be limited to the lesser of 25% of such total*
0077 *credit, and 25% of the taxpayer's tax liability in such year. The*
0078 *amount by which that portion of the credit allowed by the*
0079 *preceeding sentence to be claimed in any one taxable year ex-*
0080 *ceeds 25% of the taxpayer's liability in such year may be carried*
0081 *back for not more than three taxable years or carried forward*
0082 *until the total amount of the credit is used. Subject to the*
0083 *foregoing limitations in any one taxable year.*

0084 (1) Such credit is allowable in the taxable year in which such
0085 cash investment is made;

0086 (2) to the extent the otherwise allowable credit is limited by
0087 tax liability limitation in any taxable year, the difference be-
0088 tween the tax credit limitation and the tax liability limitation in
0089 such taxable year may be carried back three taxable years (to be
0090 applied to the earliest such carryback year first);

0091 (3) after application of subdivision (2) above, any remaining
0092 unused total credit may be carried back to taxable years com-
0093 mencing after December 31, 1985, (to be applied to the earliest
0094 such carryback year first); and

0095 (4) after application of subdivisions (2) and (3) above, any
0096 remaining unused total credit may be carried over to subse-
0097 quent taxable years until such total credit is used in full in the
0098 taxable year in which such investment is made and the taxable
0099 years following such taxable year until the total amount of the
0100 credit is used. In any one taxable year, the amount of such credit
0101 allowable for deduction from the taxpayer's tax liability shall
0102 not exceed 25% of the total amount of such credit plus any
0103 applicable carryforward amount. The amount by which that
0104 portion of the credit allowed by the preceding sentence to be
0105 claimed in any one taxable year exceeds the taxpayer's liability
0106 in such year may be carried forward until the total amount of
0107 the credit is used.

0108 (b) The secretary of revenue may shall allow credits that are
0109 attributable to not more than \$24,000,000 of cash investments in
0110 certified Kansas venture capital companies, which shall include
0111 not more than \$10,000,000 for Kansas Venture Capital, Inc. The
0112 credits shall be allocated to by the secretary for cash invest-
0113 ments in certified Kansas venture capital companies in the order
0114 that completed applications for designation as Kansas venture
0115 capital companies are received by the secretary. Allocations by
0116 the secretary of such credit shall be made based upon commit-
0117 ted future cash investments, including those contingent solely
0118 upon certification, as well as uncommitted cash investments
0119 expected to be committed or made within 90 days of certifica-
0120 tion. Any such expected uncommitted cash investments which

0121 *are not in fact made or committed within such ninety-day period*
0122 *and with respect to which the certified Kansas venture capital*
0123 *company has not so demonstrated to the secretary in writing to*
0124 *have been made within 100 days of certification, shall forfeit*
0125 *their allocation of such credit. Any certified Kansas venture*
0126 *capital company may apply to the secretary at any time for*
0127 *additional allocation of such credit based upon then committed*
0128 *cash investments, but priority as to such additional allocation*
0129 *shall be determined at the time of such subsequent application.*

0130 Notwithstanding the provisions of subsection (c), investors in
0131 Kansas venture capital companies established after July 1, 1984,
0132 which otherwise meet the requirements specified in this act,
0133 shall be, upon certification of the Kansas venture capital com-
0134 pany, entitled to the tax credit provided in subsection (a) in the
0135 calendar year in which the investment was made.

0136 (c) No taxpayer shall claim a credit under this section for cash
0137 investment in Kansas Venture Capital, Inc. No Kansas venture
0138 capital company shall qualify for the tax credit allowed by
0139 Chapter 332 of the 1986 Session Laws of Kansas for investment
0140 in stock of Kansas Venture Capital, Inc.

~~0141 (d) After the \$1,500,000 capitalization threshold required
0142 under K.S.A. 1986 Supp. 74-8306, and amendments thereto, has
0143 been reached an investor in a venture capital company may
0144 enter into a binding investment contract of commitment under
0145 which 1/2 of the face value of the contract is a cash investment
0146 made in the current year and the second 1/2 is made within one
0147 year of certification. Upon formal notification by a certified
0148 venture capital company that such an investment contract has
0149 been entered into and not less than 1/2 of the face value of such
0150 contract has been received as a cash investment, the secretary of
0151 commerce shall reserve a portion of the remaining venture
0152 capital tax credit for such investor equal to that attributable to
0153 the second 1/2 of the committed investment under such contract.
0154 The investor shall be entitled to a tax credit in the year and in
0155 the amount that the cash investment is made.~~

0156 ~~(d)~~ (e) The provisions of this section shall be applicable to all
0157 cash investments made in any taxable years year commencing

0158 after December 31, 1985, and prior to January 1, 1993.

0159 Sec. 3. K.S.A. 1986 Supp. 74-8306 is hereby amended to read
0160 as follows: 74-8306. (a) The secretary shall promulgate rules and
0161 regulations for making an application for certification of a Kansas
0162 venture capital company and shall specify the information that
0163 must be submitted at the time of application. No Kansas venture
0164 capital company shall be certified until the secretary has adopted
0165 rules and regulations as required in K.S.A. 1986 Supp. 74-8305
0166 *and amendments thereto*. A company seeking to be certified as a
0167 Kansas venture capital company must specify the level of capi-
0168 ~~talization~~ *cash investment* that the company expects to qualify
0169 for the tax credits provided for in this act. The application must
0170 show that the applicant's purpose is to encourage and assist in
0171 the creation, development and expansion of Kansas businesses
0172 and to provide maximum opportunities for the employment of
0173 Kansans by making venture capital available to Kansas busi-
0174 nesses as described and defined in K.S.A. 1986 Supp. 74-8303
0175 *and amendments thereto*.

0176 (b) The department, through the secretary, shall review the
0177 articles of incorporation or the articles of partnership of each
0178 applicant for certification and the business history of the appli-
0179 cant and determine that the capitalization is at least \$1,500,000.

0180 (c) Within 60 days of application, the secretary shall issue the
0181 certification and notify the department of revenue of such cer-
0182 tification, or shall refuse the certification and issue an order so
0183 providing.

0184 Sec. 4. K.S.A. 1986 Supp. 74-8303 74-8304 and 74-8306 are
0185 hereby repealed.

0186 Sec. 5. This act shall take effect and be in force from and
0187 after its publication in the Kansas register.

74-2308. Same; annual reports; annual compliance review of each company by secretary, costs; notice of noncompliance; decertification; notice of forfeited tax credits. (a) Each qualified Kansas venture capital company shall report to the secretary on an annual basis such information as the secretary requires to be submitted to maintain certification. As a part of such information, each Kansas venture capital company shall report the name, address and taxpayer identification number of each taxpayer who has invested in such company and amounts invested by each such taxpayer.

(b) The secretary shall provide this information contained in subsection (a) to the department of revenue on an annual basis.

(c) The secretary shall conduct an annual review of each Kansas venture capital company certified under the program to determine if the Kansas venture capital company is in compliance with the requirements of certification, to advise the Kansas venture capital company as to the certification status of its investments, and to ensure that no investment has been made in violation of the provisions of this act or rules and regulations promulgated by the department. The reasonable costs of the annual review shall be paid by each Kansas venture capital company according to a reasonable fee schedule adopted by the secretary. Any violation shall be grounds for decertification under this section.

(d) If the Kansas venture capital company has met the fifth year, seventh year and ninth year investment levels and has subsequently sold any of the companies in which those equity investments were made, the temporary liquidity of the Kansas venture capital company prior to reinvestment in the equity of new ventures will not be cause for decertification.

(e) In undertaking the annual review the secretary shall use reasonable and generally accepted national standards of venture capital company practice. If the secretary determines that a company is not in substantial compliance with the requirements for continuing in certification, the secretary shall, by written notice, inform the

officers of the company and the board of directors or partners that they will be decertified in 120 days from the date of mailing of the notice unless they correct the deficiencies and are once again in compliance with the requirements for certification.

(f) At the end of the one hundred twenty day period, if the Kansas venture capital company is still not in substantial compliance, the secretary shall send a notice of decertification to the company and to the secretary of the department of revenue. Decertification of a Kansas venture capital company shall cause the forfeiture of any right or interest to the tax credit under the provisions of this act and shall cause the total amount of tax credit previously claimed by persons under the program to be due and payable with that year's income tax liability.

(g) Following each annual examination, the secretary shall notify the department of revenue of any Kansas venture capital companies that are not in compliance with this section.

(h) The department of revenue shall send written notice to the address of each person whose tax credit has been forfeited, using the address last shown on the person's last income tax filing.

History: L. 1986, ch. 285, § 8; May 22.

74-8309. Same; voluntary decertification; liability for tax credits claimed. At any time after the end of the seventh year, a Kansas venture capital company which is in compliance with this act may voluntarily decertify itself by sending written notice of decertification to the secretary and, in such case, the investors shall not be liable for repayment to the state of credit amounts claimed under this act. In any case where a Kansas venture capital company which is not in compliance with the provisions of this act, it may voluntarily decertify itself by sending written notice of decertification to the secretary and by remitting to the secretary of the department of revenue full payment of all tax credits claimed by investors under its participation in the certification program.

History: L. 1986, ch. 285, § 9; May 22.

universal targeting mechanisms; others are regulatory measures specifically designed for organizations which only structure equity investments.

Tools and Sources of Funds

Status. Guidelines for KVCII investments in current law are ambiguous, and are not fully explicit in terms of KVCII's risk capital investments, function or SBIC status.

Recommendations. The Commission recommends that:

1. KVCII's investments be made solely in-state.
2. KVCII's investments be required to be structured as equity or as unsecured subordinated debt with warrants convertible to equity.
3. All of the \$1.5 million already invested in KVCII that is reinvested should be credited towards the \$10 million requirement for the investment of idle state funds, but shall not be eligible for the tax credit.
4. The state invest in KVCII preferred stock only after the full \$10 million has been raised.
5. The ceiling of \$10 million investment eligible for the tax credit remain unchanged for FY 1987. The Task Force recognizes that if there is an oversubscription on the original \$10 million, it should be honored. After FY 1987, and after the initial \$10 million has been raised, the ceiling is subject to review and should be negotiable upon availability of additional, unused tax credit.
6. While KVCII's investment standards are of a higher order than those set by SBIC regulations, they must not jeopardize KVCII's SBIC license. In case of an apparent conflict between SBIC guidelines and KVCII's statute, the Secretary of the Kansas Department of Commerce should be given authority to interpret KVCII's statute in ways which do not jeopardize the SBIC license at the same time that the Legislative intent of S.B. 756 is maintained.
7. Any firm located within Kansas should qualify as a "Kansas business" under the tax credit bill, regardless of the owner's residence.

Attachment 2
3/31/87

Decertification Procedure

Prior to end of 7th year

1. Voluntary Decertification:
 - a. Venture Capital Co. is in compliance with the Act.
 - b. Investors must repay all credits.
2. Forced Decertification:
 - a. Venture Capital Co. is not in compliance with the Act.
 - b. Investors must repay all credits.

After End of 7th year

1. Voluntary Decertification:
 - a. Venture Capital Co. is in compliance with the Act.
 - b. Investors do not have to repay credits.
2. Forced Decertification:
 - a. Venture Capital Company is not in compliance with the Act.
 - b. Investors must repay all credits.

Prepared: DOC 3/31/87