HOUSE RESEARCH

Bill Summary

FILE NUMBER: H.F. 2770 **DATE:** February 24, 2010
Version: As introduced

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Subject: Tax credit for investments in startup and emerging businesses

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Overview

This bill allows insurance companies that invest in Minnesota business investment companies (MBICs) a credit against the insurance premiums tax. The MBICs, in turn, are to make investment of these funds in qualified businesses. This credit generally follows the pattern of CAPCO credits allowed in a number of other states. MBICs must be certified by the commissioner of the Department of Employment and Economic Development (DEED).

Qualified businesses (i.e., those qualifying for investments by MBICs) must have their headquarters and 80 percent of their employees in Minnesota. They can have no more than 100 employees and cannot be engaged, for example, in providing professional services, banking, real estate development, insurance, oil and gas exploration, or gambling.

MBICs are to invest 100 percent of the amount of the tax credits (i.e., the insurance company investments in the MBIC) within six years. The state is entitled to 20 percent of the return on the investments (i.e., in excess of the original investment or credit amount).

The credits are nonrefundable and equal 80 percent of qualifying investments. Total credits are capped at $100 million. The credits are allowed beginning for investments made in tax year 2011, but cannot be claimed until years shown in the table (i.e., outside of the budget window).

Tax Year	% of Credit Allowed
2014	20%
2015	20%
2016	20%
2017	20%

1 **Minnesota business investment company credit.** Establishes the basic qualifications and eligibility rules for the MBIC credit.

Subd. 1. Definitions. Defines the following terms:

Affiliate is an individual or entity that owns 15 percent or more of the voting power of the securities of a MBIC.

Allocation date is the date the tax credits are allocated to participating investors (insurance companies) in MBICs by DEED.

Designated capital is the amount the participating investor (insurance company) invests in a MBIC, either directly or through qualified debt instruments.

MBIC is a for-profit entity with its headquarters or principal office in Minnesota, certified by DEED, and primarily engaged in making cash investments in qualified businesses.

Participating investor is an insurance company, but cannot be an HMO.

Person means both individuals and entities, such as corporations, partnerships and LLCs.

Qualified businesses must: (1) have a Minnesota headquarters; (2) have at least 80 percent of its employees and its principal operations in Minnesota; (3) have no more than 100 employees; (4) not be engaged in a variety of prohibited lines of business – professional services, banking, real estate development, insurance, oil and gas exploration, direct gambling, retail sales, or investing in MBICs.

Qualified debt instrument is a debt instrument issued by a MBIC with a maturity of four years or more and scheduled repayment of principal that is no faster than level amortization.

Qualified distributions are distributions by a MBIC for: (1) its startup and organizing costs, including financing costs; (2) annual management fee, not to exceed 1 percent; (3) fees for professional services; (4) federal and state taxes; and (5) payments of principal and interest on qualified debt instruments.

Qualified investment is an investment by a MBIC in a qualified business. These can be equity, debt, or hybrid investments. If the investment is repaid within one year, the amount of the investment for the percentage requirements in subdivision 4 are reduced by one-half.

State premium tax liability means the insurance premiums tax.

Subd. 2. Certification. Directs DEED to establish the application for certification of MBICs and sets out specific requirements. Applicants must pay a $7,500 application fee and have capitalization of $500,000 or more in liquid assets and have at least one principal in Minnesota with five years or more of money management experience. DEED is directed to review applicants' organizational documents and business history before certifying them. DEED must start to accept applications by August 1, 2010.

Subd. 3. Requirements. Prohibits a participating investor from owning more than 15 percent of the voting power of a MBIC, managing a MBIC, or directing a MBIC's investments, unless the MBIC is in default under its statutory or contractual obligations. A MBIC may obtain guaranties, bonds, and so forth on behalf of its participating investors.

Subd. 4. Aggregate limitations on investment tax credits; allocation. Limits the aggregate amount of tax credits that may be claiming by all participating investors (insurance companies) to $100 million. No group of investors for one MBIC can claim more than 25 percent of the credit limit. DEED will allocate the credits based on the order of filing claims. (MBICs file for the credit for their investor-insurance companies.) Claims filed on the same day have the same priority and if the claims exceed the limit, the credits are prorated. If a MBIC receives an allocation of credits and does not receive an investment of designated capital within 10 days, the credit allocation is forfeited. These credit allocations are, then, reallocated to other MBIC applicants. DEED can impose up to a $50,000 fine on the insurance company that did not make the promised investment for the credits.

Subd. 5. Requirements for continuance of certification. MBICs are required to make qualified investments under the following schedule to either maintain their certification (for first three years) or to be permitted to pay management fees (four years and later).

Years after allocation	
2	
3	
4	
6	

These percentages can be met by "recycling" the money from prior investments – e.g., the MBIC can take the proceeds from selling investment #1 and invest it in investment #2 and this amount is counted twice to meet the percentage requirement.

Before making investments the MBIC is to request DEED to provide a written determination that the business qualifies. If DEED doesn't respond within 10 business days, the investment is deemed to be qualified. A MBIC may not invest more than 15 percent in one company without DEED's approval.

Subd. 6. Reporting requirements. Requires MBICs to annually report to DEED the following:

- Its participating investors, the amounts of their investments (designated capital), and the dates received (required to be reported after the receipt of capital)
- Amount of MBIC's designated capital remaining to be invested

- Whether an investment in one business exceeded 15 percent
- Information on investments made, including the number of employees of the business
- For terminated investments, the number of employees when the investment ended
- Other information DEED requires
- Audited financial statements
- A procedures report

An annual certification fee of $5,000 applies. DEED is to notify a MBIC if it fails to meet the percentage investment requirements and it will be decertified. If DEED does not notify the MBIC, it is deemed to be in compliance.

Subd. 7. Distributions. Authorizes a MBIC to make qualified distributions at any time. Other distributions require the MBIC to have met the 100 percent investment threshold. (Put another way, investors in the MBIC can take the proceeds of the tax credits out of the MBIC – for purposes other than a qualified distributions – only after it has invested an amount equal to 100 percent of the tax credits it was allocated in qualifying small businesses.)

The MBIC must pay to the state ten percent of its profit (i.e., the return on its investment that exceeds the credit the state provided to fund the investments). If the MBIC meets the 100 percent investment benchmark, it retains the original investment (funded indirectly by the tax credits) and 90 percent of the profit.

Subd. 8. Decertification. Directs DEED to annually review each MBIC to ensure it is complying with the statutory requirements. The cost of the review is charged to the MBIC. DEED can decertify the MBIC for material violations. Decertification will result in recapture of part or all of the tax credit against the insurance premiums tax, as described in section 2. Once the MBIC has reached the 100 percent investment threshold, it is no longer subject to regulation or review.

Subd. 9. Registration requirements. Requires all investments by participating investors to be registered or exempt from registration.

Subd. 10. Rule making. Provides DEED is exempt from the APA rulemaking requirements in administering the credit.

Subd. 11. Reports to governor and legislature. Requires DEED to annually report to the governor and legislature on the credit:

- Number of MBICs
- Amount of designated capital
- Cumulative amount invested
- Cumulative amount of follow-on capital that each MBIC has created

- Total amount of investment tax credits
- Performance of each MBIC with regard to its continued certification
- Classification of businesses invested in by sector and size of company
- Locations of the companies
- MBICs that were decertified and reasons for doing so
- Other information

2 **Credit allowed against premiums tax.** Allows the credit against the insurance premiums tax.

Subd. 1. Credit allowed. Allows a participating investor in a MBIC an 80 percent credit for the amount of the investment. This credit is claimed in four equal installments (of 20 percent of the investment) in tax years 2014 to 2017. The credit is limited to the tax liability with a carryforward until the credit can be fully used. The credit applies against both the regular and retaliatory tax for a foreign insurer. The tax credit is ignored for any rate making or rate limitation for any insurance contract.

If the MBIC is decertified, the credit is subject to recapture – (1) if decertification occurs in the first two years after allocation of the credit, the entire credit is recaptured and (2) if the decertification occurs after two years, one-half of the credit is recaptured.

Subd. 2. Transfers. Authorizes an insurance company to sell or transfer the credit to another taxpayer, if the transfer is made 180 days or more after the insurance company made the investment. If the investor sells or transfers the credit, it must notify DOR within 30 days. No more than one transfer of a credit may be made in a 12-month period.

Subd. 3. Repayment. Provides that decertification of a MBIC results in disallowance of any credits to the investors for that tax year and requires the investors to repay previously claimed credits within 60 days of the decertification or revocation.