

OKLAHOMA TAX COMMISSION

TAX POLICY AND RESEARCH DIVISION
TONY MASTIN, DIRECTOR

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September 8, 2006

Re: Our file number LR-06-133

Dear

This letter ruling is in response to your inquiry of August 2, 2006 where in you posed a series of ruling requests relating to the Small Business Capital Formation Incentive Act (68 O.S. §2357.60 et. seq.) and Rural Venture Capital Formation Incentive Act (68 O.S. §2357.70 et seq.). Following a restatement of the facts outlined in your letter, are the specific rulings requested and our responses thereto.

Statement of Facts:

In the prior ruling, LR-05-156, the Oklahoma Tax Commission determined that under the facts described in that request (and the supplemental information provided on December 21, 2005), the investments qualified for tax credits under the Small Business Capital Formation Incentive Act and the Rural Capital Formation Incentive Act.

The Fund was formed to make qualified investments in an entity that qualifies as both a qualified rural small business capital company and a qualified small business capital company (the "Capital Company"). To raise capital, the Fund offers its common units to investors and obtains venture loans from financial institutions.

The Capital Company has and will continue to invest in Oklahoma small business ventures as defined in 68 O.S. §2357.61.5, and in Oklahoma rural small business ventures as defined in 68 O.S. §2357.72.6 located in metropolitan or rural areas of Oklahoma as required by the corresponding statutes. The Fund also makes direct investments in Oklahoma small business ventures and Oklahoma rural small business ventures pursuant to the provisions of the Small Business Capital Formation Incentive Act and the Rural Capital Formation Incentive Act in conjunction with the investments in the Oklahoma small business ventures and Oklahoma rural small business ventures made by the Capital Company.

The prior ruling held that the 30% credit earned by the Fund on its investment in the

Capital Company under 68 O.S. §2357.73 and the 20% credit on its investment in the Capital Company under 68 O.S. §2357.62 will pass through and be available to the members of the Fund in proportion to their investment in the Fund; that the credits will pass through to members of the Fund and be usable by them against any tax of the member then due for the current tax year plus any carry-forwards under the tax provisions of the statute, including estimated income tax payments; that the Capital Company will be considered to have invested not more than 25 % of its funds in each Oklahoma rural business venture under 68 O.S. §2357.72 and not more than 20% of its funds in each Oklahoma small business venture under 68 O.S. §2357.61; that the direct investment by the Fund in each business venture will qualify for the tax credits described under 68 O.S. §2357.63 and 2357.74; and that tax credits earned pursuant to 68 O.S. §§2357.62, 2357.63, 2357.73, and 2357.74 and being carried forward up to ten years under the relevant provisions of those sections will be allowed to offset gross production tax beginning July 1, 2006.

Rulings Requested:

1. The prior favorable determination letter (LR-05-156) and all supplemental rulings relating to the Fund will be upheld by the Oklahoma Tax Commission pursuant to the provisions of 68 O.S. §2357.63E and 68 O.S. §2357.74E because the Fund's Investment in the Capital Company consisting of equity and debt is at risk and investments were and continue to be made to further legitimate business purposes and are not made primarily for the purpose of reducing tax liability, and the Fund shall maintain Its ability to claim or otherwise utilize the tax credits authorized pursuant to the provisions of 68 O.S. §§2357.62, 2357.73, 2357.73 and 2357.74 and shall not be subject to the amendments to the Small Business Capital Formation Incentive Act or the Rural Capital Formation Incentive Act until November 1, 2006.

Yes. The rulings were contained within a "favorable determination letter" as required under §2357.63E and §2357.74E and were issued by this office prior to March 15, 2006. Entities who have obtained a favorable determination letter from the Oklahoma Tax Commission prior to March 15, 2006 will be deemed to have made a qualified investment and met the requirements of 68 Okla. Stat. § 2357.63E and § 2357.74E if:

(1) such investment is made prior to November 1, 2006 "... to satisfy a legitimate business purpose of the entity receiving such investment which is consistent with its organizational instruments, bylaws or other agreement responsible for the governance of the business venture";

(2) the capital company's funds were at risk; and

(3) if the investments meet the requirements of (1) above they will be deemed not to have been made chiefly for the purpose of reducing tax liability.

It will be necessary for the Tax Policy Division to review the actual investment plans, the bylaws or similar documents of the business venture, and any other necessary documentation prior to issuing a ruling as to whether the provisions of §2357.63E and §2357.74E have been met to qualify the investments in the business venture for the credits.

2. Based on the balancing methods used by the Capital Company, it will qualify as a qualified small business capital company pursuant to 68 O.S. §2357.61.7.d. and a qualified rural small business capital company pursuant to 68 O.S. §2357.72.8.d.

Yes. Based on the balancing methods used by the Capital Company, it will qualify as a qualified small business capital company pursuant to 68 O.S. §2357.61.7.d. and a qualified rural small business capital company pursuant to 68 O.S. §2357.72.8.d, provided, to maintain its status as a small business capital company the Capital Company may not invest more than 20% in any one company even if the company qualifies as a rural small business venture.

3. Tax credits earned upon qualified investments made prior to November 1, 2006 by the Capital Company for investments in Oklahoma small business ventures and Oklahoma rural small business ventures will be eligible to offset gross production taxes due under 68 O.S. §§1001 and 1102 and shall be available to be carried forward for ten (10) years from the date of the qualified investment.

Yes, the Capital Company and their investors may use their credits against Oklahoma gross production tax and the additional excise tax on oil and gas imposed under 68 Okla. Stat. §1001 and 1102 due on or after July 1, 2006, on qualified investments made in business ventures prior to November 1, 2006 and which meet the statutory requirements set forth in 68 Okla. Stat. §2357.63E and/or 68 Okla. Stat. §2357.74E.

Yes, the Capital Company and their investors may carry forward their credits for ten (10) years for investments made in business ventures prior to November 1, 2006 and which meet the statutory requirements set forth in 68 Okla. Stat. §2357.63E and/or 68 Okla. Stat. §2357.74E.

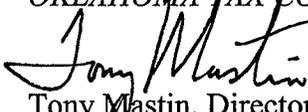
This response applies only to the circumstances set out in your request of August 2, 2006. Pursuant to Commission Rule 710:1-3-73(e), this Letter Ruling may be generally relied upon only by the entity to whom it is issued and its investors, assuming that all pertinent facts have been accurately and completely stated, and that there has been no change in applicable law.

Please be advised that the issuance of this ruling does not preclude the Oklahoma Tax Commission from conducting an audit or examination under 68 O.S. §206 if any report or return claiming a credit for the transactions outlined in this letter ruling. The Commission reserves the right to issue any assessment, correction, or adjustment authorized under 68 O.S. §221.

If I can be of further assistance, please feel free to contact me.

Sincerely,

OKLAHOMA TAX COMMISSION


Tony Mastin, Director
Tax Policy & Research Division