

Approved 3-5-87
Date

MINUTES OF THE SENATE COMMITTEE ON ECONOMIC DEVELOPMENT

The meeting was called to order by Senator Wint Winter, Jr. at
Chairperson

12:35 ~~am~~/p.m. on February 25, 1987 in room 529-S of the Capitol.

All members were present except: Senator Norma Daniels - Excused
Senator Leroy Hayden - Excused

Committee staff present:

Arden Ensley, Revisor of Statutes
Lynne Holt, Legislative Research Department
Tom Severn, Legislative Research Department
Ramon Powers, Legislative Research Department
Mary Allen, Secretary to the Committee

Conferees appearing before the committee:

David Barclay, Department of Commerce
Mark Burghart, Department of Revenue
Charles Becker, Campbell-Becker
Sam Campbell, Campbell-Becker

The meeting was called to order at 12:35 p.m. by the Chairman, Senator Wint Winter, Jr..

Senator F. Kerr moved that the minutes of the February 19, 1987, meeting of the Committee be approved. Senator Burke seconded the motion. The motion carried.

Senate Bill 243 - An Act amending the Kansas venture capital company act; concerning income tax credits for investments in certified Kansas venture capital companies.

Chairman Winter told the Committee that SB 243 was introduced at the request of the venture capital group in Hutchinson. He observed that SB 67 is in the Committee and that it also deals with some issues relative to tax credits. He noted that there are two other bills which were passed out of the Senate Tax Committee dealing with tax credits and that there is concern by staff that there may be a need to reconcile all four bills.

The Chairman called on David Barclay, Department of Commerce, to brief the Committee on the provisions of SB 243. Mr. Barclay said that the purpose of the bill is to clarify the tax credit provisions of the venture capital company act. He passed out copies of a balloon version of SB 243 (Attachment I) and noted that the suggested amendments which it contains are the product of discussions with Legislative staff to try to conform this bill to the changes which were made in the other bills passed out by the Tax Committee. He called the attention of the Committee to an outline which lists all of the 1987 Venture Capital/Seed Capital Bills and which attempts in a short form to set out what each bill provides. (Attachment II)

Mr. Barclay explained the provisions of SB 243 and said that the bill contains an attempt to clarify the definition of the term "cash investments". That term is used as it applies to investments by investors in venture capital companies. He observed that the recommendation for this provision in the bill came from Tim O'Sullivan, attorney for the Hutchinson venture capital company. He noted that the term "cash investment" is defined, in short, as both an equity interest and a debt instrument. He stated that this recommendation is consistent with Belden Daniel's recommendation that investments in venture capital companies be equity or near equity, meaning debt instruments that are unsecured, subordinated instruments.

Mr. Barclay said that SB 243 also contains a provision dealing with a modification of the twenty-five percent tax credit. He stated that the balloon version of the bill makes the tax credit conform with the changes made earlier by the Committee, making the tax credit no more than twenty-five percent and it can be carried forward.

CONTINUATION SHEET

MINUTES OF THE SENATE COMMITTEE ON ECONOMIC DEVELOPMENT

room 529-S, Statehouse, at 12:35 ~~a.m.~~/p.m. on February 25, 19 87

The Chairman asked if Section 2 of SB 243, either as it was originally written or as it is proposed in the balloon, makes any substantive changes beyond what is either in existing law or what was passed by the Tax Committee. Mr. Barclay answered that two changes are made. Section 2 eliminates the carryback provision and it eliminates the provision that limits the investment to no more than twenty-five percent of an individual's tax liability. He said that these two changes were made by the Tax Committee in another bill.

Mr. Barclay said that SB 243 provides for continuing the present statutory policy of only allocating the tax credit based on actual cash investments. The balloon version of the bill proposes to allow venture capital companies to come to the state to say that they have the requisite \$1.5 million but they expect within a ninety day period to have additional funds and they want to reserve or earmark tax credit for those additional funds which they do not, as yet, have as well as for those funds which they do have. He said that the Department of Commerce recommends that this not be allowed to occur because the \$6 million cap on income tax credits for venture capital companies will very likely be used up this year due to the number of such companies which are being formed in Kansas. He stated that if these companies come in with the full amount of venture capital which they believe that they will be able to raise, they will exceed the state's \$6 million cap by about \$4 million. He said that there are six venture capital companies attempting to raise funds in Kansas. He noted that if the state gets in the business of allowing venture capital companies to reserve tax credits for funds that they do not yet have, it could preclude one of the proposed companies from coming in.

Mark Burghart, Department of Commerce, spoke on SB 243. He said that the DOR wants to make sure that the carryback situation is taken care of in the bill and is consistent with SB 69.

The Chairman called on Charles Becker and Sam Campbell. Campbell-Becker, for their observations and suggestions on SB 243. Mr. Becker said that their company concurs with the recommended changes suggested by the Department of Commerce to SB 243. Mr. Campbell discussed briefly the questioned need to expand the definition of cash investment to include debt instruments as an allowable cash investment for private venture capital companies. Mr. Campbell said that he has not been exposed to a venture capital company that did not want to have some kind of equity option or that was not going to make a straight equity investment. He said that it is very unusual to have a straight debt instrument involved in that investment.

Chairman Winter turned the attention of the Committee to SB 67 and noted that the issue will arise about whether or not to expand the tax credit for investments by insurance companies and banks in private venture capital companies. Mr. Campbell said that, from an insurance company perspective, most of the funds that are well funded throughout the country have funds which come from insurance companies. He stated that to eliminate them from this tax credit would be a very big mistake for there would be no way to attract those funds from the large insurance company pool.

The meeting was adjourned by the Chairman at 1:35 p.m..

February 25, 1987

GUEST LIST

NAME

REPRESENTING

MARK A. BURGHART

KS. DEPARTMENT OF REVENUE

Doc Barclay

DOC

BOB SCHAFFER

COLUMBIAN SECURITIES

Carolyn Coleman

K.U.

Charles A. Becku

Campbell Becku

Sam Campbell

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SENATE BILL No. 243

By Committee on Economic Development

2-12

0017 AN ACT amending the Kansas venture capital company act;
0018 concerning income tax credits for investments in certified
0019 Kansas venture capital companies; amending K.S.A. 1986
0020 Supp. 74-8303, 74-8304 and 74-8306 and repealing the exist-
0021 ing sections.

0022 *Be it enacted by the Legislature of the State of Kansas:*

0023 Section 1. K.S.A. 1986 Supp. 74-8303 is hereby amended to
0024 read as follows: 74-8303. For the purposes of this act, the fol-
0025 lowing terms shall have the meanings provided herein, unless
0026 the context clearly indicates otherwise:

0027 (a) "Department" means the department of commerce;

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

0035 (c) "Kansas business" means any small business owned by a
0036 Kansas resident, any partnership, association or corporation
0037 domiciled in Kansas, or any corporation, even if a wholly owned
0038 subsidiary of a foreign corporation, that does business primarily
0039 in Kansas or does substantially all of its production in Kansas;

0040 (d) "Kansas venture capital company" means any for-profit
0041 partnership or corporation that has as its primary business activ-
0042 ity the investment of funds in return for equity in ventures that
0043 are in need of capital for expansion, new product development or
similar business purposes and that may be certified by the
secretary as meeting the criteria of this act and thus eligible for

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Attachment I

0046 the tax credit provided in this act;

0047 (e) "secretary" means the secretary of the department of
0048 commerce;

0049 (f) "cash investment" means money or its equivalent in con-
0050 sideration for:

0051 (1) An equity interest, such as a general or limited partner-
0052 ship interest, common or preferred stock with or without voting
0053 rights and without regard to seniority position, forms of subor-
0054 dinate or convertible debt, or both, with warrants or other
0055 means of equity conversion attached; or

0056 (2) a debt instrument, such as a note or debenture, which is
0057 unsecured, subordinated to the general creditors of the debtor,
0058 and requires no payments of principal (other than principal
0059 payments required to be made out of any future profits of such
0060 debtor) for at least a seven-year period after commencement of
0061 its term.

0062 Sec. 2. K.S.A. 1986 Supp. 74-8304 is hereby amended to read
0063 as follows: 74-8304. (a)

~~0064 the tax imposed by the Kansas income tax act on the Kansas
0065 taxable income of a taxpayer for a cash investment in a certified
0066 Kansas venture capital company in an amount equal to 25% of
0067 such taxpayer's cash investment in any such company in the
0068 taxable year in which such investment is made and the taxable
0069 years following such taxable year until the total amount of the
0070 credit is used. In any one taxable year, the amount of such total
0071 credit allowable for deduction from the taxpayer's tax liability
0072 shall not exceed 25% of the total amount of such credit, and, in no
0073 case, may such amount exceed be limited to the lesser of 25% of
0074 such total credit, and 25% of the taxpayer's tax liability in such
0075 year. The amount by which that portion of the credit allowed by
0076 the preceding sentence to be claimed in any one taxable year
0077 exceeds 25% of the taxpayer's liability in such year may be
0078 carried back for not more than three taxable years or carried
0079 forward until the total amount of the credit is used. Subject to the
0080 foregoing limitations in any one taxable year:~~

0081 (1) Such credit is allowable in the taxable year in which such
0082 cash investment is made;

There shall be allowed as a credit against the tax imposed by the Kansas income tax act on the Kansas taxable income of a taxpayer for cash investment in a certified Venture Capital Company in an amount equal to 25% of such taxpayer's cash investment in any such certified Venture Capital Company in the taxable year in which such investment is made and the taxable years following such taxable year until the total amount of the credit is used. In any one taxable year, the amount of such credit allowable for deduction from the taxpayer's tax liability shall not exceed 25% of the total amount of such credit plus any applicable carryforward amount. The amount by which that portion of the credit allowed by the preceding sentence to be claimed in any one taxable year exceeds the taxpayer's liability in such year may be carried forward until the total amount of the credit is used.

0083 ~~(2) to the extent the otherwise allowable credit is limited by~~
0084 ~~tax liability limitation in any taxable year, the difference be-~~
0085 ~~tween the tax credit limitation and the tax liability limitation in~~
0086 ~~such taxable year may be carried back three taxable years (to be~~
0087 ~~applied to the earliest such carryback year first);~~

0088 ~~(3) after application of subdivision (2) above, any remaining~~
0089 ~~unused total credit may be carried back to taxable years com-~~
0090 ~~mencing after December 31, 1985, (to be applied to the earliest~~
0091 ~~such carryback year first); and~~

0092 ~~(4) after application of subdivisions (2) and (3) above, any~~
0093 ~~remaining unused total credit may be carried over to subse-~~
0094 ~~quent taxable years until such total credit is used in full.~~

0095 (b) The secretary of revenue ~~may~~ shall allow credits that are
0096 attributable to not more than \$24,000,000 of cash investments in
0097 certified Kansas venture capital companies, which shall include
0098 not more than \$10,000,000 for Kansas Venture Capital, Inc. The
0099 credits shall be allocated ~~to~~ by the secretary for cash invest-
0100 ments in certified Kansas venture capital companies in the order
0101 that completed applications for designation as Kansas venture
0102 capital companies are received by the secretary. Allocations by

0103 ~~the secretary of such credit shall be made based upon commit-~~
0104 ~~ted future cash investments, including those contingent solely~~
0105 ~~upon certification, as well as uncommitted cash investments~~
0106 ~~expected to be committed or made within 90 days of certifica-~~
0107 ~~tion. Any such expected uncommitted cash investments which~~
0108 ~~are not in fact made or committed within such ninety-day~~
0109 ~~period and with respect to which the certified Kansas venture~~
0110 ~~capital company has not so demonstrated to the secretary in~~
0111 ~~writing to have been made within 100 days of certification, shall~~
0112 ~~forfeit their allocation of such credit.~~ Any certified Kansas

0113 venture capital company may apply to the secretary at any time
0114 for additional allocation of such credit based upon then com-
0115 mited cash investments, but priority as to such additional
0116 allocation shall be determined at the time of such subsequent
application. Notwithstanding the provisions of subsection (c),
0118 investors in Kansas venture capital companies established after
0119 July 1, 1984, which otherwise meet the requirements specified

0120 in this act, shall be, upon certification of the Kansas venture
0121 capital company, entitled to the tax credit provided in subsection
0122 (a) in the calendar year in which the investment was made.

0123 (c) No taxpayer shall claim a credit under this section for cash
0124 investment in Kansas Venture Capital, Inc. No Kansas venture
0125 capital company shall qualify for the tax credit allowed by
0126 Chapter 332 of the 1986 Session Laws of Kansas for investment
0127 in stock of Kansas Venture Capital, Inc.

0128 (d) The provisions of this section shall be applicable to all
0129 *cash investments made in any taxable years year* commencing
0130 after December 31, 1985, and prior to January 1, 1993.

0131 Sec. 3. K.S.A. 1986 Supp. 74-8306 is hereby amended to read
0132 as follows: 74-8306. (a) The secretary shall promulgate rules and
0133 regulations for making an application for certification of a Kansas
0134 venture capital company and shall specify the information that
0135 must be submitted at the time of application. No Kansas venture
0136 capital company shall be certified until the secretary has adopted
0137 rules and regulations as required in K.S.A. 1986 Supp. 74-8305
0138 *and amendments thereto*. A company seeking to be certified as a
0139 Kansas venture capital company must specify the level of ~~cap-~~
0140 ~~italization~~ *cash investment* that the company expects to qualify
0141 for the tax credits provided for in this act. The application must
0142 show that the applicant's purpose is to encourage and assist in
0143 the creation, development and expansion of Kansas businesses
0144 and to provide maximum opportunities for the employment of
0145 Kansans by making venture capital available to Kansas busi-
0146 nesses as described and defined in K.S.A. 1986 Supp. 74-8303
0147 *and amendments thereto*.

0148 (b) The department, through the secretary, shall review the
0149 articles of incorporation or the articles of partnership of each
0150 applicant for certification and the business history of the appli-
0151 cant and determine that the capitalization is at least \$1,500,000.

0152 (c) Within 60 days of application, the secretary shall issue the
0153 certification and notify the department of revenue of such cer-
0154 tification, or shall refuse the certification and issue an order so
0155 providing.

0156 Sec. 4. K.S.A. 1986 Supp. 74-8303 74-8304 and 74-8306 are

0157 hereby repealed.

0158 Sec. 5. This act shall take effect and be in force from and
0159 after its publication in the Kansas register.

1987 VENTURE CAPITAL/SEED CAPITAL BILLS

<u>BILL NO.</u>	<u>STATUS</u>	<u>PRIMARY PURPOSE</u>	<u>AMENDMENTS</u>
SB 67	In Committoo	Allows transfer of Vonturo Capital tax credits to investors who are not Kansas taxpayers.	<ol style="list-style-type: none"> 1. Provide that the credit can only be transferred one time. 2. Require investors who are not taxpayers and who transfer the credit to report who acquired the credit. This information is to be reported to the venture capital company who in turn must report it to KDOC.
SB 243	In Committee	To clarify the tax credit provisions of the venture capital company act.	<ol style="list-style-type: none"> 1. Modifies the definition of cash investments. 2. Makes the venture capital tax credit provisions consistent with the Senate Economic Development Committees previous decisions. 3. Continues the present statutory policy of only allocating the tax credit based on actual cash investments.
SB 68	Passed out of committee	Simplifies the tax credit for business research and development expenditures.	<ol style="list-style-type: none"> 1. Eliminated the provisions that: <ol style="list-style-type: none"> a. Allowed carryback of the 25% tax credit. b. Limited the tax credit to 25% of a taxpayers tax liability.
SB 69	Passed out of committee	Provides for the creation of Local Seed Capital Pools.	<ol style="list-style-type: none"> 1. Eliminated the provisions that: <ol style="list-style-type: none"> a. Allowed carryback of the 25% tax credit. b. Limited the tax credit to 25% of a taxpayers tax liability. 2. Required a minimum pool capitalization of \$200,000. 3. Made public investments optional and required safeguards for invested public funds. 4. Set out the proceduros for dorcortification of local sood capital funds.
SB 70	Passed out of committee	Requires KVCI to invest 100% of its funds in state.	<ol style="list-style-type: none"> 1. Required KVCI to invest 100% of its funds in state. 2. Allowed KVCI to count its curront assets of \$1.5 million toward the \$10 million being raised. 3. Exempted venturo capital companies from franchise tax. 4. Exempted venture capital companies from making certain reports to the Secretary of State.

Senate Committee on Economic Development

2-25-87

Attachment II