

Approved: March 21, 2000
Date

MINUTES OF THE SENATE COMMERCE COMMITTEE.

The meeting was called to order by Chairperson Alicia Salisbury at 8:00 a.m. on March 17, 2000 in Room 123-S of the Capitol.

All members were present except: Senator Feleciano

Committee staff present: Lynne Holt, Legislative Research Department
Jerry Ann Donaldson, Legislative Research Department
Bob Nugent, Revisor of Statutes
Betty Bomar, Secretary

Conferees appearing before the committee:

Major General Gregory B. Gardner, Adjutant General
Judy Moler, Kansas Association of Counties
Lieutenant Governor/Secretary Gary Sherrer
Charles Ranson, President, Kansas, Inc.

Others attending: See attached list

HB 2945 - Task force to make recommendations to legislature regarding 911 and E911

Major General Gregory B. Gardner, Adjutant General of Kansas, stated the Adjutant General's Office is minimally involved in the emergency network, and requested that they not be included as a member of the task force created by **HB 2945**. Major General Gardner suggested that a member of the emergency medical service and a firefighter be included on the task force.

Judy Moler, Kansas Association of Counties (KAC), stated KAC prefers the provisions of **SCR 1641** to **HB 2945**.

Senator Jordan moved, seconded by Senator Barone, that HB 2945 be struck in its entirety and the provisions of SCR 1641 be incorporated into a substitute for HB 2945, and be amended on Page 2, by adding "and a firefighter", and striking "The Adjutant General or the Adjutant General's designee". The voice vote was in favor of the motion.

Senator Donovan moved, seconded by Senator Jordan, that substitute for HB 2945 as amended be recommended favorably for passage. The recorded vote was in favor of the motion.

HB 2938 - Relaxation of restrictions on interstate practice of public accountancy

Senator Ranson moved, seconded by Senator Steffes, that HB 2938 be amended at Page 2, line 15, following the word "of" by inserting "professional" and adding a "y" to the word "dishonest". The voice vote was in favor of the motion.

Senator Barone moved, seconded by Senator Steffes, that HB 2938 be conceptually amended on Page 13, by inserting an "administrative appeal process for firms". The voice vote was in favor of the motion.

Senator Steffes moved, seconded by Senator Barone, that HB 2938 be recommended favorably for passage as amended. The recorded vote was in favor of the motion.

HB 2769 - Variance for nonconforming boilers and pressure vessels

Senator Steineger moved, seconded by Senator Donovan, that HB 2769 be recommended favorably for passage and placed on the consent calendar. The recorded vote was in favor of the

CONTINUATION SHEET

motion.

HB 2688 Capital formation company act

Lieutenant Governor/Secretary Gary Sherrer, Kansas Department of Commerce and Housing (KDOC&H), in response to a question posed to him yesterday regarding his "last minute" opposition to **HB 2688**, referred to the Preliminary Minutes of the Joint Committee on Economic Development, dated December 2, 1999, wherein Steve Kelly stated the reservations of the KDOC&H with the proposed legislation. (Attachment 1)

In responding to Senator Ranson's request for clarification of his March 16 testimony, Lieutenant Governor/Secretary Sherrer reiterated his concerns with public policy relative to three issues: 1) that as written, **HB 2688** allows for continued investment in a qualified Kansas business for a period of seven years even though the firm may no longer meet the criteria established to be a qualified Kansas business; 2) that there is no stipulated minimum number of years that a CFC would have to continue to operate; and 3) that CFCs are allowed to invest the balance of monies not tied up in equity investments in other types of investments. Lt. Governor Sherrer reminded the Committee that these were policy issues of which the Committee should be aware before passage of the legislation.

KDOC&H estimates the need for 1.5 FTE to administer the program. Oklahoma has an operating budget of \$350,00 for the administration of a similar program. The Lt. Governor showed the Committee a flow chart of duties connected with the administration of the program, prepared by KDOC&H staff.

Charles Ranson, President, Kansas, Inc., distributed proposed amendments to **HB 2688**, which addresses some of the concerns stated by Lt. Governor Sherrer. (Attachment 2)

Mr. Ranson explained why business should remain eligible for investment for a seven year period and offered an amendment to require that at least 50% of a company's employees remain in the state to be eligible for follow-on investment.

The committee raised questions regarding the timing of tax credit availability to qualified investors. Mr. Ranson explained that the tax credits could be taken in 10% interval each year as long as the CFC reached investment goals as provided in Section 5, at Page 4, line 40.

He further explained that tax credits could be forfeited if the CFC failed to reach the established investment goals.

Senator Jordan moved, seconded by Senator Donovan, that the Minutes of the March 15th and March 16th Meetings be approved. The vote was unanimous in favor of the motion.

The meeting adjourned at 9:00 a.m.

The next meeting is scheduled for March 21, 2000.

**PRELIMINARY
MINUTES**

JOINT COMMITTEE ON ECONOMIC DEVELOPMENT

November 2-3, 1999
Room 514-S—Statehouse

Members Present

Representative William G. Mason, Chairperson
Senator Pat Ranson, Vice Chairperson
Senator Jim Barone
Senator U. L. "Rip" Gooch
Senator Nick Jordan
Senator Alicia Salisbury
Representative Jerry Aday
Representative Mary Compton
Representative Doug Gatewood
Representative Annie Kuether
Representative Margaret Long
Representative Vern Osborne
Representative Jene Vickrey

Staff Present

Rae Anne Davis, Kansas Legislative Research Department
April Holman, Kansas Legislative Research Department
Lynne Holt, Kansas Legislative Research Department
Renae Jefferies, Revisor of Statutes Office
Bob Nugent, Revisor of Statutes Office
Rose Marie Glatt, Committee Secretary

Conferees

Charles Ranson, President, Kansas, Inc.
Harold Stones, Kansas Special Director for U.S. Senator Pat Roberts
Bob Rosander, President, NANTEK (Manhattan)
Ralph Lagergren, President, Rimfire Management Corporation and Inventor of Bi-Rotor Combine
(Winfield)

Senate Commerce Committee
Date: 3-17-00

Attachment # 1-1 thru 1-3

- The Kansas Securities Commissioner is not in a position to assess an investment; however, regardless of which agency is assigned oversight of the program, none of them (the Securities Commission, Kansas Department of Commerce and Housing, or K DFA) presently has in-house expertise to regulate a venture capital fund;
- If requirements governing contracts with investors are statutorily imposed and it does not make good economic sense for investors to operate under those conditions, the number of investments will be limited as will the number of companies that will benefit;
- One could certainly include those contractual requirements in statute and test the market but one might lose something by testing it because Kansas is presently not perceived as being overly friendly to the seed capital industry; and
- Tax credits are almost uniformly 100 percent in states authorizing CapCos; there are some states offering 110 percent tax credits.

Senator Barone asked for clarification on the decertification process governing CapCos. Mr. Ranson and Ms. Miller, upon Chairperson Mason's request, agreed to provide further information on this issue on November 3.

Chairperson Mason adjourned the meeting at 5:00 p.m.

Wednesday, November 3 Morning Session

The meeting was called to order at 9:10 a.m., in Room 514-S, Statehouse.

Mr. Ranson presented highlights of the 1999 Annual Report of Kansas, Inc., (a copy of the report is on file at the Kansas Legislative Research Department). He advised the Committee of Kansas, Inc.'s website.

Chairperson Mason introduced the new Deputy Secretary of the Kansas Department of Commerce and Housing, Fred Schwien, who in turn introduced his staff. Mr. Schwien summarized the mission, organizational structure, budget, and major program activities of the divisions as reflected in the Department's 1999 Fiscal Year Annual Report (a copy of the report is on file at the Kansas Legislative Research Department). Copies of the slide presentation highlighting aspects of the annual report were distributed to Committee members (Attachment 10). A complete copy of Mr. Schwien's oral presentation was included in the packet distributed to the Committee at the conclusion of his presentation (Attachment 11).

In response to a question regarding the difficulty in obtaining patents in Kansas, Mr. Schwien stated that he was not aware of that specific problem, but he would look into that issue. Discussion followed regarding U.S. premium beef and the importance of partnering between the economic development agencies to develop seed capital in Kansas.

X To respond to a question about the ability of the Department of Commerce and Housing to find capital for start-up companies in Kansas, Mr. Schwien recognized Steve Kelly. Mr. Kelly clarified that the Department's current role is to work with companies that are beyond the start-up stage. He noted that technical companies in Kansas experience difficulty in attracting funds, and suggested that it might be due to rapid changes in the industry and the perception of Kansas as a conservative

state. To address the question on the Department's position regarding the proposed CapCo program, Mr. Kelly expressed concerns about balancing the proposed program against the Department's budget. He pointed out that due to budget constraints, the Department has not been aggressive in terms of new initiatives over the past few years. The agency staff has tried to work with current programs, making minor changes, and providing additional flexibility within the existing framework rather than adding new programs.

In response to a question as to whether the Department's main concern was budgetary, Mr. Kelly agreed that it was, but added it was also important to see how the proposed program fits into the greater economic development strategy. He spoke of an effort, currently underway, to begin developing a comprehensive economic development strategy to move Kansas into the next century. He noted that this is an ongoing effort. In his view, the primary questions with respect to the proposed program relate to: funding, the availability of sufficient capital to make this program successful, and the impact of the tax credits authorized by the program on the overall budget.

In response to a question about whether SB 315 fits with the Department's mission if the Department is given statutory oversight of the program, Mr. Kelly noted the Department's concern centers on having adequate resources and staff to do the job effectively. In response to a question about Department priorities, were the Department to have oversight of the program, Mr. Kelly explained that the Department would find the best person or persons to administer the program. He also noted that background checks provided by the Securities Commission would be helpful and reminded the Committee that the Securities Commissioner testified that his office would be willing to assume that responsibility.

Chairperson Mason stated that on the previous day, the Committee had preliminary discussions on SB 315 which were not completed. He invited further discussion on SB 315.

In response to Senator Barone's request from the previous day, Representative Mason recognized Mr. Ranson to talk about the decertification process. Mr. Ranson explained that the technical advisory committee involved with the *Best Practices Study* recommended oversight of the program be given to the Securities Commission. Most of the hard work to demonstrate competence and raise money will be done by the CapCos which is where the accountability actually resides. Mr. Ranson observed that regulatory oversight of the CapCos in the country is evenly split between securities commissions and departments of economic development. Mr. Ranson also noted that the proposed program would not be taking money away from the State General Fund. A funding mechanism would be created that would not detract from the resources going to other programs. The annual report of the Department of Commerce and Housing demonstrates substantial success in attracting and retaining businesses. However, the proposed program would assist in creating businesses which, in Mr. Ranson's view, is a weakness in Kansas.

Chairperson Mason recognized Mr. Bendis for additional comments on the certification and decertification processes. Mr. Bendis observed that the CapCo program could be self-supporting to some extent because CapCos could be assessed a certification or application fee and renewal fee.

With respect to the provision on decertification in the bill, Mr. Ranson referred to Section 6, subsections (e) and (f) of the proposed substitute bill, beginning with line 22: Decertification of a CapCo after it has met all requirements of paragraphs (1) to (4) of subsection (a) of Section 5, and amendments thereto, shall cause the forfeiture of tax credits commencing with the taxable year of the investor in which the decertification arose and for all future taxable years with no recapture of tax credits obtained by an investor or transferee with respect to the investor's or transferee's tax years which ended before the decertification occurred. Mr. Ranson stressed the importance of subsection (f): Once a CapCo has invested 100% of its certified capital in qualified Kansas businesses, all future tax credits to be claimed by investors or transferees with respect to said CapCo pursuant to this act shall be nonforfeitable. Mr. Ranson explained that the bill is trying to provide accountability in that the burden is placed on the CapCos to both meet all the standards that are set out in the bill and invest funds in a timely fashion. Tax credits are not forfeited if they are not claimed. Forfeiture

Changes from Original set of Kansas, Inc.
amendments are indicated by text blocks.

[As Amended by House Committee of the Whole]

Session of 2000

Substitute for HOUSE BILL No. 2688

By Committee on Economic Development

2-8

10 AN ACT [relating to income taxation;] ~~concerning~~ venture capital;
11 enacting the Kansas certified capital formation company act[; provid-
12 ing a credit therefrom for certain food locker plant expenses].
13

14 Be it enacted by the Legislature of the State of Kansas:

15 Section 1. This act shall be known and may be cited as the Kansas
16 certified capital formation company act. The purpose of this act is to
17 enhance the development of seed and venture capital in Kansas and to
18 support the modernization and expansion of the state's economy. As used
19 in this act, unless the context clearly requires otherwise, the following
20 terms mean:

21 (a) "Affiliate of a certified capital formation company" means:

22 (1) Any person that directly or indirectly, owns, controls or possesses
23 the power or ability to vote ten percent or more of the outstanding voting
24 securities or other beneficial ownership interests of the Kansas certified
25 capital formation company;

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

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

32 (4) any partnership in which the Kansas certified capital formation
33 company is a general partner;

34 (5) any person who is an officer, director, general partner, managing
35 member, managing director or agent of the Kansas certified capital for-
36 mation company or an immediate family member of such person.

37 (b) "Affiliate of an investor" means:

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

41 (2) any person ten percent or more of whose outstanding voting se-
42 curities or other beneficial ownership interests are directly or indirectly

Senate Commerce Committee

Date: 3-17-00

Attachment # 2-1 thru 2-13

43 owned, controlled or possessed with the power to be voted by the

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1 investor;

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

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

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

(c) "Authorized capital formation company and Authorized CFC" mean a capital formation company that has been designated by the secretary as having met the requirements of this act necessary to raise capital investments but that has not yet received the designation as a certified capital formation company.

7 ~~(c)~~ (d) "Applicable percentage" means one hundred percent.

8 ~~(d)~~ (e) "CFC" means any ~~certified~~ capital formation company.

9 ~~(e)~~ (f) "Capital in a qualified Kansas business" means any note, stock,
10 partnership or membership interest or other form of equity investment
11 or hybrid security, of any nature and description whatsoever, including a
12 debt instrument or security which has the characteristics of indebtedness
13 but which provides for conversion into equity or equity participation in-
14 struments such as options or warrants which are acquired by a certified CFC as a
15 result of a transfer of cash to a business. Capital in a qualified Kansas
16 business shall not include secured debt instruments.

17 ~~(f)~~ (g) "Certified capital" means cash, marketable securities and other
18 assets held by a certified capital formation company equal to the amount
19 of certified capital investment made by investors in the certified capital
20 formation company.

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

27 ~~(h)~~ (i) "Certified capital investment" means an investment of cash by an
28 investor which is certified by the secretary made in such manner as to
29 acquire a beneficial ownership interest in a Kansas certified capital for-
30 mation company.

31 ~~(i)~~ (j) "Commissioner" means the securities commissioner of Kansas or
32 persons acting under the supervision of the commissioner.

33 ~~(j)~~ (k) "In existence" means the date of the first sale of goods or services
34 by a qualified Kansas business or a business seeking to be so qualified.

35 ~~(k)~~ (l) "Investor" means any person that invests cash. If the investor is
36 a natural person, the investor shall have a net worth of at least \$1,000,000
37 and such net worth shall be not less than 10 times the amount of the

38 investor's certified investment in a CFC. The investor's net worth shall
39 not include the value of any equity in the investor's primary residence.

40 (h) (m) "Liquidating distribution" means any distribution other than a
41 qualified distribution.

42 (m) (n) "Person" means any natural person or any business association,
43 including but not limited to, a corporation, limited liability company, gen-

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1 eral or limited partnership or trust ~~but shall not include entities subject to~~
~~privilege tax imposed pursuant to chapter 79 article 11 of the Kansas~~
~~statutes annotated or entities subject to premium tax or privilege fee~~
~~imposed pursuant to K.S.A. 40-252, and amendments thereto.~~

Banks and Insurance
Companies may be
investors and receive tax
credits.

2 (n) (o) "Qualified distribution" means any distribution or payment made
3 by a certified capital formation company for costs and expenses of form-
4 ing, syndicating, managing or operating the certified capital formation
5 company, including an annual management fee and reasonable and nec-
6 essary fees in accordance with industry custom for professional fees in-
7 cluding, but not limited to, legal and accounting fees, relating to operating
8 the certified capital formation company.

9 (o) (p) "Qualified Kansas business" means:

10 (1) A business that satisfies the requirements of subparagraphs (A)
11 through (F) of this subsection.

12 (A) Such business is independently owned and operated and has its
13 principal business office located in Kansas or, in the case of a company
14 domiciled outside the state of Kansas, which certifies that the company's
15 principal business office will be located in Kansas within six months fol-
16 lowing the date of the initial investment.

17 (B) At least fifty percent of the employees of the business shall be
18 resident in Kansas or, in the case of a company domiciled outside the
19 state of Kansas, certifies that at least fifty percent of its employees will
20 be resident in Kansas within six months following the date of the initial
21 qualified venture capital investment.

22 (C) Such business is in need of venture capital and cannot obtain
23 conventional financing to fund its further development and future
24 operations.

25 (D) Such business shall be engaged in commerce for the purpose of
26 manufacturing, processing or assembling or distributing products, con-
27 ducting research and development or providing services in interstate
28 commerce.

29 (E) For businesses involved in commerce for the purpose of provid-
30 ing services in interstate commerce, that business must demonstrate that
31 more than fifty percent of its gross revenues are derived from sales out-
32 side the state of Kansas or provide reasonable documentation that the

33 company will derive at least fifty percent of its gross sales outside the
34 state within a three-year period.

35 (F) Such business, at the time of the initial qualified venture capital
36 investment, shall have been in existence less than five years and shall not
37 have had gross sales in excess of \$1,000,000 in any single fiscal year.

38 (2) Any business which, subject to paragraph (a)(6) of section 5, is
39 approved as a qualified Kansas business at the time of the first qualified
40 venture capital investment in such business by a Kansas certified capital
41 formation company, for a period of seven years following the date of such
42 first investment, shall continue to be classified as a qualified Kansas busi-
43 ness and may receive follow-on investments from any Kansas certified

4

1 CFC, and such follow-on investments shall consti-
2 tute qualified venture capital investments even though such business may
3 not meet other qualifications of this subsection at the time of such follow-
4 on investments. *This provision shall not however remove the requirement*
set forth in paragraph (p)(1)(B) of this section which states that at
least 50% of the employees of the business shall be resident in Kansas.

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

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

13 (B) a business engaged primarily as a passive business, in irregular or
14 noncontinuous operations, or which derives substantially all of its income
15 from passive investments that generate interest, dividends, royalties or
16 capital gains;

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

18 (D) a subsidiary of a certified capital formation company;

19 (E) another certified capital formation company;

20 (F) an affiliate of the certified capital formation company;

21 (G) an investor of the certified capital formation company or an af-
22 filiate or subsidiary of an investor of the certified capital formation com-
23 pany unless approved in writing by the secretary.

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

27 (r) (r) "Secretary" means the secretary of commerce and housing or per-
28 sons under the secretary's direction.

29 (s) (s) "Tax credit" means a credit against the tax imposed by the Kansas
30 income tax act, or the premium tax or privilege fee imposed pursuant to
31 K.S.A. 40-252, and amendments thereto, or the privilege tax as measured
32 by net income of financial institutions imposed pursuant to chapter 79,
33 article 11 of the Kansas Statutes Annotated.

Amendment per Lt. Gov's
concern.

Banks and Insurance
Companies may again be
investors and receive tax
credits.

How Kansas benefits even if a company leaves the state or is sold after the CFC invests.

Because the CFC's investment is an "equity" investment, the CFC (and the state which sees 20% of the CFC's profits) still benefits if a company is sold or moves to another state. Let's take the real-life cases of **Ralph Lagergren and Agri-Technology** which was purchased by John-Deere and **Clint Everton and Knowledge Communications** which was purchased by Harcourt General of Boston.

Agri-Technology: The state's Ad Astra fund had made equity investments in Agri-Technology during the design and patent process. The company was purchased by John-Deere Company late in FY 95.

Although the combine would not be manufactured in Kansas, the state still reaped benefit from those investments. Building the infrastructure.

- **Profits to the Investors:** Approximately \$500,000 back to Ad Astra fund from the purchase of their ownership in Agri-Technology.
- **Kansas Seed Capital Infrastructure is Strengthened:** As a limited partner in Ad Astra, KTEC received \$335,259 to reinvest in other companies that may remain in the state and create jobs and tax revenues.
- **Tax Revenues on Gains:** The Agri-Technology principals & employees received substantial taxable income.
- **Creation of Angel Investors:** Using his resources derived from the Agri-Technology deal, Ralph Lagergran has subsequently been instrumental in three additional start-ups in Kansas. Two of these are now moving past the start-up stage.

Knowledge Communications: KTEC affiliates and Ad Astra, made early equity investments in Knowledge. Necessary additional capital could not be found in Kansas and the company nearly ceased operation. After receiving \$1.25 million from Dallas investors in exchange for half its ownership, Knowledge moved its administrative and marketing functions to Dallas. The company was later acquired by Harcourt General of Boston.

Although part of the jobs were lost, the state still benefitted from its initial investment.

- **Profits to the Investors:** KTEC and its affiliates received approximately **\$2.8 million** in net profits after the sale of their equity position.
- **Kansas Seed Capital Infrastructure is Strengthened:** That **\$2.8 million** is now available to reinvest in other companies that may remain in the state and create jobs and tax revenues.
- **Profit Sharing by State:** Had a CFC made the \$1.25 million investment, its returns would have been approximately \$7.75 million. 20% of the profits (\$1.55 mil) would have also come back to the state treasury upon distribution.

What if a business just moves to another state?

The CFC's ownership position stays in place, no more CFC investment is allowed, and the value of the equity position grows with the company. At some point the company will either buy-out the CFC, the company will be acquired, or an IPO will take place. At that time, the CFC receives its returns, the infrastructure is strengthened, and the state shares in the profit.

Companies must have the flexibility to make profit maximizing decisions.

Removing this flexibility, by requiring them to remain in the state, will give them reason to by-pass CFC investment and to seek capital outside Kansas.

34 Sec. 2. (a) Any investor that makes a certified capital investment shall
35 earn a tax credit against state tax liability equal to 100% of the amount of
36 such investor's certified capital investment. The investor, or a person to
37 whom the credits were duly transferred, shall be entitled to claim not
38 more than 10% of the credit per taxable year for taxable years ~~com-~~
39 ~~mencing after taxable year 2001 ending after June 30, 2003.~~ If the amount of
40 the tax credit allowed under subsection (a) exceeds the tax liability of the
41 taxpayer for any taxable year, such excess amount shall be refunded to the taxpayer.

42 (b) No certified capital investment in a **single** CFC by any one person shall
43 be less than \$25,000 or more than **\$2,000,000**; nor shall any one person's combined
investment for the purpose of earning tax credits exceed **\$10,000,000**.

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1 (c) The total amount of tax credits which may be allowed shall not
2 exceed \$50,000,000. The total amount of tax credits which may be allowed
3 under this act shall not exceed \$5,000,000 per fiscal year.

4 Sec. 3. (a) The secretary may **authorize and subsequently** certify profit
5 or not-for-profit entities which ~~submit an application to be designated as a CFC~~
meet the requirements of this act. The secretary
6 shall compile a list of every **certified** CFC, including the address and telephone
7 number of the **certified** CFC's principal place of business. The secretary shall
8 publicize the list in order to inform Kansas companies of the availability
9 of potential investment capital.

10 (b) The secretary shall review the organizational documents for each
11 applicant for **certification authorization as a CFC** and the business history
12 of the applicant to determine:

13 (1) That at the time of application **for authorization as a CFC**, the applicant
14 owns cash, marketable securities and other liquid assets valued at no less than \$500,000; ~~or~~
15 that prior to January 1, 2000, the applicant was designated as an inno-
16 vation and commercialization corporation or an affiliate ~~of an~~ innovation
17 and commercialization corporation created under the Kansas technology
18 enterprise corporation innovation and commercialization corporation
19 program;

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

24 (c) To continue to be certified, the CFC must own and shall peri-
25 odically demonstrate to the secretary, as the secretary may require, that
26 the liquid asset base for the certified capital formation company is at least
27 \$500,000 at all times during the CFC's participation in the program au-
28 thorized by this act. ~~and that such moneys have been used for making~~
29 ~~qualified venture capital investments.~~

30 (d) With respect to any person who submits or has submitted an
31 application **for authorization as to become** a CFC, the commissioner shall investigate to de-
32 termine and report to the secretary whether any of the directors, trustees,
33 managers, officers, general partners, beneficial owners of 10% or more
34 of any class of equity securities or any promoters employed or otherwise

- 35 associated with that person at the time of such application:
36 (1) Has been affiliated with any company that has filed a registration
37 statement which is subject to a currently effective stop order entered
38 pursuant to any state law;
39 (2) has been convicted of any felony or misdemeanor in connection
40 with the purchase or sale of any security or any felony involving fraud or
41 deceit including, but not limited to, forgery, embezzlement of money
42 under false pretenses, larceny or conspiracy to defraud;
43 (3) is currently subject to any state administrative order or judgment

6

- 1 entered by a state securities administrator or is subject to any state ad-
2 ministrative order or judgment in which fraud or deceit was found and
3 an order or judgment was entered;
4 (4) is currently subject to any state administrative order or judgment
5 which prohibits the use of any exemption from registration in connection
6 with the purchase or sale of securities;
7 (5) is subject to any order, judgment or decree of any court of com-
8 petent jurisdiction temporarily or preliminarily restraining or enjoining,
9 or is subject to any order, judgment or decree of any court of competent
10 jurisdiction permanently restraining or enjoining that person from engag-
11 ing in or continuing any conduct or practice in connection with the pur-
12 chase or sale of any security, rendering investment advice or involving the
13 making or any false filing with any state;
14 (6) has been convicted of or pleaded nolo contendere to any criminal
15 offense other than a misdemeanor involving motor vehicle violations.
16 (e) The secretary shall not **authorize certify** any CFC if the commissioner's
17 report includes any affirmative findings pursuant to subsection (d).
18 (f) The secretary shall review documentation regarding the qualifi-
19 cations of the persons who will actively manage the CFC and make a
20 determination as to whether such persons possessed sufficient knowledge
21 and professional experience in the areas of investment, venture capital,
22 business management and evaluation, portfolio management, and such
23 other area of expertise to the degree that a reasonable person would be
24 confident in such manager's ability to manage the CFC. **No certification authorization**
25 shall be issued when it is the opinion of the secretary that such persons
26 do not possess this requisite degree of knowledge and expertise.
27 (g) No investor shall individually, or collectively with or through one
28 or more affiliates, by means of ownership, agreement or otherwise, own,
29 control or possess the power or ability to cause or direct the making of
30 any qualified venture capital investments by a **certified** CFC.
31 (h) **Within a period of time established by the secretary, after receipt of**
application for authorization as a CFC, ~~75 days of~~ application, the secretary
shall either issue the authorization certification and notify the secretary
of the department of revenue of such certification or shall refuse the certification
deny authorization and communicate in detail to the applicant the grounds
for the refusal denial, including any suggestions for the removal of those grounds.

36 Sec. 4. (a) A CFC shall have a period of 365 days from the date of
37 receiving certification from the secretary in which to procure the amount
38 of certified capital investment required by subsection (b). All certified
39 capital investments in the CFC shall be received within such 365-day
40 funding period, notwithstanding the provisions of subsection (c).
41 (b) Before closing its fund of certified capital investment, and pur-
42 suant to subsection (b) of section 3, and amendments thereto, a CFC
43 shall raise a minimum aggregate certified capital investment of no less

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1 than \$5,000,000. In the case of a CFC designated prior to January 1,
2 2000, as an innovation and commercialization corporation or an affiliate
3 of an innovation and commercialization corporation created under the
4 KTEC innovation and commercialization corporation program, such min-
5 imum certified capital investment shall be no less than \$1,000,000. Total
6 capital investment deemed certified for the purpose of earning tax credits
7 shall not exceed \$10,000,000 in a single CFC. No capital investments shall
8 be certified by the secretary until such time when the minimum cumu-
9 lative investments are met. Failure of a CFC to raise the minimum cu-
10 mulative investments may result in the revocation of the certification by
11 the secretary.

12 (c) Once fully capitalized pursuant to the provisions of subsection (b),
13 a CFC may make application to the secretary for authorization to seek
14 additional certified capital investment.

Sec. 4. (a) An authorized capital formation company having been authorized by the secretary pursuant to Section 3 shall have a period of not more than 365 days from the date of receiving authorization in which to procure certified capital investment.

(b) In order to receive certification by the secretary, an authorized capital formation company shall raise a minimum aggregate certified capital investment of no less than \$5,000,000. In the case of an authorized capital formation company formed by an innovation and commercialization corporation or an affiliate innovation and commercialization corporation created under the KTEC innovation and commercialization corporation program, such minimum certified capital investment shall be no less than \$1,000,000.

(c) Total capital investment deemed certified for the purpose of earning tax credits shall not exceed \$10,000,000 in a single capital formation company. In the case of a capital formation company formed by an innovation and commercialization corporation or an affiliate innovation and commercialization corporation created under the KTEC innovation and commercialization corporation program, such maximum certified capital investment shall not exceed \$1,500,000.

(d) If during the fund raising period, an authorized capital formation

company demonstrates to the secretary that the maximum cumulative certified capital investment has been met pursuant to this act, the secretary shall either designate the capital formation company as a certified capital formation company and notify the secretary or revenue of such certification; or shall deny the certification and notify the capital formation company of the basis for denial.

(e) All capital investment deemed certified for the purpose of earning tax credits must be certified by the investor to be new monies in that such monies were not being used for seed or venture capital prior to making the investment in a CFC. Any attempt to transfer funds from an existing venture capital fund to a CFC for the purposes of earning a tax credit shall constitute a violation of this act and may lead to decertification.

(f) No capital investments shall be certified by the secretary until such time when the minimum cumulative certified capital investments are met.

(g) Upon the end of the fund raising period as established by the secretary, capital formation companies that have reached the minimum cumulative certified capital investment requirement but have failed to reach the maximum cumulative certified capital investment requirements shall be certified by the secretary in rank order based on the amount of certified capital investment raised by the capital formation company and the amount of tax credits available for allocation upon the secretary's satisfaction that all such investment was made pursuant to this act.

(h) The secretary will notify the department of revenue upon certification of a capital formation company.

(i) Designation as an innovation and commercialization corporation or an affiliate innovation and commercialization corporation created under the Kansas technology enterprise corporation shall not relieve such entity from compliance with any provisions of this act except where stated otherwise.

- 15 Sec. 5. (a) To continue to be certified, a CFC shall make qualified
16 venture capital investments according to the following schedule:
17 (1) Within three years after the date on which a CFC is certified as
18 a CFC at least 25% of its certified capital shall be, or have been, used for
19 making qualified venture capital investments;
20 (2) within four years after the date on which a CFC is certified as a
21 CFC at least 40% of its certified capital shall be, or have been, used for
22 making qualified venture capital investments;
23 (3) within five years after the date on which a CFC is certified as a
24 CFC at least 50% of its total certified capital shall be, or have been, used
25 for making qualified venture capital investments;
26 (4) within seven years after the date on which a CFC is certified as

27 a CFC at least 70% of its total certified capital shall be, or have been,
28 used for making qualified venture capital investments.

29 (5) a CFC shall not make an investment in an affiliate of the CFC or
30 an affiliate of an investor. For the purposes of this subsection, if a com-
31 pany is not an affiliate before a CFC initially invests in the company, it
32 shall not be deemed to be an affiliate if such CFC provides additional
33 qualified venture capital investment to such company subsequent to its
34 initial investment. No corporate officer, employee or shareholder, no lim-
35 ited or general partner or other person personally affiliated with any CFC
36 shall personally invest in any portfolio company regardless of whether the
37 portfolio company is affiliated with the CFC.

38 (6) a CFC, at least ~~15~~ 30 working days prior to making what it deter-
39 mines to be any initial qualified venture capital investment, shall first
40 certify to the secretary that the company in which it proposes to invest
41 meets the definition of a qualified Kansas business pursuant to section 1,
42 and amendments thereto. The CFC shall state the amount of capital it
43 intends to invest and identify the business in which it intends to make

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1 the investment. The CFC shall also provide to the secretary a written
2 explanation of the basis for its determination that the business meets the
3 definition of a qualified Kansas business, if the secretary determines that
4 the business does not meet the definition of a qualified Kansas business,
5 the secretary, within the ~~15~~ 30 working-day period prior to the making of
6 the proposed investment, shall notify the CFC of the determination and
7 provide the CFC an explanation thereof. If the secretary fails to notify
8 the CFC of the determination within the ~~15~~ 30 working-day period pre-
9 scribed herein, the business in which the CFC proposes to invest shall
10 be deemed to be a qualified Kansas business. If a CFC fails to notify the
11 secretary prior to making an initial investment in a business, the business
12 in which the CFC invested shall be deemed not to be a qualified Kansas
13 business even though the business, at the time of the investment, met
14 the requirements of section 1, and amendments thereto;

15 (7) all certified capital which is not then required to be invested in
16 qualified venture capital investments or which has been previously in-
17 vested in qualified venture capital investments and returned by the com-
18 pany, may be held or invested in such manner as the CFC, in its discre-
19 tion, deems appropriate. The proceeds of all certified capital which is
20 returned by to a CFC after it was originally invested in qualified venture
21 capital investments, may be invested in other qualified venture capital
22 investments and shall be credited toward any requirement in this act with
23 respect to placing certified capital in qualified venture capital
24 investments.

25 (b) A CFC may make qualified distributions at any time. In order to
26 lawfully make liquidating distributions, a CFC must have invested an
27 aggregate amount equal to 100% of its certified capital in qualified ven-
28 ture capital investments.

29 (c) Liquidating distributions in excess of the certified capital forma-

30 tion company's original certified capital and any additional capital contri-
31 butions to the certified capital formation company shall be subject to audit
32 by a certified public accounting firm acceptable to the secretary, at the
33 expense of the certified capital formation company.

34 (d) If at the time any liquidating distribution is made by a CFC, the
35 aggregate sum of all liquidating distributions of the CFC exceeds the
36 aggregate sum of the CFC's original certified capital and any subsequent
37 qualified venture capital contributions to the CFC, as determined by au-
38 dit, the CFC, prior to any additional distributions, shall pay to the state
39 treasurer's office ~~10%~~ 20% of the proportion of the distribution in excess of
40 such amount.

41 (e) Documents and other materials submitted by CFC's or by busi-
42 nesses for purposes of **authorization or** original certification or the continuance of certi-
43 fication as a CFC shall not be public records if it is determined by the

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1 secretary that disclosure of such information would compromise trade
2 secrets of qualified Kansas businesses unless otherwise specified in this
3 act.

4 (f) Each CFC shall report the following to the secretary:

5 (1) ~~As soon as practicable, but in any case no later than 15 days after~~
6 ~~the receipt of a certified capital investment, the name of each investor,~~
7 ~~the amount of each investor's certified capital investment and the date~~
8 ~~when the certified capital investment was received;~~

9 (2) within 90 days of the close of the CFC's fiscal year, annual audited
10 financial statements. The audit shall address the methods of operation
11 and conduct of business of the CFC to determine if the CFC is complying
12 with the statutes and program rules and that the funds received by the
13 CFC have been invested in accordance with the time limits provided by
14 this act.

15 (3) at the end of each quarter, that no more than 20% of the assets
16 of a CFC shall be invested in a single qualified Kansas business at any
17 one time unless the CFC can demonstrate that a greater percentage in a
18 single qualified Kansas business at any one time is the result of losses
19 suffered by the CFC in other qualified venture capital investments.

20 (g) Any material related to the sale of ownership in a CFC or soliciting
21 investment in a CFC shall include the following statement: "By ~~author-~~
22 ~~izing authorizing or certifying the formation of~~ a certified capital formation company, the State of
23 Kansas does not endorse the quality of management or the potential for
24 earnings of a particular company. The use of the word "certified" or "**authorized**" in an
25 offering does not constitute a recommendation or endorsement of an
26 investment by the Kansas Securities Commission or any other State
27 Official."

28 (h) The secretary may establish reasonable initial filing fees for ap-
29 plications for **authorization and** certification pursuant to this act and may also establish an
30 annual nonrefundable fee for CFC's seeking continued certification.

31 Sec. 6. (a) To ensure that no qualified venture capital investment or
32 investor's certified capital investment has been made in violation of this

33 act, the secretary shall conduct an annual review of each CFC to deter-
34 mine if the CFC is complying with the requirements of certification. The
35 costs of the annual review shall be paid by each CFC according to a
36 reasonable fee schedule adopted by the secretary.

37 (b) Any material violation of this act by a CFC shall be grounds for
38 decertification under this section. If the secretary determines that a CFC
39 is not in compliance with the requirements for continuing certification,
40 the secretary, by written notice, shall inform the officers of the CFC and
41 the board of directors, managers, trustees or general partners that they
42 shall be decertified within 120 days from the date of mailing of the notice,
43 unless they correct the deficiencies detailed in the notice and demon-

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1 strate to the secretary's satisfaction that the CFC is again in compliance
2 with the requirements for certification as determined by the secretary.

3 (c) At the end of the 120 day grace period, if the CFC is still not in
4 compliance, the secretary may send a notice of decertification to the CFC
5 and to the secretary of revenue including a list of the decertified ~~capital~~ capital
6 investments by investor and transferee.

7 (d) Decertification of a CFC prior to the CFC meeting all require-
8 ments of paragraphs (1) through (4) of subsection (a) of section 5, and
9 amendments thereto, shall cause the recapture of all tax credits previously
10 allowed to an investor or transferee and the forfeiture of all future tax
11 credits to otherwise be claimed by an investor or transferee with respect
12 to any certified capital investment in the decertified CFC.

13 (e) Decertification of a CFC after it has met all requirements of par-
14 agraphs (1) through (4) of subsection (a) of section 5, and amendments
15 thereto, shall cause the forfeiture of tax credits commencing with the
16 taxable year of the investor or transferee in which the decertification arose
17 and for all future taxable years with no recapture of tax credits allowed
18 to an investor or transferee with respect to the taxable years which ended
19 before the decertification occurred. Once a CFC has invested 100% of
20 its certified capital in qualified Kansas businesses, all future tax credits to
21 be claimed pursuant to this act by investors or transferees with respect
22 to such CFC shall not be subject to recapture.

23 Sec. 7. The secretary shall prepare and submit an annual report to
24 the governor and the legislature no later than October 1 of each year.
25 Such report shall be presented to the standing committee on commerce
26 in the senate, standing committee on economic development in the house
27 of representatives and the joint committee on economic development.
28 Such report shall include but not be limited to:

29 (a) The total dollar amount each CFC received from all investors
30 allowed tax credits and any other investors and the identity of all investors
31 allowed tax credits;

32 (b) the total amount invested by each CFC in qualified Kansas busi-
33 nesses, the identity and location of those businesses, the amount invested
34 in each qualified Kansas business and the total number of permanent full-
35 time jobs created or retained by each qualified Kansas business as a result

36 of the investment; and
37 (c) the cumulative amount of any liquidating disbursements received
38 by the state from the CFC's.

39 Sec. 8. The secretary may revoke the certification of a CFC if any
40 material representation to the secretary in connection with the application
41 process proves to have been falsely made or if the application materially
42 violates any requirement established by the secretary.

43 Sec. 9. (a) Any investor that is not subject to taxation under the pro-

1 visions of the Kansas income tax act, privilege or premium tax that makes a
cer-
2 tified capital investment shall be deemed to acquire an interest in the
3 nature of a transferable tax credit limited to 100% of such investment.
4 The credit established pursuant to this act may be sold or transferred
5 subject to approval by the secretary. An investor as described in this sec-
6 tion shall not be allowed a refund for the interest herein created. Only
7 the full amount of the credit for any one investment may be transferred,
8 and the credit may be transferred only one time. Documentation of any
9 credit transfer shall be provided to the secretary. The secretary shall trans-
10 mit a copy of such documentation to the secretary of revenue.

11 (b) The secretary, after consulting with the secretary of revenue, shall
12 develop such rules and regulations as are necessary to facilitate the op-
13 eration of the transfer program consistent with the interest of the state
14 in tracking the transfer of ownership and the use of tax credits earned by
15 the transferee.

16 (c) Any such sale or transfer shall not affect the time schedule for
17 taking the tax credit, as provided in this act. Any tax credits recaptured
18 pursuant to section 6 shall be the liability of the taxpayer which actually
19 claimed the tax credit. In approving the sale or transfer of the tax credit
20 pursuant to this section, the secretary may require the transferor or the
21 transferee or both to execute guarantees or post bonds with respect to
22 any potential tax credit recapture.

23 (d) Any payment received for tax credits pursuant to this section is
24 taxable income of the transferor of the credit and the amount equal to
25 the difference the dollar value of the tax credit transferred minus the
26 sales price of the tax credit shall be taxable income of the transferee.

27 (e) The secretary shall make and promulgate rules and regulations
28 consistent with the provisions of this act as are necessary or useful to carry
29 out the provisions of this act.

30 (f) Every final order, decision, license or other official act of the sec-
31 retary pursuant to this act is subject to review in accordance with the act
32 for judicial review and civil enforcement of agency actions, K.S.A. 77-601
33 et seq. and amendments thereto.

34 (g) In view of the objectives of these requirements and the underlying
35 policies of the act, the act is not available with respect to any transaction
36 or series of transactions that, although in technical compliance with these
37 rules, is part of a plan or scheme to evade the requirements of this act or

Banks and
Insurance
Companies
may be
investors and
receive tax

38 to distort the benefits entitled to be realized under the act. In such cases,
39 no investor in any CFC shall be entitled to the benefit of any tax credits
40 provided for hereunder.

41 (h) The offer or sale of a security by a CFC pursuant to this act shall
42 be subject to the registration requirements of K.S.A. 17-1254, 17-1255,
43 17-1257, 17-1258, 17-1259 and 17-1260, and amendments thereto.

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1 [Sec. 10. (a) For all taxable years commencing after December
2 31, 1999, there shall be allowed as a credit against the tax liability
3 of a taxpayer who operates a food locker plant imposed under the
4 Kansas income tax act, an amount equal to any expenses paid for
5 improvements in the facilities of such food locker plant. The credit
6 allowed by this section in any taxable year to the taxpayer shall not
7 exceed \$10,000. If the amount of such tax credit exceeds the tax-
8 payer's income tax liability for any such taxable year, such excess
9 amount may be carried over for deduction from the taxpayer's tax
10 liability in the next succeeding taxable year or years until the total
11 amount of the tax credit has been deducted from tax liability.

12 [(b) As used in this section "food locker plant" means a plant
13 which: (1) Is inspected by the Kansas department of agriculture as
14 provided under the Kansas meat and poultry inspection act; and

15 [(2) prepares meat, meat food products, poultry or poultry
16 products which have been inspected and passed and which are
17 being prepared and sold in normal retail quantities; or

18 [(3) prepares such meat, meat products, poultry or poultry
19 products for the owner of such food locker plant.]

20 Sec. 10. [11.] This act shall take effect and be in force from and after
21 its publication in the statute book.

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