

Approved: March 22, 1999  
Date

MINUTES OF THE SENATE COMMERCE COMMITTEE.

The meeting was called to order by Chairperson Alicia Salisbury at 8:00 a.m. on March 19, 1999 in Room 123-S of the Capitol.

All members were present except: Senator Steineger

Committee staff present:

Lynne Holt, Legislative Research Department  
Bob Nugent, Revisor of Statutes  
Betty Bomar, Committee Secretary

Conferees appearing before the committee:

John Prather, Chairman, Kansas, Inc.  
Larry Williams, Vice-Chairman, Kansas, Inc.  
Deryl K. Schuster, Member, Board of Directors, Kansas, Inc.  
Shirley Sicilian, Policy and Research, Department of Revenue  
Rich Bendis, President, Kansas Technology Enterprise Corporation

Others attending: See attached list

Upon motion by Senator Umbarger, seconded by Senator Donovan the Minutes of the March 18, 1999 Meeting were unanimously approved.

**SB 315 - Certified Capital Company Act**

John Prather, Chairman, Kansas, Inc., testified in support of **SB 315**, stating seed and venture capital is one of the elements of a broad based strategy for economic development. The bill creates the Certified Capital Company Act for the purpose of enhancing the development of seed and venture capital, which is greatly needed in the State of Kansas.

Larry Williams, Vice-Chairman, Kansas, Inc., testified in support of **SB 315**, stating there is not seed and venture capital available through banks and other loaning institutions as a result of regulators; consequently, there is a deepening need for states to be more inventive in creating seed and venture capital for new companies in order to create new businesses and jobs.

Deryl K. Schuster, Member of Kansas, Inc., Board of Directors, testified in support of **SB 315**, stating the lack of attracting loans by early stage or start-up businesses, as well as all new market type businesses, is one of the greatest impediments or deficiencies faced by new market type businesses throughout the United States. The lack of equity capital is the biggest problem lenders encounter when trying to find a way to say "yes" on long term loan requests to new and early state businesses. The need for this type of legislation is real and it is needed now. (Attachment 1)

Senator Brownlee stated there should be an assurance that companies that want investments provide some basis on which a determination can be made that the companies could actually succeed.

Shirley Sicilian, Department of Revenue, in response to a question from Senator Brownlee stated there is a tracking mechanism through the Security Exchange Commission as to which investors made certified investments in venture capital companies. There would not be information available as to how many jobs were created; that would be more of a research issue and not something the Department of Revenue would be involved in. Ms. Sicilian distributed proposed technical amendments that provide for the tax credit and its transferability. (Attachment 2)

Rich Bendis, President, Kansas Technology Enterprise Corporation, (KTEC), summarized the essence of **SB 315**, and referred the Committee to a Sheet entitled "SB 315-Key Points", distributed to the Committee. (Attachment 3)

CONTINUATION SHEET

MINUTES OF THE SENATE COMMERCE COMMITTEE, Room 123-S of the Statehouse, at 8:00 a.m. on March 19, 1999.

Mr. Bendis stated the Key-Points are issues raised by the Committee in prior testimony and the issues that have been addressed in the Balloon (Attachment 4) provided by the Revisor of Statutes.

Mr. Bendis stated it is evident that seed capital is non-existent in Kansas today. This information is documented from independent third-parties, and the lack of seed capital is more true in Kansas than many other areas of the country. **SB 315** is not a technology company bill. Only real estate, retail, and financial and personal services are excluded. Therefore, all 105 counties and companies in all 105 counties are eligible. As an example, the 13 counties considered depressed in Southeast Kansas could create a Capco with a \$5 million minimum fund that could make multi-form investments in many companies rather than the individual type of investing that is common place today. The minimum investment has been reduced to \$25,000 and investments are made only in Kansas companies with less than \$1 million in revenue and less than five years old. Kansas has 7500 businesses in the state, 6700 of which have less than 19 employees. We are a small business economy and most of the companies with less than 19 employees will generate less than \$1 million in revenue; therefore, a lot of businesses in Kansas are eligible for Capco investment.

Under this legislation, companies must agree to stay in Kansas for at least ten years if they receive investment through a Capco. If they do not stay, there should be some type of a payback mechanism to pay back the investment they received through the Capco and a penalty if they leave early.

Senator Ranson inquired if the pay back and penalty is included in the bill? Mr. Bendis stated there are other bills that address that, but no, it is not included in this bill.

Mr. Bendis stated **SB 315** provides for \$50 million total tax credits available with no more than \$5 million to be claimed per year. The tax implications to the State of Kansas are, therefore, spread over a ten year period which provides that the investor is only going to get a 50% benefit when taking into consideration what the money cost is over a ten year period. A minimum of \$5 million investment in each Capco is required, helping to create a venture capital industry by forming \$5 million seed and venture capital funds which are willing to invest in companies in Kansas. Capco managers are screened for competency and are regulated by the Securities Commission to protect the investors. The Securities Commission has audit authority and oversight powers. The Department of Revenue administers the tax credits. The proposed legislation reflects lessons learned from other states and from the Kansas 1986 tax credits.

The meeting adjourned at 9:00 a.m.

The next meeting is scheduled for March 22, 1999.



Statement by Deryl K. Schuster, President,  
Business Loan Center, Inc., Mid-America Division and  
Member of Kansas, Inc. Board of Directors and  
Chairman, National Association of Government Guaranteed Lenders

To: Kansas Senate Commerce Committee

Re: Senate Bill Number 315

Madame Chair and distinguished Senators all. It is my pleasure to call several of you friends. To you all I thank you for the leadership that you provide in working to strengthen the economic vitality of our great state. Wearing my hat as Chairman of the National Association of Government Guaranteed Lenders, an organization whose 700 plus lender members made over 80% of all SBA guaranteed loans last year, I had the pleasure earlier this week of testifying before the United States Senate Committee on Small Business. The similarities of today and the opportunity of last Tuesday are most interesting. The purpose of the United States Senate hearing was to discuss the President's fiscal 2000 budget. The President's budget includes a request for direct appropriation to assist businesses that the administration classifies as "new markets." Those businesses finding it traditionally difficult to obtain loans and equity. As defined by the President, new market businesses include start-ups, early stage firms, businesses in rural areas, inner-city areas, as well as minority, female and handicapped applicants. I must tell you that from a national perspective, the difficulty in attracting investment capital, and even loans by early stage or start-up businesses, as well as all new market type businesses, was well established in the Washington D.C. hearing last Tuesday. I heard Senator John Kerry from Massachusetts, the ranking minority on the Senate Small Business Committee, say that in his state venture capital was one of the biggest impediments or deficiencies new market type businesses face. In addition, I heard the President of the National Association of Certified

Senate Commerce Committee

Date: 3-19-99

Attachment # 1 - 1 thru 1 - 3



Development Companies say that the lack of equity or investment capital was the most serious problem faced by new and early stage businesses. Representing the National Association of Government Guaranteed Lenders as well as my company, Business Loan Center, I joined in confirming that the lack of equity capital was the biggest problem lenders encounter when trying to find a way to say "yes" on long term loan requests to new and early stage businesses. Senators, if this is a problem in Boston, how much greater the problem must be in Wichita, Topeka, Pittsburgh, McPherson or Thayer. The need is real and it is a national problem. The difference between Senate Bill 315 and the President's budget, is that the administration is asking for direct appropriation to help address the problem. We in Kansas are asking for tax credits. A much more sellable approach, in my opinion.

Please let me relate a real live situation that occurred while I was in Washington this week. I called my office in Wichita for messages. One call was from a Mr. Greg Shuey, President, TensorTech, a technology development company from Johnson County that my company had made a loan to several years ago to help finance this start-up high tech firm. At that time Mr. Shuey had adequate personal investment capital to leverage into a \$212,000 SBA loan. Mr. Shuey's background is incredible. He was the project manager for a \$700 million dollar satellite program for the U.S. Air Force, and he was also Air Force Director of Engineering at the Johnson's Space Center. He owned and started the first American technology transfer company in Korea, representing the State of Florida, Kansas City Aviation Department, Burns and McDonald, etc. As mentioned, we were able to make the initial loan because he had accumulated adequate personal investment capital to support the loan. Also, at that time SBA's guarantee was 85% instead of the current 75%, which made it easier to say "yes." Mr. Shuey's loan has paid as agreed, so I had not heard from him for several years. When I returned his call from Washington D.C. he told me his business had done extremely well but that he had

developed new technology that could revolutionize compression technology in the video communication industry. Technology in which several national and international firms have expressed interest. His immediate need is to find \$500,000 of investment capital to complete the development, to be followed by a \$4.5 million stock offering when the technology is totally marketable. I told him that our company only made loans and by name I suggested he contact the established venture capital firms operating in our area. Unfortunately, he was way ahead of me in that each venture capital firm I mentioned he gave me the reason why they had declined to come to the table. His need was too small, too early stage, not enough collateral, or whatever. Mr. Shuey had decided he needed to find "angel type investors." Senators, the best I could do was to suggest that Mr. Shuey contact Charles Ranson, President of Kansas, Inc., who had been working on a venture capital initiative for our state to see if he had heard of any additional venture capital or angel type investment sources during his involvement with this issue. Please know I received approval from Mr. Shuey to communicate this actual, real life situation. I am sure Mr. Shuey would be pleased to explain his dilemma in greater detail, if requested. Unfortunately, lenders in Kansas, yes in America, are confronted with this situation on a regular basis. Investment capital to new and early stage firms is a serious void in economic development that some states have tried to fill and with which even Congress is struggling. I appeal to you to let Kansas join those states where people like Greg Shuey might find hope and help and where our state might enjoy the fruits of their labors in creating jobs, tax revenue, and innovation. Senators, I ask for you to take the leadership to make Senate Bill 315 happen this year! The need is real and it is now! To defer action is to invite the Greg Shueys of our State to take their businesses elsewhere. We should not let that happen! Thank you and I would be pleased to respond to any questions.

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Office of Policy & Research

TESTIMONY

**To:** Senator Alicia Salisbury, Chairperson  
Senate Commerce Committee

**From:** Shirley Sicilian

**Re:** Senate Bill 315

**Date:** March 19, 1999

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Chairperson Salisbury and members of the Senate Commerce Committee, thank you very much for the opportunity to testify today. My name is Shirley Sicilian and I am the Director of Policy and Research at the Department of Revenue.

At your last meeting I mentioned some technical, non substantive changes might be made to the sections of senate bill 315 that provide for the tax credit and its transferability. I have made these few suggestions as balloon amendments to the bill as introduced (attached). I believe that each suggestion is simply technical clean-up.

There is one clean-up in particular that I would like to bring to your attention to ensure that it is in keeping with the committee's intentions for the bill. That is on page 5, lines 8 and 9 of the bill. I have stricken the sentence that read "The commission [SEC] shall be responsible for the administration of the tax credits authorized by this act." By statute, the Department of Revenue is charged with administration of the income and financial institutions privilege taxes. That would include administration of credits against those taxes. My understanding of the bill's intent is that the SEC would administer the venture capital *program* created by this act, including:

- determination of whether an investment is a "certified capital investment" in a "certified capital company" that has raised the "minimum aggregate certified investment" required.
- determination of whether an interest in a tax credit originally earned by such investment has been duly transferred, to what person(s), in what amount, and for what price
- audit of those determinations
- review of those determinations upon appeal

But that the Department of Revenue would administer the *tax credit* created by this act, including

- determination of whether the SEC has "certified" such investment, or "certified" transfer of a all or a portion of an interest in the tax credit to be allowed by such investment
- determination of the amount of carry-over credit for each taxpayer
- determination of whether the cumulative amount of credit allowed Senate Commerce Committee has reached \$5,000,000.

Date: 3-19-99

Attachment # 2-1 thru 2-15

2-2

## SENATE BILL No. 315

By Committee on Commerce

2-12

9 AN ACT concerning venture capital; enacting the Kansas certified capital  
10 company act; amending K.S.A. 1998 Supp. 17-1262 and repealing the  
11 existing section.

12  
13 *Be it enacted by the Legislature of the State of Kansas:*

14 New Section 1. This act shall be known and may be cited as the  
15 "Kansas Certified Capital Company Act". The purpose of this act is to  
16 enhance the development of seed and venture capital in Kansas and to  
17 support the modernization and expansion of the state's rural economy.  
18 As used in this act, the following terms mean:

19 (a) "Certified capital company" means any partnership, corporation,  
20 trust or limited liability company, whether organized on a profit or not  
21 for profit basis, that is domiciled in and qualified to conduct business in  
22 Kansas and that has as its primary business activity, the investment of cash  
23 in qualified Kansas businesses, and which is certified by the securities  
24 commissioner of Kansas as satisfying the criteria of this act.

25 (b) "Capco" means any certified capital company.

26 (c) "Tax credit" means a transferable, non-refundable credit against  
27 the tax imposed by the Kansas income tax act, the premium tax or priv-  
28 ilege fee imposed pursuant to K.S.A. 40-252, and amendments thereto,  
29 or the privilege tax as measured by net income of financial institutions  
30 imposed pursuant to chapter 79, article 11 of the Kansas Statutes  
31 Annotated.

32 (d) "Applicable percentage" means one hundred percent.

33 (e) "Capital in a qualified Kansas business" means any note, stock,  
34 partnership or membership interest or other form of equity investment  
35 or hybrid security, of any nature and description whatsoever, including a  
36 debt instrument or security which has the characteristics of indebtedness  
37 but which provides for conversion into equity or equity participation in-  
38 struments such as options or warrants which are acquired by a Kansas  
39 certified capital company as a result of a transfer of cash to a business.  
40 Capital in a qualified Kansas business shall not include secured debt  
41 instruments.

42 (f) "Certified capital investment" means an investment of cash by an  
43 investor made in such manner as to acquire a beneficial ownership inter-



1 est in a Kansas certified capital company.

2 (g) "Certified capital" means cash, marketable securities and other  
3 liquid assets held by a certified capital company equal to the amount of  
4 certified capital investment made by investors in the certified capital  
5 company.

6 (h) "Commission" means the Kansas securities commission.

7 (i) "Commissioner" means the securities commissioner of Kansas or  
8 a person acting under the supervision of the commissioner.

9 (j) "Investor" means any natural person or entity, including a cor-  
10 poration, limited liability company, general or limited partnership, trust  
11 or limited liability company that invests cash.

12 (k) "Liquidating distribution" means payments remitted to investors  
13 or to the certified capital company derived from earnings.

14 (l) "Person" means any natural person or entity, including a corpo-  
15 ration, limited liability company, general or limited partnership, trust or  
16 limited liability company.

17 (m) "Qualified distribution" means any distribution or payment re-  
18 mitted to equity holders of a certified capital company in connection with  
19 the following:

20 (1) Reasonable costs and expenses of forming, syndicating, managing  
21 or operating the certified capital company;

22 (2) Fees paid to qualified managers for managing or operating the  
23 certified capital company.

24 (n) "Qualified venture capital investment" means the investment of  
25 cash by a Kansas certified capital company in such a manner as to acquire  
26 capital in a qualified Kansas business.

27 (o) "Qualified Kansas business" means:

28 (1) A business that satisfies the requirements of paragraphs (A)  
29 through (B) of this subsection.

30 (A) Such business is independently owned and operated and has its  
31 principal business office located in Kansas or, in the case of a company  
32 domiciled outside the state of Kansas, which certifies that the company's  
33 principal business office will be located in Kansas within six months fol-  
34 lowing the date of the initial investment;

35 (B) such business shall, at the time of the initial qualified venture  
36 capital investment, have no more than 50 full time equivalent employees,  
37 at least fifty percent of whom are resident in Kansas or, in the case of a  
38 company domiciled outside the state of Kansas, certifies that at least fifty  
39 percent of its employees will be resident in Kansas within six months  
40 following the date of the initial qualified venture capital investment;

41 (C) such business is in need of venture capital and cannot obtain  
42 conventional financing to fund its further development and future  
43 operations;

1 (D) such business shall be engaged in commerce for the purpose of  
2 manufacturing, processing or assembling or distributing products, con-  
3 ducting research and development or providing services in interstate  
4 commerce.

5 (E) For businesses involved in commerce for the purpose of provid-  
6 ing services in interstate commerce, that business must demonstrate that  
7 more than fifty percent of its gross revenues are derived from sales out-  
8 side the state of Kansas, or in the case of an early stage business, provide  
9 reasonable documentation that the company will derive at least fifty per-  
10 cent of its gross sales outside the state within a three-year period.

11 (2) Any business which, subject to audit, is properly classified as a  
12 qualified Kansas business at the time of the first qualified venture capital  
13 investment in such business by a Kansas certified capital company shall,  
14 for a period of seven years following the date of such first investment,  
15 continue to be classified as a qualified Kansas business and may receive  
16 follow-on investments from any Kansas certified capital company, and  
17 such follow-on investments shall constitute qualified venture capital in-  
18 vestments even though such business may not meet other qualifications  
19 of this subsection at the time of such follow-on investments.

20 (3) A qualified Kansas business shall not include:

21 (A) Any commercial enterprise primarily engaged in the sale at retail  
22 of goods or services taxable under the Kansas retailer's sales tax act; any  
23 service provider set forth in K.S.A. 17-2707, and amendments thereto;  
24 any bank, savings and loan or lending institution; any real estate, real  
25 estate development or insurance company; or any commercial enterprise  
26 deriving its revenues directly from noncommercial customers in exchange  
27 for personal services;

28 (B) a business engaged primarily as a passive business, irregular or  
29 noncontinuous operations, or which derives substantially all of its income  
30 from passive investments that generate interest, dividends, royalties or  
31 capital gains;

32 (C) a business engaged in oil and gas exploration and development;

33 (D) a subsidiary of a certified capital company;

34 (E) another certified capital company;

35 (F) an affiliate of the certified capital company;

36 (G) an investor of the certified capital company or an affiliate or sub-  
37 sidiary of an investor of the certified capital company unless approved in  
38 writing by the commissioner.

39 (4) At the time of the initial qualified venture capital investment, the  
40 qualified Kansas business shall certify that the business shall remain dom-  
41 icated in Kansas for the next 10 years and any new manufacturing facility  
42 financed directly by a qualified investment shall be located in and shall  
43 remain in Kansas for the 10 years following.

- 1 (p) "Affiliate of a certified capital company" means:
- 2 (1) any person that directly or indirectly, owns, controls or possesses
- 3 the power or ability to vote ten percent or more of the outstanding voting
- 4 securities or other beneficial ownership interests of the Kansas certified
- 5 capital company;
- 6 (2) any person ten percent or more of whose outstanding voting se-
- 7 curities or other beneficial ownership interests are directly or indirectly
- 8 owned, controlled or possessed with the power to be voted by the Kansas
- 9 certified capital company;
- 10 (3) any person directly or indirectly controlling, controlled by, or un-
- 11 der common control with the Kansas certified capital company;
- 12 (4) any partnership in which the Kansas certified capital company is
- 13 a general partner;
- 14 (5) any person who is an officer, director, general partner, managing
- 15 member, manager director or agent of the Kansas certified capital com-
- 16 pany or an immediate family member of such person.

- 17 (q) "Affiliate of an investor" means:
- 18 (1) Any person that directly or indirectly, owns, controls or possesses
- 19 the power or ability to vote ten percent or more of the outstanding voting
- 20 securities or other beneficial ownership interests of the investor;
- 21 (2) any person ten percent or more of whose outstanding voting se-
- 22 curities or other beneficial ownership interests are directly or indirectly
- 23 owned, controlled, or possessed with the power to be voted by the
- 24 investor;
- 25 (3) any person directly or indirectly controlling, controlled by or un-
- 26 der common control with the investor;
- 27 (4) a partnership in which the investor is a general partner;
- 28 (5) any person who is an officer, director or agent of the investor or
- 29 an immediate family member of such officer, director or agent.

30 New Sec. 2. (a) Any investor that makes a certified capital investment  
 31 shall earn a vested tax credit against state tax liability equal to 100% of  
 32 the amount of such investor's certified capital investment. An investor, or  
 33 person to whom the credits were duly transferred, shall be entitled to use  
 34 not more than 10% of the vested credit per year beginning with tax filings  
 35 for calendar year 2001. Any tax credit not used by an investor, or a person  
 36 to whom the credits were duly transferred, in any single year may be  
 37 carried forward and applied against tax liabilities of such investor or trans-  
 38 feree for subsequent calendar years.

39 (b) A tax credit claimed against state tax liability as described in sub-  
 40 section (a) may not exceed the state tax liability of the investor, or person  
 41 to whom the credits were duly transferred, for any taxable year. All such  
 42 credits against state tax liability may be carried forward indefinitely until  
 43 the credits are utilized.

taxable year for taxable years commencing after December 31, 2000

If the amount of the credit allowed under subsection (a) exceeds the state tax liability of the investor or transferee for any taxable year, the amount which exceeds such tax liability of such portion thereof may be carried over for credit in the same manner in the succeeding taxable years, until the total amount of such credit is used

1 (c) If the investor is an individual, the investor shall have a personal  
 2 net worth of at least \$1,000,000 and at least ten times the amount of such  
 3 investor's certified capital investment in a capco. The investor's net worth  
 4 shall not include the value of any equity in such investor's primary  
 5 residence.

move to § 1(j) - definition of investor

6 (d) No certified capital investment in a capco by any one person shall  
 7 be less than \$50,000.

move to § 1(F) - definition of certified capital investment

8 (e) ~~The commission shall be responsible for the administration of the~~  
 9 ~~tax credits authorized by this act.~~

tax credit earned allowed

10 (f) ~~The total amount of tax credits which may be allocated by the~~  
 11 ~~commissioner shall not exceed \$50,000,000. The total amount of tax cred-~~  
 12 ~~its which may be claimed under this act shall not exceed \$5,000,000 per~~  
 13 ~~year.~~

fiscal year. The Secretary of Revenue shall allow such credits on a first-come-first-serve basis.

14 New Sec. 3. (a) The commissioner may certify profit or not-for-profit  
 15 entities which submit an application to be designated as a capco. The  
 16 commissioner shall compile a list of every capco, including the address  
 17 and telephone number of the capco's principal place of business. The  
 18 commissioner shall forward the list to the secretary of commerce and  
 19 housing. The secretary of commerce and housing shall publicize the list  
 20 in order to inform Kansas companies of the availability of potential in-  
 21 vestment capital. The commission shall review the organizational docu-  
 22 ments for each applicant for certification and the business history of the  
 23 applicant to determine:

24 (1) that at the time of application, the applicant owns cash, market-  
 25 able securities and other liquid assets valued at no less than \$500,000, or  
 26 that the applicant is designated as an innovation and commercialization  
 27 corporation or an affiliate of an innovation and commercialization cor-  
 28 poration created under the Kansas technology enterprise corporation in-  
 29 novation and commercialization corporation program;

30 (2) that the officers and the board of directors, general partners, trus-  
 31 tees, managing members, or managers, as the case may be, are thoroughly  
 32 acquainted with the requirements of this act and acknowledge such by a  
 33 signed certification.

34 (b) To continue to be certified, the capco must own and shall peri-  
 35 odically provide information to the commissioner as the commissioner  
 36 may require in order for the commissioner to determine that the liquid  
 37 asset base for the certified capital company is at least \$500,000 at all times  
 38 during the capco's participation in the program authorized by this act or  
 39 that such moneys have been used for making qualified venture capital  
 investments.

41 (c) No entity which submits an application to be designated as a capco  
 42 shall be certified by the commissioner if any of its directors, trustees,  
 43 managers, officers, general partners, beneficial owners of 10% or more



1 of any class of its equity securities, or any promoters employed or oth-  
2 erwise associated with it at the time of such application:

3 (1) Has been affiliated with any company that has filed a registration  
4 statement which is subject to a currently effective stop order entered  
5 pursuant to any state law;

6 (2) has been convicted of any felony or misdemeanor in connection  
7 with the purchase or sale of any security or any felony involving fraud or  
8 deceit including, but not limited to, forgery, embezzlement, obtaining  
9 money under false pretenses, larceny or conspiracy to defraud;

10 (3) is currently subject to any state administrative order or judgment  
11 entered by a state securities administrator or is subject to any state ad-  
12 ministrative order or judgment in which fraud or deceit was found and  
13 an order or judgment was entered;

14 (4) is currently subject to any state administrative order or judgment  
15 which prohibits the use of any exemption from registration in connection  
16 with the purchase or sale of securities;

17 (5) is subject to any order, judgment or decree of any court of com-  
18 petent jurisdiction temporarily or preliminarily restraining or enjoining,  
19 or is subject to any order, judgment or decree of any court of competent  
20 jurisdiction permanently restraining or enjoining that person from engag-  
21 ing in or continuing any conduct or practice in connection with the pur-  
22 chase or sale of any security, rendering investment advice, or involving  
23 the making or any false filing with any state;

24 (6) has been convicted of or plead nolo contendere to any criminal  
25 offense other than a misdemeanor involving motor vehicle violations.

26 (d) The commissioner shall further review documentation regarding  
27 the qualifications of the persons who will actively manage the capco and  
28 make a determination as to whether such persons possessed sufficient  
29 knowledge and professional experience in the areas of investment, ven-  
30 ture capital, business management and evaluation, portfolio management,  
31 and such other area of expertise to the degree that a reasonable person  
32 would be confident in such manager's ability to manage the capco. No  
33 certification shall be issued when it is the opinion of the commissioner  
34 that such persons do not possess this requisite degree of knowledge and  
35 expertise.

36 (e) No investor shall individually, or collectively with or through one  
37 or more affiliates, by means of ownership, agreement or otherwise, own,  
38 control, or possess the power or ability to cause or direct the making of  
39 any qualified venture capital investments by a capco.

40 (f) Within 75 days of application, the commission shall either issue  
41 the certification and notify the secretary of the department of revenue of  
42 such certification or shall refuse the certification and communicate in  
43 detail to the applicant the grounds for the refusal, including any sugges-

1 tions for the removal of those grounds.

2 New Sec. 4. (a) A capco shall have a period of 365 days from the  
3 date of receiving certification from the commissioner in which to procure  
4 the amount of certified capital investment required by subsection (b). All  
5 certified capital investments in the capco shall be received within such  
6 three-hundred-sixty-five-day funding period, notwithstanding the provi-  
7 sions of subsection (c).

8 (b) Before closing its fund of certified capital investment, and pur-  
9 suant to subsection (a) of section 3, and amendments thereto, a capco  
10 shall raise a minimum aggregate certified capital investment of no less  
11 than \$5,000,000. In the case of a capco designated as an innovation and  
12 commercialization corporation or an affiliate of an innovation and com-  
13 mercialization corporation created under the KTEC innovation and com-  
14 mercialization corporation program, such minimum certified capital in-  
15 vestment shall be no less than \$1,000,000. No tax credits shall be issued  
16 ~~by the commissioner until such time when these minimum cumulative~~  
17 ~~investments are met.~~ Failure of a capco to raise the minimum cumulative  
18 investments may result in the revocation of the certification by the  
19 commissioner.

20 (c) Once fully capitalized pursuant to the provisions of subsection (b),  
21 a capco may make application to the commissioner for authorization to  
22 seek additional certified capital investment.

23 New Sec. 5. (a) To continue to be certified, a capco shall make qual-  
24 ified venture capital investments according to the following schedule:

25 (1) Within three years after the date on which a capco is certified as  
26 a capco at least 25% of its certified capital shall be, or have been, used  
27 for making qualified venture capital investments;

28 (2) within four years after the date on which a capco is certified as a  
29 capco at least 40% of its certified capital shall be, or have been, used for  
30 making qualified venture capital investments;

31 (3) within five years after the date on which a capco is certified as a  
32 capco at least 50% of its total certified capital shall be, or have been, used  
33 for making qualified venture capital investments;

34 (4) within seven years after the date on which a capco is certified as  
35 a capco at least 70% of its total certified capital shall be, or have been,  
36 used for making qualified venture capital investments.

37 (5) A capco shall not make an investment in an affiliate of the capco  
38 or an affiliate of an investor. For the purposes of this subsection, if a legal  
39 entity is not an affiliate before a capco initially invests in the entity, it  
40 shall not be deemed to be an affiliate if such capco provides additional  
41 qualified venture capital investment to such entity subsequent to its initial  
42 investment. No corporate officer, employee or shareholder, no limited or  
43 general partner or other person personally affiliated with any capco shall

aggregate  
allowed by the Secretary of Revenue pursuant  
to section 2 for any certified capital  
investment in a particular capco  
until that capco has raised the  
applicable minimum aggregate  
certified capital investment

aggregate

2-9

1 personally invest in any portfolio company regardless of whether the port-  
2 folio company is affiliated with the capco.

3 (6) A capco, at least 15 working days prior to making what it deter-  
4 mines to be any initial qualified venture capital investment, shall first  
5 certify to the commissioner that the company in which it proposes to  
6 invest meets the definition of a qualified Kansas business pursuant to  
7 paragraph (15) of subsection (a) of section 1, and amendments thereto.  
8 The capco shall state the amount of capital it intends to invest and identify  
9 the business in which it intends to make the investment. The capco shall  
10 also provide to the commissioner a written explanation of the basis for its  
11 determination that the business meets the definition of a qualified Kansas  
12 business, if the commissioner determines that the business does not meet  
13 the definition of a qualified Kansas business, the commissioner shall,  
14 within the fifteen-working-day period prior to the making of the proposed  
15 investment, notify the capco of the determination and provide the capco  
16 an explanation thereof. If the commissioner fails to notify the capco of  
17 his or her determination within the 15 working day period prescribed  
18 herein, the business in which the capco proposes to invest shall be  
19 deemed to be a qualified Kansas business. If a capco fails to notify the  
20 commissioner prior to making an initial investment in a business, the  
21 business in which the capco invested shall be deemed not to be a qualified  
22 Kansas business even though the business, at the time of the investment,  
23 met the requirements of paragraph (o) of subsection (a) of section 1, and  
24 amendments thereto;

25 (7) All certified capital which is not then required to be invested in  
26 qualified venture capital investments or which has been previously in-  
27 vested in qualified venture capital investments and returned by the com-  
28 pany, may be held or invested in such manner as the capco, in its discre-  
29 tion, deems appropriate. The proceeds of all certified capital which is  
30 returned by a capco after it was originally invested in qualified venture  
31 capital investments, may be invested in other qualified venture capital  
32 investments and shall be credited toward any requirement in this act with  
33 respect to placing certified capital in qualified venture capital  
34 investments.

35 (b) A capco may make qualified distributions at any time. In order to  
36 lawfully make liquidating distributions, a capco must have invested an  
37 aggregate amount equal to 100% of its certified capital in qualified ven-  
38 ture capital investments.

39 (c) Cumulative liquidating distributions to equity holders in excess of  
40 the certified capital company's original certified capital and any additional  
41 capital contributions to the certified capital company shall be subject to  
42 audit by a nationally recognized, certified public accounting firm accept-  
43 able to the commissioner at the expense of the certified capital company.

1 The audit shall determine whether aggregate cumulative liquidating dis-  
2 tributions to all investors and equity holders, when combined with all tax  
3 credits utilized by investors pursuant to this act, have resulted in an annual  
4 internal rate of return of 15% computed on the sum of total original  
5 certified capital of the certified capital company and any additional capital  
6 contributions to the certified capital company.

7 (d) If at any time of any such distribution made by the capco which  
8 has achieved the annual internal rate of return specified under subsection  
9 (c) such distribution taken together with all other such distributions made  
10 by the certified capital company, other than qualified distributions, ex-  
11 ceeds in the aggregate the sum of the certified capital company's original  
12 certified capital and any additional capital contributions to the certified  
13 capital company, as determined by the audit, the certified capital com-  
14 pany shall, prior to any additional distributions, pay to the Kansas state  
15 treasurer's office 25% of the proportion of such distribution in excess of  
16 such amount.

17 (e) Documents and other materials submitted by Kansas certified  
18 capital companies or by businesses for purposes of original certification  
19 or the continuance of certification shall not be public records if it is de-  
20 termined by the commissioner that disclosure of such information would  
21 compromise trade secrets of qualified Kansas businesses or the privacy  
22 rights of any investor and shall be maintained in a secured environment  
23 by the commissioner.

24 (f) Each capco shall report the following to the commission:

25 (1) As soon as practicable, but in any case no later than 15 days, after  
26 the receipt of a certified capital investment, the name of each investor  
27 from whom the certified capital investment was received, the amount of  
28 each investor's certified capital investment, and the date when the cer-  
29 tified capital investment was received;

30 (2) Each capco shall provide to the commissioner, annual audited  
31 financial statements to the commission within 90 days of the close of the  
32 fiscal year. The audit shall address the methods of operation and conduct  
33 of business of the capco to determine if the capco is complying with the  
34 statutes and program rules and that the funds received by the capco have  
35 been invested in accordance with the time limits provided by this act.

36 (3) At the end of each quarter, that no more than 20% of the assets  
37 of a capco shall be invested in a single qualified Kansas business at any  
38 one time unless the capco can demonstrate that a greater percentage in  
39 a single qualified Kansas business at any one time is the result of losses  
40 suffered by the capco in other qualified venture capital investments.

41 New Sec. 6. To ensure that no qualified venture capital investment  
42 or investor's certified capital investment has been made in violation of  
43 this act, the commissioner shall conduct an annual review of each capco



1 to determine if the capco is complying with the requirements of certifi-  
2 cation, and shall advise the capco as to the status of its investments as  
3 qualified venture capital investments. The costs of the annual review shall  
4 be paid by each capco according to a reasonable fee schedule adopted by  
5 the commission.

6 (b) Any material violation of this act shall be grounds for decertifi-  
7 cation under this section. If the commission determines that a company  
8 is not in compliance with any requirements for continuing in certification,  
9 it shall, by written notice, inform the officers of the company and the  
10 board of directors, managers, trustees or general partners that they may  
11 be decertified within 120 days from the date of mailing of the notice,  
12 unless they correct the deficiencies detailed in the notice and demon-  
13 strate to the commissioner's satisfaction that the capco is again in com-  
14 pliance with the requirements for certification as determined by the  
15 commissioner.

16 (c) At the end of the one-hundred-twenty-day grace period, if the  
17 capco is still not in compliance, the commission may then send a notice  
18 of decertification to the capco and to the secretary of department of  
19 revenue. Decertification of a capco prior to the capco meeting all require-  
20 ments of paragraph (1) through (3) of subsection (a) of section 5, and  
21 amendments thereto, shall cause the recapture of all tax credits previously  
22 claimed by an investor ~~and the forfeiture of all future tax credits to oth-~~  
23 erwise be claimed by an investor ~~with respect to his or her certified capital~~  
24 investment in the capco. Decertification of a capco after it has met all  
25 requirements of paragraphs (1) to (3) of subsection (a) of section 5, and  
26 amendments thereto, shall cause the forfeiture of tax credits commencing  
27 with the taxable year of the investor ~~in which the decertification arose~~  
28 and for all future taxable years ~~with no recapture of tax credits obtained~~  
29 by an investor ~~with respect to the investor's tax years which ended before~~  
30 the decertification occurred. Once a capco has invested 100% of its cer-  
31 tified capital in qualified Kansas businesses, all future tax credits to be  
32 claimed by investors ~~with respect to said capco pursuant to this act shall~~  
33 be nonforfeitable.

~~and the forfeiture of all future tax credits to oth-~~ or transferee  
~~with respect to his or her certified capital~~ or transferee  
~~in which the decertification arose~~ or transferee  
~~with respect to the investor's tax years which ended before~~ or transferee  
~~with respect to said capco pursuant to this act shall~~ or transferees

34 New Sec. 7. The commissioner shall prepare and submit an annual  
35 report to the governor and the legislature no later than October 1 of each  
36 year. Such report shall be presented to the standing committee on com-  
37 merce in the senate, standing committee on economic development in  
38 the house of representatives, and the joint committee on economic de-  
39 velopment. Such report shall include but not be limited to:

40 (1) The total dollar amount each capco received from all investors  
41 receiving tax credits and any other investors and the identity of all inves-  
42 tors receiving tax credits;

43 (2) the total amount invested by each capco in qualified Kansas busi-

1 nesses, the identity and location of those businesses, the amount invested  
2 in each qualified Kansas business, and the total number of permanent  
3 full-time jobs created or retained by each qualified Kansas business as a  
4 result of the investment.

5 (3) The cumulative amount of any liquidating disbursements received  
6 by the state from the Kansas certified capital companies.

7 New Sec. 8. The commission may revoke the certification of a capco  
8 if any material representation to the commission in connection with the  
9 application process proves to have been falsely made or if the application  
10 materially violates any requirement established by the commission pur-  
11 suant to this act.

12 New Sec. 9 (a) The tax credit established pursuant to this act may  
13 be sold or transferred in accordance with rules and regulations adopted  
14 by the commission. The commission, in cooperation with the secretary of  
15 the department of revenue, shall develop such rules and regulations to  
16 facilitate the operation of the program consistent with the interest of the  
17 state in tracking the transfer of ownership and the use of tax credits  
18 earned by the holder in due course.

19 (b) Any such sale or transfer shall not affect the time schedule for  
20 taking the tax credit, as provided in this act. Any tax credits recaptured  
21 pursuant to section 6 shall be the liability of the taxpayer which actually  
22 claimed the tax credit. In approving the sale or transfer of the tax credit  
23 pursuant to this section, the commission may require the transferor or  
24 the transferee or both the transferor and the transferee to execute guar-  
25 antees or post bonds with respect to any potential tax credit recapture.

26 (c) Any payment received for tax credits is taxable income of the  
27 transferor of the credit and any ~~difference between the transfer price and~~  
28 ~~the sale price of the tax credit shall be taxable income of the transferee.~~

29 (d) The commission shall make and promulgate rules and regulations  
30 consistent with the provisions of this act as are necessary or useful to  
31 carryout the provisions of this act which are necessary to implement the  
32 act.

33 (e) Every final order, decision, license or other official act of the com-  
34 missioner pursuant to this act is subject to administrative review in ac-  
35 cordance with the Kansas administrative procedure act.

36 (f) In view of the objectives of these requirements and the underlying  
37 policies of the act, the act is not available with respect to any transaction  
38 or series of transactions that, although in technical compliance with these  
39 rules, is part of a plan or scheme to evade the requirements of this act or  
40 to distort the benefits entitled to be realized under the act. In such cases,  
41 no investor in any capco shall be entitled to the benefit of any tax credits  
42 provided for hereunder.

move to §2 establishing tax credits

excess of the amount of the tax credit transferred over the payment made for the tax credit.

1 follows: 17-1262. Except as expressly provided in this section, the follow-  
2 ing transactions shall be exempt from the registration requirements of  
3 K.S.A. 17-1254, 17-1255, 17-1257, 17-1258, 17-1259 and 17-1260, and  
4 amendments thereto:

5 (a) Any isolated transaction, whether effected through a broker-  
6 dealer or not.

7 (b) Any nonissuer distribution by or through a registered broker-  
8 dealer of outstanding securities at a price reasonably related to the current  
9 market price of such securities, if Moody's manual, Standard & Poor's  
10 manual, or any recognized securities manual approved by the commis-  
11 sioner, contains the names of the issuer's officers and directors, a balance  
12 sheet of the issuer as of a date within 18 months, and a profit and loss  
13 statement for either the fiscal year preceding that date or the most recent  
14 year of operations. If the commissioner finds that the sale of certain se-  
15 curities in this state under this exemption would work or tend to work a  
16 fraud on purchasers thereof, the commissioner may revoke the exemption  
17 provided by this subsection with respect to such securities by issuing an  
18 order to that effect and sending copies of such order to all registered  
19 broker-dealers.

20 (c) Any nonissuer transaction by a registered broker-dealer pursuant  
21 to an unsolicited order or offer to buy. The commissioner may require,  
22 by rules and regulations, that: (1) The customer acknowledge upon a  
23 specified form that the sale was unsolicited; and (2) a signed copy of each  
24 such form be preserved by the broker-dealer for a specified period.

25 (d) Any transactions in a bond or other evidence of indebtedness  
26 secured by a real or chattel mortgage or deed of trust, or by an agreement  
27 for the sale of real estate or chattels, if the entire mortgage, deed of trust  
28 or agreement, together with all the bonds or other evidences of indebt-  
29 edness secured thereby, is offered and sold as a unit.

30 (e) Any transaction by an executor, administrator, sheriff, marshal,  
31 receiver, trustee in bankruptcy, guardian or conservator; any transaction  
32 executed by a bona fide pledgee without any purpose of evading this act  
33 or any transaction incident to a judicially approved reorganization in  
34 which a security is issued in exchange for one or more outstanding se-  
35 curities, claims or property interests.

36 (f) Any offer or sale to a bank, savings institution, trust company,  
37 insurance company, investment company as defined in the investment  
38 company act of 1940, pension or profit-sharing trust or other financial  
39 institution or institutional buyer or to a broker-dealer or underwriter.

40 (g) Any offer or sale of a preorganization certificate or subscription  
41 if: (1) No commission or other remuneration is paid or given directly or  
42 indirectly for soliciting any prospective subscriber and no advertising has  
43 been published in connection with any such sale; (2) no payment is made

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# SENATE BILL No. 315

By Committee on Commerce

2-12

9 AN ACT concerning venture capital; enacting the Kansas certified capital  
10 company act; amending K.S.A. 1998 Supp. 17-1262 and repealing the  
11 existing section.

12  
13 *Be it enacted by the Legislature of the State of Kansas:*

14 New Section 1. This act shall be known and may be cited as the  
15 "Kansas Certified Capital Company Act". The purpose of this act is to  
16 enhance the development of seed and venture capital in Kansas and to  
17 support the modernization and expansion of the state's rural economy.  
18 As used in this act, the following terms mean:

19 (a) "Certified capital company" means any partnership, corporation,  
20 trust or limited liability company, whether organized on a profit or not  
21 for profit basis, that is domiciled in and qualified to conduct business in  
22 Kansas and that has as its primary business activity, the investment of cash  
23 in qualified Kansas businesses, and which is certified by the securities  
24 commissioner of Kansas as satisfying the criteria of this act.

25 (b) "Capco" means any certified capital company.

26 (c) "Tax credit" means a transferable, non-refundable credit against  
27 the tax imposed by the Kansas income tax act, the premium tax or priv-  
28 ilege fee imposed pursuant to K.S.A. 40-252, and amendments thereto,  
29 or the privilege tax as measured by net income of financial institutions  
30 imposed pursuant to chapter 79, article 11 of the Kansas Statutes  
31 Annotated.

32 (d) "Applicable percentage" means one hundred percent.

33 (e) "Capital in a qualified Kansas business" means any note, stock,  
34 partnership or membership interest or other form of equity investment  
35 or hybrid security, of any nature and description whatsoever, including a  
36 debt instrument or security which has the characteristics of indebtedness  
37 but which provides for conversion into equity or equity participation in-  
38 struments such as options or warrants which are acquired by a Kansas  
39 certified capital company as a result of a transfer of cash to a business.  
40 Capital in a qualified Kansas business shall not include secured debt  
41 instruments.

42 (f) "Certified capital investment" means an investment of cash by an  
43 investor made in such manner as to acquire a beneficial ownership inter-



1 est in a Kansas certified capital company.

2 (g) "Certified capital" means cash, marketable securities and other  
3 liquid assets held by a certified capital company equal to the amount of  
4 certified capital investment made by investors in the certified capital  
5 company.

6 (h) "Commission" means the Kansas securities commission.

7 (i) "Commissioner" means the securities commissioner of Kansas or  
8 a person acting under the supervision of the commissioner.

9 (j) "Investor" means any natural person or entity, including a cor-  
10 poration, limited liability company, general or limited partnership, trust  
11 or limited liability company that invests cash.

12 (k) "Liquidating distribution" means payments remitted to investors  
13 or to the certified capital company derived from earnings.

14 (l) "Person" means any natural person or entity, including a corpo-  
15 ration, limited liability company, general or limited partnership, trust or  
16 limited liability company.

17 (m) "Qualified distribution" means any distribution or payment re-  
18 mitted to equity holders of a certified capital company in connection with  
19 the following:

20 (1) Reasonable costs and expenses of forming, syndicating, managing  
21 or operating the certified capital company;

22 (2) Fees paid to qualified managers for managing or operating the  
23 certified capital company.

24 (n) "Qualified venture capital investment" means the investment of  
25 cash by a Kansas certified capital company in such a manner as to acquire  
26 capital in a qualified Kansas business.

27 (o) "Qualified Kansas business" means:

28 (1) A business that satisfies the requirements of paragraphs (A)  
29 through (B) of this subsection.

30 (A) Such business is independently owned and operated and has its  
31 principal business office located in Kansas or, in the case of a company  
32 domiciled outside the state of Kansas, which certifies that the company's  
33 principal business office will be located in Kansas within six months fol-  
34 lowing the date of the initial investment;

35 (B) such business shall, at the time of the initial qualified venture  
36 capital investment, have no more than 50 full time equivalent employees,  
37 at least fifty percent of whom are resident in Kansas or, in the case of a  
38 company domiciled outside the state of Kansas, certifies that at least fifty  
39 percent of its employees will be resident in Kansas within six months  
40 following the date of the initial qualified venture capital investment;

41 (C) such business is in need of venture capital and cannot obtain  
42 conventional financing to fund its further development and future  
43 operations;

1 (D) such business shall be engaged in commerce for the purpose of  
2 manufacturing, processing or assembling or distributing products, con-  
3 ducting research and development or providing services in interstate  
4 commerce.

5 (E) For businesses involved in commerce for the purpose of provid-  
6 ing services in interstate commerce, that business must demonstrate that  
7 more than fifty percent of its gross revenues are derived from sales out-  
8 side the state of Kansas, or in the case of an early stage business, provide  
9 reasonable documentation that the company will derive at least fifty per-  
10 cent of its gross sales outside the state within a three-year period.

11 (2) Any business which, subject to audit, is properly classified as a  
12 qualified Kansas business at the time of the first qualified venture capital  
13 investment in such business by a Kansas certified capital company shall,  
14 for a period of seven years following the date of such first investment,  
15 continue to be classified as a qualified Kansas business and may receive  
16 follow-on investments from any Kansas certified capital company, and  
17 such follow-on investments shall constitute qualified venture capital in-  
18 vestments even though such business may not meet other qualifications  
19 of this subsection at the time of such follow-on investments.

20 (3) A qualified Kansas business shall not include:

21 (A) Any commercial enterprise primarily engaged in the sale at retail  
22 of goods or services taxable under the Kansas retailer's sales tax act; any  
23 service provider set forth in K.S.A. 17-2707, and amendments thereto;  
24 any bank, savings and loan or lending institution; any real estate, real  
25 estate development or insurance company; or any commercial enterprise  
26 deriving its revenues directly from noncommercial customers in exchange  
27 for personal services;

28 (B) a business engaged primarily as a passive business, irregular or  
29 noncontinuous operations, or which derives substantially all of its income  
30 from passive investments that generate interest, dividends, royalties or  
31 capital gains;

32 (C) a business engaged in oil and gas exploration and development;

33 (D) a subsidiary of a certified capital company;

34 (E) another certified capital company;

35 (F) an affiliate of the certified capital company;

36 (G) an investor of the certified capital company or an affiliate or sub-  
37 sidiary of an investor of the certified capital company unless approved in  
38 writing by the commissioner.

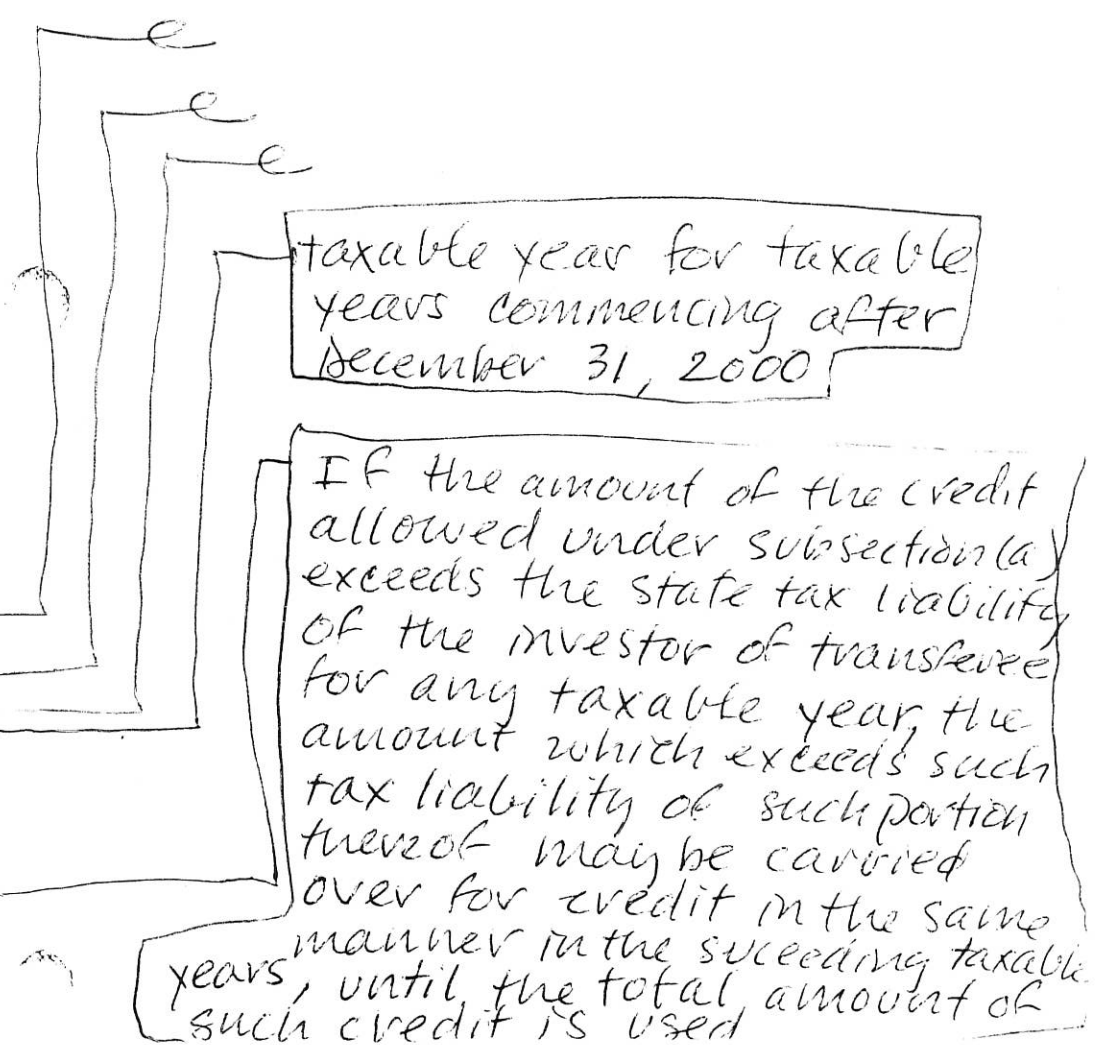
39 (4) At the time of the initial qualified venture capital investment, the  
40 qualified Kansas business shall certify that the business shall remain dom-  
41 icated in Kansas for the next 10 years and any new manufacturing facility  
42 financed directly by a qualified investment shall be located in and shall  
43 remain in Kansas for the 10 years following.

- 1 (p) "Affiliate of a certified capital company" means:
- 2 (1) any person that directly or indirectly, owns, controls or possesses
- 3 the power or ability to vote ten percent or more of the outstanding voting
- 4 securities or other beneficial ownership interests of the Kansas certified
- 5 capital company;
- 6 (2) any person ten percent or more of whose outstanding voting se-
- 7 curities or other beneficial ownership interests are directly or indirectly
- 8 owned, controlled or possessed with the power to be voted by the Kansas
- 9 certified capital company;
- 10 (3) any person directly or indirectly controlling, controlled by, or un-
- 11 der common control with the Kansas certified capital company;
- 12 (4) any partnership in which the Kansas certified capital company is
- 13 a general partner;
- 14 (5) any person who is an officer, director, general partner, managing
- 15 member, manager director or agent of the Kansas certified capital com-
- 16 pany or an immediate family member of such person.

- 17 (q) "Affiliate of an investor" means:
- 18 (1) Any person that directly or indirectly, owns, controls or possesses
- 19 the power or ability to vote ten percent or more of the outstanding voting
- 20 securities or other beneficial ownership interests of the investor;
- 21 (2) any person ten percent or more of whose outstanding voting se-
- 22 curities or other beneficial ownership interests are directly or indirectly
- 23 owned, controlled, or possessed with the power to be voted by the
- 24 investor;
- 25 (3) any person directly or indirectly controlling, controlled by or un-
- 26 der common control with the investor;
- 27 (4) a partnership in which the investor is a general partner;
- 28 (5) any person who is an officer, director or agent of the investor or
- 29 an immediate family member of such officer, director or agent.

30 New Sec. 2. (a) Any investor that makes a certified capital investment  
 31 shall earn a ~~vested~~ tax credit against state tax liability equal to 100% of  
 32 the amount of such investor's certified capital investment. An investor, or  
 33 person to whom the credits were duly transferred, shall be entitled to use  
 34 not more than 10% of the ~~vested~~ credit per year beginning with tax filings  
 35 for calendar year 2001. Any tax credit not used by an investor, or a person  
 36 to whom the credits were duly transferred, in any single year may be  
 37 carried forward and applied against tax liabilities of such investor or trans-  
 38 ferree for subsequent calendar years.

39 (b) ~~A tax credit claimed against state tax liability as described in sub-~~  
 40 ~~section (a) may not exceed the state tax liability of the investor, or person~~  
 41 ~~to whom the credits were duly transferred, for any taxable year. All such~~  
 42 ~~credits against state tax liability may be carried forward indefinitely until~~  
 43 ~~the credits are utilized.~~



1 (c) If the investor is an individual, the investor shall have a personal  
 2 net worth of at least \$1,000,000 and at least ten times the amount of such  
 3 investor's certified capital investment in a capco. The investor's net worth  
 4 shall not include the value of any equity in such investor's primary  
 5 residence.

— move to § 1(j) - definition of investor

6 (d) No certified capital investment in a capco by any one person shall  
 7 be less than \$50,000.

— move to § 1(F) - definition of certified capital investment

8 (e) ~~The commission shall be responsible for the administration of the~~  
 9 ~~tax credits authorized by this act.~~

— tax credit earned allowed

10 (f) ~~The total amount of tax credits which may be allocated by the~~  
 11 ~~commissioner shall not exceed \$50,000,000. The total amount of tax cred-~~  
 12 ~~its which may be claimed under this act shall not exceed \$5,000,000 per~~  
 13 ~~year.~~

14 New Sec. 3. (a) The commissioner may certify profit or not-for-profit  
 15 entities which submit an application to be designated as a capco. The  
 16 commissioner shall compile a list of every capco, including the address  
 17 and telephone number of the capco's principal place of business. The  
 18 commissioner shall forward the list to the secretary of commerce and  
 19 housing. The secretary of commerce and housing shall publicize the list  
 20 in order to inform Kansas companies of the availability of potential in-  
 21 vestment capital. The commission shall review the organizational docu-  
 22 ments for each applicant for certification and the business history of the  
 23 applicant to determine:

fiscal year. The Secretary of Revenue shall allow such credits on a first-come-first-serve basis.

24 (1) that at the time of application, the applicant owns cash, market-  
 25 able securities and other liquid assets valued at no less than \$500,000, or  
 26 that the applicant is designated as an innovation and commercialization  
 27 corporation or an affiliate of an innovation and commercialization cor-  
 28 poration created under the Kansas technology enterprise corporation in-  
 29 novation and commercialization corporation program;

30 (2) that the officers and the board of directors, general partners, trust-  
 31 ees, managing members, or managers, as the case may be, are thoroughly  
 32 acquainted with the requirements of this act and acknowledge such by a  
 33 signed certification.

34 (b) To continue to be certified, the capco must own and shall peri-  
 35 odically provide information to the commissioner as the commissioner  
 36 may require in order for the commissioner to determine that the liquid  
 37 asset base for the certified capital company is at least \$500,000 at all times  
 38 during the capco's participation in the program authorized by this act or  
 39 that such moneys have been used for making qualified venture capital  
 investments.

41 (c) No entity which submits an application to be designated as a capco  
 42 shall be certified by the commissioner if any of its directors, trustees,  
 43 managers, officers, general partners, beneficial owners of 10% or more

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1 of any class of its equity securities, or any promoters employed or oth-  
2 erwise associated with it at the time of such application:

3 (1) Has been affiliated with any company that has filed a registration  
4 statement which is subject to a currently effective stop order entered  
5 pursuant to any state law;

6 (2) has been convicted of any felony or misdemeanor in connection  
7 with the purchase or sale of any security or any felony involving fraud or  
8 deceit including, but not limited to, forgery, embezzlement, obtaining  
9 money under false pretenses, larceny or conspiracy to defraud;

10 (3) is currently subject to any state administrative order or judgment  
11 entered by a state securities administrator or is subject to any state ad-  
12 ministrative order or judgment in which fraud or deceit was found and  
13 an order or judgment was entered;

14 (4) is currently subject to any state administrative order or judgment  
15 which prohibits the use of any exemption from registration in connection  
16 with the purchase or sale of securities;

17 (5) is subject to any order, judgment or decree of any court of com-  
18 petent jurisdiction temporarily or preliminarily restraining or enjoining,  
19 or is subject to any order, judgment or decree of any court of competent  
20 jurisdiction permanently restraining or enjoining that person from engag-  
21 ing in or continuing any conduct or practice in connection with the pur-  
22 chase or sale of any security, rendering investment advice, or involving  
23 the making or any false filing with any state;

24 (6) has been convicted of or plead nolo contendere to any criminal  
25 offense other than a misdemeanor involving motor vehicle violations.

26 (d) The commissioner shall further review documentation regarding  
27 the qualifications of the persons who will actively manage the capco and  
28 make a determination as to whether such persons possessed sufficient  
29 knowledge and professional experience in the areas of investment, ven-  
30 ture capital, business management and evaluation, portfolio management,  
31 and such other area of expertise to the degree that a reasonable person  
32 would be confident in such manager's ability to manage the capco. No  
33 certification shall be issued when it is the opinion of the commissioner  
34 that such persons do not possess this requisite degree of knowledge and  
35 expertise.

36 (e) No investor shall individually, or collectively with or through one  
37 or more affiliates, by means of ownership, agreement or otherwise, own,  
38 control, or possess the power or ability to cause or direct the making of  
39 any qualified venture capital investments by a capco.

40 (f) Within 75 days of application, the commission shall either issue  
41 the certification and notify the secretary of the department of revenue of  
42 such certification or shall refuse the certification and communicate in  
43 detail to the applicant the grounds for the refusal, including any sugges-



1 tions for the removal of those grounds.

2 New Sec. 4. (a) A capco shall have a period of 365 days from the  
3 date of receiving certification from the commissioner in which to procure  
4 the amount of certified capital investment required by subsection (b). All  
5 certified capital investments in the capco shall be received within such  
6 three-hundred-sixty-five-day funding period, notwithstanding the provi-  
7 sions of subsection (c).

8 (b) Before closing its fund of certified capital investment, and pur-  
9 suant to subsection (a) of section 3, and amendments thereto, a capco  
10 shall raise a minimum aggregate certified capital investment of no less  
11 than \$5,000,000. In the case of a capco designated as an innovation and  
12 commercialization corporation or an affiliate of an innovation and com-  
13 mercialization corporation created under the KTEC innovation and com-  
14 mercialization corporation program, such minimum certified capital in-  
15 vestment shall be no less than \$1,000,000. No tax credits shall be issued  
16 ~~by the commissioner until such time when these minimum cumulative~~  
17 ~~investments are met.~~ Failure of a capco to raise the minimum cumulative  
18 investments may result in the revocation of the certification by the  
19 commissioner.

20 (c) Once fully capitalized pursuant to the provisions of subsection (b),  
21 a capco may make application to the commissioner for authorization to  
22 seek additional certified capital investment.

23 New Sec. 5. (a) To continue to be certified, a capco shall make qual-  
24 ified venture capital investments according to the following schedule:

25 (1) Within three years after the date on which a capco is certified as  
26 a capco at least 25% of its certified capital shall be, or have been, used  
27 for making qualified venture capital investments;

28 (2) within four years after the date on which a capco is certified as a  
29 capco at least 40% of its certified capital shall be, or have been, used for  
30 making qualified venture capital investments;

31 (3) within five years after the date on which a capco is certified as a  
32 capco at least 50% of its total certified capital shall be, or have been, used  
33 for making qualified venture capital investments;

34 (4) within seven years after the date on which a capco is certified as  
35 a capco at least 70% of its total certified capital shall be, or have been,  
36 used for making qualified venture capital investments.

37 (5) A capco shall not make an investment in an affiliate of the capco  
38 or an affiliate of an investor. For the purposes of this subsection, if a legal  
39 entity is not an affiliate before a capco initially invests in the entity, it  
40 shall not be deemed to be an affiliate if such capco provides additional  
41 qualified venture capital investment to such entity subsequent to its initial  
42 investment. No corporate officer, employee or shareholder, no limited or  
43 general partner or other person personally affiliated with any capco shall

aggregate  
allowed by the Secretary of Revenue pursuant  
to section 2 for any certified capital  
investment in a particular capco  
until that capco has raised the  
applicable minimum aggregate  
certified capital investment

aggregate

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1 personally invest in any portfolio company regardless of whether the port-  
2 folio company is affiliated with the capco.

3 (6) A capco, at least 15 working days prior to making what it deter-  
4 mines to be any initial qualified venture capital investment, shall first  
5 certify to the commissioner that the company in which it proposes to  
6 invest meets the definition of a qualified Kansas business pursuant to  
7 paragraph (15) of subsection (a) of section 1, and amendments thereto.  
8 The capco shall state the amount of capital it intends to invest and identify  
9 the business in which it intends to make the investment. The capco shall  
10 also provide to the commissioner a written explanation of the basis for its  
11 determination that the business meets the definition of a qualified Kansas  
12 business, if the commissioner determines that the business does not meet  
13 the definition of a qualified Kansas business, the commissioner shall,  
14 within the fifteen-working-day period prior to the making of the proposed  
15 investment, notify the capco of the determination and provide the capco  
16 an explanation thereof. If the commissioner fails to notify the capco of  
17 his or her determination within the 15 working day period prescribed  
18 herein, the business in which the capco proposes to invest shall be  
19 deemed to be a qualified Kansas business. If a capco fails to notify the  
20 commissioner prior to making an initial investment in a business, the  
21 business in which the capco invested shall be deemed not to be a qualified  
22 Kansas business even though the business, at the time of the investment,  
23 met the requirements of paragraph (o) of subsection (a) of section 1, and  
24 amendments thereto;

25 (7) All certified capital which is not then required to be invested in  
26 qualified venture capital investments or which has been previously in-  
27 vested in qualified venture capital investments and returned by the com-  
28 pany, may be held or invested in such manner as the capco, in its discre-  
29 tion, deems appropriate. The proceeds of all certified capital which is  
30 returned by a capco after it was originally invested in qualified venture  
31 capital investments, may be invested in other qualified venture capital  
32 investments and shall be credited toward any requirement in this act with  
33 respect to placing certified capital in qualified venture capital  
34 investments.

35 (b) A capco may make qualified distributions at any time. In order to  
36 lawfully make liquidating distributions, a capco must have invested an  
37 aggregate amount equal to 100% of its certified capital in qualified ven-  
38 ture capital investments.

39 (c) Cumulative liquidating distributions to equity holders in excess of  
40 the certified capital company's original certified capital and any additional  
41 capital contributions to the certified capital company shall be subject to  
42 audit by a nationally recognized, certified public accounting firm accept-  
43 able to the commissioner at the expense of the certified capital company.

1 The audit shall determine whether aggregate cumulative liquidating dis-  
2 tributions to all investors and equity holders, when combined with all tax  
3 credits utilized by investors pursuant to this act, have resulted in an annual  
4 internal rate of return of 15% computed on the sum of total original  
5 certified capital of the certified capital company and any additional capital  
6 contributions to the certified capital company.

7 (d) If at any time of any such distribution made by the capco which  
8 has achieved the annual internal rate of return specified under subsection  
9 (c) such distribution taken together with all other such distributions made  
10 by the certified capital company, other than qualified distributions, ex-  
11 ceeds in the aggregate the sum of the certified capital company's original  
12 certified capital and any additional capital contributions to the certified  
13 capital company, as determined by the audit, the certified capital com-  
14 pany shall, prior to any additional distributions, pay to the Kansas state  
15 treasurer's office 25% of the proportion of such distribution in excess of  
16 such amount.

17 (e) Documents and other materials submitted by Kansas certified  
18 capital companies or by businesses for purposes of original certification  
19 or the continuance of certification shall not be public records if it is de-  
20 termined by the commissioner that disclosure of such information would  
21 compromise trade secrets of qualified Kansas businesses or the privacy  
22 rights of any investor and shall be maintained in a secured environment  
23 by the commissioner.

24 (f) Each capco shall report the following to the commission:

25 (1) As soon as practicable, but in any case no later than 15 days, after  
26 the receipt of a certified capital investment, the name of each investor  
27 from whom the certified capital investment was received, the amount of  
28 each investor's certified capital investment, and the date when the cer-  
29 tified capital investment was received;

30 (2) Each capco shall provide to the commissioner, annual audited  
31 financial statements to the commission within 90 days of the close of the  
32 fiscal year. The audit shall address the methods of operation and conduct  
33 of business of the capco to determine if the capco is complying with the  
34 statutes and program rules and that the funds received by the capco have  
35 been invested in accordance with the time limits provided by this act.

36 (3) At the end of each quarter, that no more than 20% of the assets  
37 of a capco shall be invested in a single qualified Kansas business at any  
38 one time unless the capco can demonstrate that a greater percentage in  
39 a single qualified Kansas business at any one time is the result of losses  
40 suffered by the capco in other qualified venture capital investments.

41 New Sec. 6. To ensure that no qualified venture capital investment  
42 or investor's certified capital investment has been made in violation of  
43 this act, the commissioner shall conduct an annual review of each capco

1 follows: 17-1262. Except as expressly provided in this section, the follow-  
2 ing transactions shall be exempt from the registration requirements of  
3 K.S.A. 17-1254, 17-1255, 17-1257, 17-1258, 17-1259 and 17-1260, and  
4 amendments thereto:

5 (a) Any isolated transaction, whether effected through a broker-  
6 dealer or not.

7 (b) Any nonissuer distribution by or through a registered broker-  
8 dealer of outstanding securities at a price reasonably related to the current  
9 market price of such securities, if Moody's manual, Standard & Poor's  
10 manual, or any recognized securities manual approved by the commis-  
11 sioner, contains the names of the issuer's officers and directors, a balance  
12 sheet of the issuer as of a date within 18 months, and a profit and loss  
13 statement for either the fiscal year preceding that date or the most recent  
14 year of operations. If the commissioner finds that the sale of certain se-  
15 curities in this state under this exemption would work or tend to work a  
16 fraud on purchasers thereof, the commissioner may revoke the exemption  
17 provided by this subsection with respect to such securities by issuing an  
18 order to that effect and sending copies of such order to all registered  
19 broker-dealers.

20 (c) Any nonissuer transaction by a registered broker-dealer pursuant  
21 to an unsolicited order or offer to buy. The commissioner may require,  
22 by rules and regulations, that: (1) The customer acknowledge upon a  
23 specified form that the sale was unsolicited; and (2) a signed copy of each  
24 such form be preserved by the broker-dealer for a specified period.

25 (d) Any transactions in a bond or other evidence of indebtedness  
26 secured by a real or chattel mortgage or deed of trust, or by an agreement  
27 for the sale of real estate or chattels, if the entire mortgage, deed of trust  
28 or agreement, together with all the bonds or other evidences of indebt-  
29 edness secured thereby, is offered and sold as a unit.

30 (e) Any transaction by an executor, administrator, sheriff, marshal,  
31 receiver, trustee in bankruptcy, guardian or conservator; any transaction  
32 executed by a bona fide pledgee without any purpose of evading this act  
33 or any transaction incident to a judicially approved reorganization in  
34 which a security is issued in exchange for one or more outstanding se-  
35 curities, claims or property interests.

36 (f) Any offer or sale to a bank, savings institution, trust company,  
37 insurance company, investment company as defined in the investment  
38 company act of 1940, pension or profit-sharing trust or other financial  
39 institution or institutional buyer or to a broker-dealer or underwriter.

40 (g) Any offer or sale of a preorganization certificate or subscription  
41 if: (1) No commission or other remuneration is paid or given directly or  
42 indirectly for soliciting any prospective subscriber and no advertising has  
43 been published in connection with any such sale; (2) no payment is made

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1 by any subscriber; and (3) such certificate or subscription is expressly  
2 voidable by the subscriber until such subscriber has been notified of final  
3 acceptance or completion of the organization and until the securities sub-  
4 scribed for have been registered. The commissioner may require, by rules  
5 and regulations or by order, reports of sales under this exemption.

6 (h) Any transaction pursuant to an offer to existing security holders  
7 of the issuer, including persons who at the time of the transaction are  
8 holders of convertible securities, nontransferable warrants or transferable  
9 warrants exercisable within 90 days of their issuance, if: (1) No commis-  
10 sion or other remuneration (other than a standby commission) is paid or  
11 given directly or indirectly for soliciting any security holder in this state;  
12 or (2) the issuer first files a notice specifying the terms of the offer and  
13 the commissioner does not by order disallow the exemption within the  
14 next five full business days.

15 (i) Any offer (but not a sale) of a security if: (1) Registration state-  
16 ments for such security have been filed under both this act and the se-  
17 curities act of 1933 if no stop order or refusal order is in effect and no  
18 public proceeding or examination looking toward such an order is pending  
19 under either act; or (2) a registration statement for such security has been  
20 filed under K.S.A. 17-1256 or 17-1258, and amendments thereto, no stop  
21 order or emergency order issued pursuant to K.S.A. 17-1260, and amend-  
22 ments thereto, is in effect and the offer is made on behalf of the issuer  
23 by a registered broker-dealer.

24 (j) The issuance of any stock dividend, whether the corporation dis-  
25 tributing the dividend is the issuer of the stock or not, if nothing of value  
26 is given by stockholders for the distribution other than the surrender of  
27 a right to a cash dividend where the stockholder can elect to take a div-  
28 idend in cash or stock.

29 (k) A transaction involving the distribution of the securities of an is-  
30 suer to the security holders of another person in connection with a  
31 merger, consolidation, exchange of securities, sale of assets or other re-  
32 organizations to which the issuer, or its parent or subsidiary, and the other  
33 person, or its parent or subsidiary, are parties, if:

34 (1) The securities to be distributed are registered under the securities  
35 act of 1933 before the consummation of the transaction; or

36 (2) the securities to be distributed are not required to be registered  
37 under the securities act of 1933, written notice of the transaction and a  
38 copy of the materials, if any, by which approval of the transaction will be  
39 solicited is given to the commissioner at least 10 days before the consum-  
40 mation of the transaction and the commissioner does not disallow, by  
41 order, the exemption within the next 10 days.

42 (l) The offer or sale of securities by an issuer that is a corporation,  
43 limited partnership or limited liability company formed under the laws

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1 by any subscriber; and (3) such certificate or subscription is expressly  
2 voidable by the subscriber until such subscriber has been notified of final  
3 acceptance or completion of the organization and until the securities sub-  
4 scribed for have been registered. The commissioner may require, by rules  
5 and regulations or by order, reports of sales under this exemption.

6 (h) Any transaction pursuant to an offer to existing security holders  
7 of the issuer, including persons who at the time of the transaction are  
8 holders of convertible securities, nontransferable warrants or transferable  
9 warrants exercisable within 90 days of their issuance, if: (1) No commis-  
10 sion or other remuneration (other than a standby commission) is paid or  
11 given directly or indirectly for soliciting any security holder in this state;  
12 or (2) the issuer first files a notice specifying the terms of the offer and  
13 the commissioner does not by order disallow the exemption within the  
14 next five full business days.

15 (i) Any offer (but not a sale) of a security if: (1) Registration state-  
16 ments for such security have been filed under both this act and the se-  
17 curities act of 1933 if no stop order or refusal order is in effect and no  
18 public proceeding or examination looking toward such an order is pending  
19 under either act; or (2) a registration statement for such security has been  
20 filed under K.S.A. 17-1256 or 17-1258, and amendments thereto, no stop  
21 order or emergency order issued pursuant to K.S.A. 17-1260, and amend-  
22 ments thereto, is in effect and the offer is made on behalf of the issuer  
23 by a registered broker-dealer.

24 (j) The issuance of any stock dividend, whether the corporation dis-  
25 tributing the dividend is the issuer of the stock or not, if nothing of value  
26 is given by stockholders for the distribution other than the surrender of  
27 a right to a cash dividend where the stockholder can elect to take a div-  
28 idend in cash or stock.

29 (k) A transaction involving the distribution of the securities of an is-  
30 suer to the security holders of another person in connection with a  
31 merger, consolidation, exchange of securities, sale of assets or other re-  
32 organizations to which the issuer, or its parent or subsidiary, and the other  
33 person, or its parent or subsidiary, are parties, if:

34 (1) The securities to be distributed are registered under the securities  
35 act of 1933 before the consummation of the transaction; or

36 (2) the securities to be distributed are not required to be registered  
37 under the securities act of 1933, written notice of the transaction and a  
38 copy of the materials, if any, by which approval of the transaction will be  
39 solicited is given to the commissioner at least 10 days before the consum-  
40 mation of the transaction and the commissioner does not disallow, by  
41 order, the exemption within the next 10 days.

42 (l) The offer or sale of securities by an issuer that is a corporation,  
43 limited partnership or limited liability company formed under the laws



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1 of the state of Kansas, if: (1) The aggregate number of sales by the issuer  
2 in the twelve-month period ending on the date of the sale does not exceed  
3 20 sales; (2) the seller believes that the purchaser is purchasing for in-  
4 vestment; (3) no commission nor other remuneration is paid or given,  
5 directly or indirectly, for soliciting the purchaser; and (4) neither the  
6 issuer nor any person acting on its behalf shall offer or sell the securities  
7 by any form of general solicitation or general advertising, including, but  
8 not limited to, the following: (A) Any advertisement, article, notice or  
9 other communication published in any newspaper, magazine or similar  
10 media or broadcast over television or radio or (B) any seminar or meeting  
11 whose attendees have been invited by any general solicitation or general  
12 advertising.

13 In calculating the number of sales in a twelve-month period, sales made  
14 in violation of K.S.A. 17-1255, and amendments thereto, and sales exempt  
15 from registration under subsection (a) or (l) shall be taken into account.  
16 For purposes of the exemption in this subsection, a husband and wife  
17 shall be considered as one purchaser. A corporation, partnership, asso-  
18 ciation, joint-stock company, trust or other unincorporated organization  
19 shall be considered as one purchaser unless it was organized for the pur-  
20 pose of acquiring the purchased securities. In such case each beneficial  
21 owner of equity interest or equity securities in the entity shall be consid-  
22 ered a separate purchaser. The commissioner may withdraw this exemp-  
23 tion or impose conditions upon its use.

24 (m) Any transaction pursuant to rules and regulations adopted by the  
25 commissioner for limited offerings which was adopted for the purpose of  
26 furthering the objectives of compatibility with federal exemptions and  
27 uniformity among the states.

28 (n) Any transaction pursuant to rules and regulations adopted by the  
29 commissioner concerning the offer or sale of an oil, gas or mining lease,  
30 fee or title if the commissioner finds that registration is not necessary or  
31 appropriate for the protection of investors.

32 (o) Any offer or sale by an investment company, as defined by K.S.A.  
33 16-630, and amendments thereto, of its investment certificates.

34 (p) The offer or sale of a security, issued by Kansas Venture Capital,  
35 Inc., or its successors.

36 (q) *The offer or sale of a security issued by capco as defined in section*  
37 *1, and amendments thereto.*

38 Sec. 11. K.S.A. 1998 Supp. 17-1262 is hereby repealed.

39 Sec. 12. This act shall take effect and be in force from and after its  
40 publication in the statute book.

## SB 315 - Key Points

- ◆ Seed capital is virtually non-existent in Kansas today.
- ◆ Bill is catalyst for formation of private seed capital industry in Kansas.
- ◆ Not a technology company bill. Only real estate, retail, and financial and personal services are excluded.
- ◆ Businesses in all 105 counties are eligible for investments.
- ◆ 100 percent tax credit to accredited investor in CapCo, *with suggested minimum investment of \$25,000.*
- ◆ CapCo's would invest only in Kansas companies with *less than \$1 million in revenue and less than five years old.*
- ◆ Companies receiving investment agree to stay in Kansas for at least ten years.
- ◆ \$50 million maximum credits available with no more than \$5 million to be claimed per year.
- ◆ Total tax credits will not exceed \$10 million to investors in any single CapCo.
- ◆ A minimum of \$5 million investment in each CapCo is required.
- ◆ Bill is designed to attract out-of-state capital to Kansas through transferrable tax credits.
- ◆ CapCo managers screened for competency to ensure success of CapCo and positive economic benefits to state in return for tax credits.
- ◆ Purpose of securities regulations is to protect investors.

With publicly traded companies (stock market and mutual funds), investor protection is through public reporting requirements imposed on companies.

With privately traded companies (seed capital funds), investor protection is through "accredited investor only" restriction.

- ◆ Securities Commission has audit authority and other oversight powers.
- ✕ ◆ *Department of Revenue would administer tax credits.*
- ◆ State shares in financial success of CapCo's: 25 percent of distributions after guaranteed 15 percent IRR.
- ◆ Bill reflects lessons learned from other states' CapCo's and Kansas' 1986 tax credits

Senate Commerce Committee

Date: 3-19-99

Attachment # 3

\* Suggested amendments are in italics.

# SENATE BILL No. 315

By Committee on Commerce

2-12

9 AN ACT concerning venture capital; enacting the Kansas certified capital  
10 company act; amending K.S.A. 1998 Supp. 17-1262 and repealing the  
11 existing section.

12  
13 *Be it enacted by the Legislature of the State of Kansas:*

14 New Section 1. This act shall be known and may be cited as the  
15 "Kansas Certified Capital Company Act". The purpose of this act is to  
16 enhance the development of seed and venture capital in Kansas and to  
17 ~~support the modernization and expansion of the state's rural economy.~~  
18 As used in this act, the following terms mean:

19 (a) "Certified capital company" means any partnership, corporation,  
20 trust or limited liability company, whether organized on a profit or not  
21 for profit basis, that is domiciled in and qualified to conduct business in  
22 Kansas and that has as its primary business activity, the investment of cash  
23 in qualified Kansas businesses, and which is ~~(certified) by the securities~~  
24 commissioner of Kansas ~~(as satisfying the criteria) of this act.~~

25 (b) "Capco" means any certified capital company.

26 (c) "Tax credit" means a transferable, non-refundable credit against  
27 the tax imposed by the Kansas income tax act, the premium tax or priv-  
28 ilege fee imposed pursuant to K.S.A. 40-252, and amendments thereto,  
29 or the privilege tax as measured by net income of financial institutions  
30 imposed pursuant to chapter 79, article 11 of the Kansas Statutes  
31 Annotated.

32 (d) "Applicable percentage" means one hundred percent.

33 (e) "Capital in a qualified Kansas business" means any note, stock,  
34 partnership or membership interest or other form of equity investment  
35 or hybrid security, of any nature and description whatsoever, including a  
36 debt instrument or security which has the characteristics of indebtedness  
37 but which provides for conversion into equity or equity participation in-  
38 struments such as options or warrants which are acquired by a Kansas  
39 certified capital company as a result of a transfer of cash to a business.  
40 Capital in a qualified Kansas business shall not include secured debt  
41 instruments.

42 (f) "Certified capital investment" means an investment of cash by an  
43 investor ~~made in such manner as to acquire a beneficial ownership inter-~~

unless the context clearly requires otherwise

regulated

in accordance with the provisions

which is certified by the securities  
commissioner to have been

Senate Commerce Committee

Date 3-19-99

Attachment # H-1 thru H-9

42

1 est in a Kansas certified capital company.  
2 (g) "Certified capital" means cash, marketable securities and other  
3 liquid assets held by a certified capital company equal to the amount of  
4 certified capital investment made by investors in the certified capital  
5 company.

6 (h) "Commission" means the Kansas securities commission.

7 (i) "Commissioner" means the securities commissioner of Kansas or  
8 a person acting under the supervision of the commissioner.

9 (j) "Investor" means any natural person or entity, including a cor-  
10 poration, limited liability company, general or limited partnership, trust  
11 or limited liability company that invests cash.

12 (k) "Liquidating distribution" means payments remitted to investors  
13 or to the certified capital company derived from earnings.

14 (l) "Person" means any natural person or entity, including a corpo-  
15 ration, limited liability company, general or limited partnership, trust or  
16 limited liability company.

17 (m) "Qualified distribution" means any distribution or payment re-  
18 mitted to equity holders of a certified capital company in connection with  
19 the following:

20 (1) Reasonable costs and expenses of forming, syndicating, managing  
21 or operating the certified capital company;

22 (2) Fees paid to qualified managers for managing or operating the  
23 certified capital company.

24 (n) "Qualified venture capital investment" means the investment of  
25 cash by a Kansas certified capital company in such a manner as to acquire  
26 capital in a qualified Kansas business.

27 (o) "Qualified Kansas business" means:

28 (1) A business that satisfies the requirements of paragraphs (A)  
29 through (B) of this subsection.

30 (A) Such business is independently owned and operated and has its  
31 principal business office located in Kansas or, in the case of a company  
32 domiciled outside the state of Kansas, which certifies that the company's  
33 principal business office will be located in Kansas within six months fol-  
34 lowing the date of the initial investment;

35 (B) such business shall, at the time of the initial qualified venture  
36 capital investment, have no more than 50 full time equivalent employees,  
37 at least fifty percent of whom are resident in Kansas or, in the case of a  
38 company domiciled outside the state of Kansas, certifies that at least fifty  
39 percent of its employees will be resident in Kansas within six months  
40 following the date of the initial qualified venture capital investment;

41 (C) such business is in need of venture capital and cannot obtain  
42 conventional financing to fund its further development and future  
43 operations;

If the investor is an individual natural person, the investor shall have a personal net worth of not less than \$1,000,000 and such net worth shall be at least ten times the amount of the investor's certified capital investment in a capco. The investor's net worth shall not include any equity in the investor's primary residence.

(F)

At least 50% of the employees of such business shall be resident within the state or certify that at least 50% of its employees shall be residents within the state within six months following the date of initial investment.

(C) Such business shall, at the time of the initial qualified venture capital investment, have been in existence for five years or less and have gross sales during its most recent fiscal year of not more than \$1,000,000.

(E)

2-4

1 (D) such business shall be engaged in commerce for the purpose of  
2 manufacturing, processing or assembling or distributing products, con-  
3 ducting research and development or providing services in interstate  
4 commerce.

(F)

5 (E) For businesses involved in commerce for the purpose of provid-  
6 ing services in interstate commerce, that business must demonstrate that  
7 more than fifty percent of its gross revenues are derived from sales out-  
8 side the state of Kansas, or ~~(in the case of an early stage business)~~ provide  
9 reasonable documentation that the company will derive at least fifty per-  
10 cent of its gross sales outside the state within a three-year period.

11 (2) Any business which, subject to audit, is properly classified as a  
12 qualified Kansas business at the time of the first qualified venture capital  
13 investment in such business by a Kansas certified capital company shall,  
14 for a period of seven years following the date of such first investment,  
15 continue to be classified as a qualified Kansas business and may receive  
16 follow-on investments from any Kansas certified capital company, and  
17 such follow-on investments shall constitute qualified venture capital in-  
18 vestments even though such business may not meet other qualifications  
19 of this subsection at the time of such follow-on investments.

20 (3) A qualified Kansas business shall not include:

21 (A) Any commercial enterprise primarily engaged in the sale at retail  
22 of goods or services taxable under the Kansas retailer's sales tax act; any  
23 service provider set forth in K.S.A. 17-2707, and amendments thereto;  
24 any bank, savings and loan or lending institution; any real estate, real  
25 estate development or insurance company; or any commercial enterprise  
26 deriving its revenues directly from noncommercial customers in exchange  
27 for personal services;

28 (B) a business engaged primarily as a passive business, irregular or  
29 noncontinuous operations, or which derives substantially all of its income  
30 from passive investments that generate interest, dividends, royalties or  
31 capital gains;

32 (C) a business engaged in oil and gas exploration and development;

33 (D) a subsidiary of a certified capital company;

34 (E) another certified capital company;

35 (F) an affiliate of the certified capital company;

36 (G) an investor of the certified capital company or an affiliate or sub-  
37 sidiary of an investor of the certified capital company unless approved in  
38 writing by the commissioner.

39 (4) At the time of the initial qualified venture capital investment, the  
40 qualified Kansas business shall certify that the business shall remain dom-  
41 icated in Kansas for the next 10 years and any new manufacturing facility  
42 financed directly by a qualified investment shall be located in and shall  
43 remain in Kansas for the 10 years following.

to the commissioner

H-H

1 (p) "Affiliate of a certified capital company" means:

2 (1) any person that directly or indirectly, owns, controls or possesses  
3 the power or ability to vote ten percent or more of the outstanding voting  
4 securities or other beneficial ownership interests of the Kansas certified  
5 capital company;

6 (2) any person ten percent or more of whose outstanding voting se-  
7 curities or other beneficial ownership interests are directly or indirectly  
8 owned, controlled or possessed with the power to be voted by the Kansas  
9 certified capital company;

10 (3) any person directly or indirectly controlling, controlled by, or un-  
11 der common control with the Kansas certified capital company;

12 (4) any partnership in which the Kansas certified capital company is  
13 a general partner;

14 (5) any person who is an officer, director, general partner, managing  
15 member, manager director or agent of the Kansas certified capital com-  
16 pany or an immediate family member of such person.

17 (q) "Affiliate of an investor" means:

18 (1) Any person that directly or indirectly, owns, controls or possesses  
19 the power or ability to vote ten percent or more of the outstanding voting  
20 securities or other beneficial ownership interests of the investor;

21 (2) any person ten percent or more of whose outstanding voting se-  
22 curities or other beneficial ownership interests are directly or indirectly  
23 owned, controlled, or possessed with the power to be voted by the  
24 investor;

25 (3) any person directly or indirectly controlling, controlled by or un-  
26 der common control with the investor;

27 (4) a partnership in which the investor is a general partner;

28 (5) any person who is an officer, director or agent of the investor or  
29 an immediate family member of such officer, director or agent.

30 New Sec. 2. (a) Any investor that makes a certified capital investment  
31 shall earn a ~~vested~~ tax credit against state tax liability equal to 100% of  
32 the amount of such investor's certified capital investment. An investor, or  
33 person to whom the credits were duly transferred, shall be entitled to ~~use~~  
34 not more than 10% of the ~~vested~~ credit per year beginning with tax filings  
35 ~~for calendar year 2001~~. Any tax credit not used by an investor, or a person  
36 to whom the credits were duly transferred, in any single year may be  
37 carried forward and applied against tax liabilities of such investor or trans-  
38 ferree for subsequent calendar years.

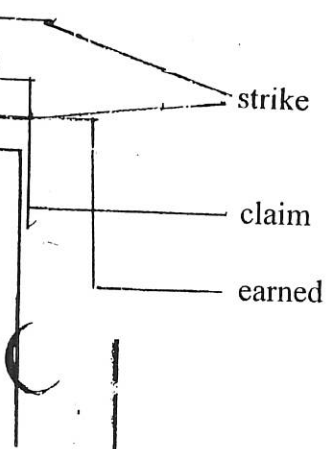
39 (b) A tax credit claimed against state tax liability as described in sub-  
40 section (a) may not exceed the state tax liability of the investor, or person  
41 to whom the credits were duly transferred, for any taxable year. All such  
42 credits against state tax liability may be carried forward indefinitely until  
43 the credits are utilized.

(r) "in existence" means the first day of sale

strike

claim

earned





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1 ~~(c) If the investor is an individual, the investor shall have a personal~~  
2 ~~net worth of at least \$1,000,000 and at least ten times the amount of such~~  
3 ~~investor's certified capital investment in a capco. The investor's net worth~~  
4 ~~shall not include the value of any equity in such investor's primary~~  
5 ~~residence.~~

6 (d) No certified capital investment in a capco by any one person shall  
7 be less than \$50,000

\$25,000

8 ~~(e) The commission shall be responsible for the administration of the~~  
9 ~~tax credits authorized by this act.~~

10 (f) The total amount of tax credits which may be allocated by the  
11 commissioner shall not exceed \$50,000,000. The total amount of tax cred-  
12 its which may be claimed under this act shall not exceed \$5,000,000 per  
13 year.

14 New Sec. 3. (a) The commissioner may certify profit or not-for-profit  
15 entities which submit an application to be designated as a capco. The  
16 commissioner shall compile a list of every capco, including the address  
17 and telephone number of the capco's principal place of business. The  
18 commissioner shall forward the list to the secretary of commerce and  
19 housing. The secretary of commerce and housing shall publicize the list  
20 in order to inform Kansas companies of the availability of potential in-  
21 vestment capital. ~~The commission shall review the organizational docu-~~  
22 ~~ments for each applicant for certification and the business history of the~~  
23 ~~applicant to determine:~~

commissioner

24 (1) that at the time of application, the applicant owns cash, market-  
25 able securities and other liquid assets valued at no less than \$500,000, or  
26 that the applicant is designated as an innovation and commercialization  
27 corporation or an affiliate of an innovation and commercialization cor-  
28 poration created under the Kansas technology enterprise corporation in-  
29 novation and commercialization corporation program;

30 (2) that the officers and the board of directors, general partners, trus-  
31 tees, managing members, or managers, as the case may be, are thoroughly  
32 acquainted with the requirements of this act and acknowledge such by a  
33 signed certification.

34 (b) To continue to be certified, the capco must own and shall peri-  
35 odically provide information to the commissioner as the commissioner  
36 may require in order for the commissioner to determine that the liquid  
37 asset base for the certified capital company is at least \$500,000 at all times  
38 during the capco's participation in the program authorized by this act or  
39 that such moneys have been used for making qualified venture capital  
40 investments.

41 (c) No entity which submits an application to be designated as a capco  
42 shall be certified by the commissioner if any of its directors, trustees,  
43 managers, officers, general partners, beneficial owners of 10% or more

4-6

1 tions for the removal of those grounds.

2 New Sec. 4. (a) A capco shall have a period of 365 days from the  
3 date of receiving certification from the commissioner in which to procure  
4 the amount of certified capital investment required by subsection (b). All  
5 certified capital investments in the capco shall be received within such  
6 three-hundred-sixty-five-day funding period, notwithstanding the provi-  
7 sions of subsection (c).

8 (b) Before closing its fund of certified capital investment, and pur-  
9 suant to subsection (a) of section 3, and amendments thereto, a capco  
10 shall raise a ~~minimum~~ aggregate certified capital investment of no less  
11 than \$5,000,000. In the case of a capco designated as an innovation and  
12 commercialization corporation or an affiliate of an innovation and com-  
13 mercialization corporation created under the KTEC innovation and com-  
14 mercialization corporation program, such minimum certified capital in-  
15 vestment shall be no less than \$1,000,000. No tax credits shall be issued  
16 by the commissioner until such time when these minimum cumulative  
17 investments are met. Failure of a capco to raise the minimum cumulative  
18 investments may result in the revocation of the certification by the  
19 commissioner.

20 (c) Once fully capitalized pursuant to the provisions of subsection (b),  
21 a capco may make application to the commissioner for authorization to  
22 seek additional certified capital investment.

23 New Sec. 5. (a) To continue to be certified, a capco shall make qual-  
24 ified venture capital investments according to the following schedule:

25 (1) Within three years after the date on which a capco is certified as  
26 a capco at least 25% of its certified capital shall be, or have been, used  
27 for making qualified venture capital investments;

28 (2) within four years after the date on which a capco is certified as a  
29 capco at least 40% of its certified capital shall be, or have been, used for  
30 making qualified venture capital investments;

31 (3) within five years after the date on which a capco is certified as a  
32 capco at least 50% of its total certified capital shall be, or have been, used  
33 for making qualified venture capital investments;

34 (4) within seven years after the date on which a capco is certified as  
35 a capco at least 70% of its total certified capital shall be, or have been,  
36 used for making qualified venture capital investments.

37 (5) A capco shall not make an investment in an affiliate of the capco  
38 or an affiliate of an investor. For the purposes of this subsection, if a legal  
39 entity is not an affiliate before a capco initially invests in the entity, it  
40 shall not be deemed to be an affiliate if such capco provides additional  
41 qualified venture capital investment to such entity subsequent to its initial  
42 investment. No corporate officer, employee or shareholder, no limited or  
43 general partner or other person personally affiliated with any capco shall

No capco shall raise in excess of  
\$10,000,000 in certified capital investment  
subject to the earning of tax credits

14-17

1 personally invest in any portfolio company regardless of whether the port-  
2 folio company is affiliated with the capco.

3 (6) A capco, at least 15 working days prior to making what it deter-  
4 mines to be any initial qualified venture capital investment, shall first  
5 certify to the commissioner that the company in which it proposes to  
6 invest meets the definition of a qualified Kansas business pursuant to  
7 ~~paragraph (15) of subsection (a)~~ of section 1, and amendments thereto.

8 The capco shall state the amount of capital it intends to invest and identify  
9 the business in which it intends to make the investment. The capco shall  
10 also provide to the commissioner a written explanation of the basis for its  
11 determination that the business meets the definition of a qualified Kansas  
12 business, if the commissioner determines that the business does not meet  
13 the definition of a qualified Kansas business, the commissioner shall,  
14 within the fifteen-working-day period prior to the making of the proposed  
15 investment, notify the capco of the determination and provide the capco  
16 an explanation thereof. If the commissioner fails to notify the capco of  
17 his or her determination within the 15 working day period prescribed  
18 herein, the business in which the capco proposes to invest shall be  
19 deemed to be a qualified Kansas business. If a capco fails to notify the  
20 commissioner prior to making an initial investment in a business, the  
21 business in which the capco invested shall be deemed not to be a qualified  
22 Kansas business even though the business, at the time of the investment,  
23 met the requirements of ~~paragraph (a) of subsection (a)~~ of section 1, and  
24 amendments thereto;

subsection (o)

25 (7) All certified capital which is not then required to be invested in  
26 qualified venture capital investments or which has been previously in-  
27 vested in qualified venture capital investments and returned by the com-  
28 pany, may be held or invested in such manner as the capco, in its discre-  
29 tion, deems appropriate. The proceeds of all certified capital which is  
30 returned by a capco after it was originally invested in qualified venture  
31 capital investments, may be invested in other qualified venture capital  
32 investments and shall be credited toward any requirement in this act with  
33 respect to placing certified capital in qualified venture capital  
34 investments.

35 (b) A capco may make qualified distributions at any time. In order to  
36 lawfully make liquidating distributions, a capco must have invested an  
37 aggregate amount equal to 100% of its certified capital in qualified ven-  
38 ture capital investments.

39 (c) Cumulative liquidating distributions to equity holders in excess of  
40 the certified capital company's original certified capital and any additional  
41 capital contributions to the certified capital company shall be subject to  
42 audit by a nationally recognized, certified public accounting firm accept-  
43 able to the commissioner, at the expense of the certified capital company.

8-4

1 The audit shall determine whether aggregate cumulative liquidating dis-  
2 tributions to all investors and equity holders, when combined with all tax  
3 credits utilized by investors pursuant to this act, have resulted in an annual  
4 internal rate of return of 15% computed on the sum of total original  
5 certified capital of the certified capital company and any additional capital  
6 contributions to the certified capital company.

7 (d) If at any time of any such distribution made by the capco which  
8 has achieved the annual internal rate of return specified under subsection  
9 (c) such distribution taken together with all other such distributions made  
10 by the certified capital company, other than qualified distributions, ex-  
11 ceeds in the aggregate the sum of the certified capital company's original  
12 certified capital and any additional capital contributions to the certified  
13 capital company, as determined by the audit, the certified capital com-  
14 pany shall, prior to any additional distributions, pay to the [Kansas] state  
15 treasury ~~(the)~~ 25% of the proportion of such distribution in excess of  
16 such amount.

for deposit in the state general fund

17 (e) Documents and other materials submitted by Kansas certified  
18 capital companies or by businesses for purposes of original certification  
19 or the continuance of certification shall not be public records if it is de-  
20 termined by the commissioner that disclosure of such information would  
21 compromise trade secrets of qualified Kansas businesses or the privacy  
22 rights of any investor and shall be maintained in a secured environment  
23 by the commissioner.

24 (f) Each capco shall report the following to the commission:

25 (1) As soon as practicable, but in any case no later than 15 days, after  
26 the receipt of a certified capital investment, the name of each investor  
27 from whom the certified capital investment was received, the amount of  
28 each investor's certified capital investment, and the date when the cer-  
29 tified capital investment was received;

30 (2) Each capco shall provide to the commissioner, annual audited  
31 financial statements to the commission within 90 days of the close of the  
32 fiscal year. The audit shall address the methods of operation and conduct  
33 of business of the capco to determine if the capco is complying with the  
34 statutes and program rules and that the funds received by the capco have  
35 been invested in accordance with the time limits provided by this act.

36 (3) At the end of each quarter, that no more than 20% of the assets  
37 of a capco shall be invested in a single qualified Kansas business at any  
38 one time unless the capco can demonstrate that a greater percentage in  
39 a single qualified Kansas business at any one time is the result of losses  
40 suffered by the capco in other qualified venture capital investments.

41 New Sec. 6. To ensure that no qualified venture capital investment  
42 or investor's certified capital investment has been made in violation of  
43 this act, the commissioner shall conduct an annual review of each capco

(g) Any materials related to the sale of ownership in a capco or soliciting investment in a capco shall include the following statement:

By authorizing the formation of a certified capital company. The State of Kansas does not endorse the quality of management or the potential for earnings of a particular company and is not liable for damages or losses to an investor in the company. The use of the term "certified" in an offering does not constitute a recommendation or endorsement of the investment by the Kansas Securities Commission.

(h) The commissioner may establish reasonable initial filing fees for applications for certification pursuant to this act and may also establish an annual nonrefundable fee for capcos seeking ongoing certification.

5-H

1 to determine if the capco is complying with the requirements of certifi-  
2 cation, and shall advise the capco as to the status of its investments as  
3 qualified venture capital investments. The costs of the annual review shall  
4 be paid by each capco according to a reasonable fee schedule adopted by  
5 the commission.

6 (b) Any material violation of this act/shall be grounds for decertifi-  
7 cation under this section. If the commission determines that a company  
8 is not in compliance with any requirements for continuing in certification,  
9 it shall, by written notice, inform the officers of the company and the  
10 board of directors, managers, trustees or general partners that they may  
11 be decertified within 120 days from the date of mailing of the notice,  
12 unless they correct the deficiencies detailed in the notice and demon-  
13 strate to the commissioner's satisfaction that the capco is again in com-  
14 pliance with the requirements for certification as determined by the  
15 commissioner.

16 (c) At the end of the one-hundred-twenty-day grace period, if the  
17 capco is still not in compliance, the commission may then send a notice  
18 of decertification to the capco and to the secretary of department of  
19 revenue. Decertification of a capco prior to the capco meeting all require-  
20 ments of paragraph (1) through (3), of subsection (a) of section 5, and  
21 amendments thereto, shall cause the recapture of all tax credits previously  
22 claimed by an investor/and the forfeiture of all future tax credits to oth-  
23 erwise be claimed by an investor/with respect to his or her certified capital  
24 investment in the capco. Decertification of a capco after it has met all  
25 requirements of paragraphs (1) to (3) of subsection (a) of section 5, and  
26 amendments thereto, shall cause the forfeiture of tax credits commencing  
27 with the taxable year of the investor in which the decertification arose  
28 and for all future taxable years with no recapture of tax credits obtained  
29 by an investor with respect to the investor's tax years which ended before  
30 the decertification occurred. Once a capco has invested 100% of its cer-  
31 tified capital in qualified Kansas businesses, all future tax credits to be  
32 claimed by investors with respect to said capco pursuant to this act shall  
33 be nonforfeitable.

34 New Sec. 7. The commissioner shall prepare and submit an annual  
35 report to the governor and the legislature no later than October 1 of each  
36 year. Such report shall be presented to the standing committee on com-  
37 merce in the senate, standing committee on economic development in  
38 the house of representatives, and the joint committee on economic de-  
39 velopment. Such report shall include but not be limited to:

40 (1) The total dollar amount each capco received from all investors  
41 receiving tax credits and any other investors and the identity of all inves-  
42 tors receiving tax credits;

43 (2) the total amount invested by each capco in qualified Kansas busi-

by a capco

commissioner

along with a list of the decertified capital investment by investor and transferee

or transferee

(4)

commissioner