HOUSE RESEARCH
Bill Summary

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Overview

This bill establishes a Minnesota Business Investment Company (MBIC) credit program, often referred to as CAPCO programs in other states, and modifies the angel investment credit program that was enacted by the 2010 Legislature.

CAPCO programs fund investments in venture capital investment firms by providing future credits against state premiums tax to insurance companies that invest in the state-designated venture capital firms. CAPCO refers to "certified capital companies," the firms that the state designates ("certifies") as a company that an insurance company may invest in and qualify for the program's tax credits.

The bill makes the following changes in the angel investment credit:

- Increases the annual limit on tax credits from $12 million to $20 million.
- Repeals the minimum wage requirements that apply to the businesses that receive the investments.
- Prohibits businesses receiving creditable investment from making a public stock offering or selling the business within six months after the investment was made.
- Allows contact information on the businesses receiving the credit to be disclosed to the public.

1 **Minnesota business investment company (MBIC) 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, directly or indirectly, 15 percent or more of the voting power of the securities of an MBIC or insurance company.

Allocation date is the date the tax credits are allocated to participating investors (insurance companies) in MBICs by the Department of Employment and Economic Development (DEED).

Designated capital is the amount the participating investor (insurance company) invests in an 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 an 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 an 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 an 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 8 are reduced by one-half.

State premium tax liability means insurance premiums tax liability.

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, have capitalization of $500,000 or more in liquid assets, and have at least two principals or persons employed 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, 2012.

Subd. 3. Requirements. Prohibits a participating investor (i.e., an insurance company) from owning more than 15 percent of the voting power of an MBIC, managing an MBIC, or directing an MBIC's investments, unless the MBIC is in default under its statutory or contractual obligations. An 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 claimed by all participating investors (insurance companies) to $100 million. No group of investors for one MBIC can file credit allocation claims in excess of $100 million. 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 an MBIC receives an allocation of credits and does not receive an investment of designated capital within 10 days, the credit allocation is forfeited. Forfeited credit allocations are, then, reallocated to other MBIC applicants. DEED can impose up to a $50,000 fine on the investor-insurance company that did not make the promised investment for the credits.

Subd. 5. Requirements for continuance of certification. Requires MBICs to invest a minimum percentage of their designated capital in qualified businesses 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	% of designated capital required to be invested
2	35%
3	50%
4	60%
6	100%

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 ($10,000 if filed after April 1) applies. DEED must notify an 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 an 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 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 6. 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. Rulemaking. Provides DEED is exempt from the Administrative Procedures Act (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 attracted
- 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
- Gross number of jobs created and retained
- Locations of the companies
- MBICs that were decertified and reasons for doing so
- Other information

2 **Angel credit; definitions.** Makes two changes in the definition provisions for the angel investment credit:

- Repeals the definition of an intern since section 3 eliminates the compensation limitations that use the term intern.
- Eliminates debt with a mandatory conversion to equity as a type of qualifying investment under the credit.

3 **Angel credit; qualifying small business.** Makes two changes in the requirements that a small business must satisfy to qualify under the angel investment credit:

- Eliminates the compensation or minimum wage requirements. These restrictions require the business to pay annual wages to employees equal to 175 percent of federal poverty guidelines for a family of four and to interns equal to 175 percent of federal minimum wage. These rules do not apply to executives, officers, and board members.
- Prohibits the company from having its securities trade on a public stock exchange or to sell the business within 180 days of the date the investment qualifying for the credit was made.

4 **Angel credit; annual limit.** Increase the annual cap on angel credit allocations from $12 million to $20 million, effective for tax years 2012 to 2014. Retains the present law sunset of the credit after 2014.

5 **Angel credit, permitted disclosure.** Modifies the exemption from the data practices act for disclosure of information on the businesses that receive investments qualifying for the angel credit. Under present law, only the name of the qualified business may be disclosed. This section would allow the mailing address, telephone number, e-mail address, contact person's name, and industry type to also be disclosed.

6 **Credit allowed against premiums tax.** Allows the MBIC credit against the insurance premiums tax.

Subd. 1. Credit allowed. Allows a participating investor in an MBIC an 85 percent credit for the amount of the investment. This credit is claimed in five installments, as follows:

- Tax year 2016: 10 percent
- Tax year 2017: 15 percent
- Tax years 2018 - 2020: 20 percent per year

The credit is limited to premiums 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. If decertification occurs in the first two years after allocation of the credit, the entire credit is recaptured. 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 it 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.