

OKLAHOMA TAX COMMISSION

TAX POLICY DIVISION
DAWN CASH, DIRECTOR

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October 30, 2007

REDACTED LETTER RULING

Re: LR-07-170

Dear

This letter ruling is in response to your letter ruling request dated October 15, 2007 and request for additional ruling dated October 25, 2007, wherein you posed a series of ruling requests relating to the Rural Venture Capital Formation Incentive Act (68 O.S. §2357.70 et seq.). Following a verbatim restatement of the facts outlined in your letters, are the specific rulings requested and our responses thereto.

FACTS

The [REDACTED] ("Fund") is a limited liability company formed under the laws of the State of Oklahoma on [REDACTED]. The purpose of the Fund is to raise equity capital from accredited investors and to aggregate such equity capital for investment in [REDACTED] ("CAPITAL COMPANY") and [REDACTED], an Oklahoma limited liability company ("VENTURE").

Fund will issue [REDACTED] shares of Common membership pursuant to the investment plan indicated on the attached flowchart.

For purposes of this letter, the terms "qualified rural small business capital company," "Oklahoma rural small business venture," "equity," "near-equity" and "subordinated debt" shall have the same meanings as are provided in the Act, as appropriate.

CAPITAL COMPANY is a [REDACTED] limited liability company organized to provide the direct investment of equity and near-equity funds to companies within the state of Oklahoma. CAPITAL COMPANY's principal place of business is [REDACTED]. The "capitalization," as defined in the Act, of CAPITAL COMPANY is greater than \$1,000,000. The investment into VENTURE at any time during calendar year 2007 will not be more than 25% of CAPITAL COMPANY's "capitalization," as defined in the Act.

VENTURE, an operating VENTURE company located in Oklahoma for more than [REDACTED] years, plans to [REDACTED]

[REDACTED]. The owners of VENTURE are [REDACTED]. They have been in the [REDACTED] business for more than [REDACTED] years. At the end of [REDACTED] VENTURE owned approximately [REDACTED]

In order to improve capacity and efficiency in production, VENTURE will [REDACTED]

VENTURE's affiliated entities have operated with approximately twenty-five (25) employees and an aggregate gross revenue of approximately four million dollars (\$4,000,000). Other than these entities and their employees, there are no other activities of [REDACTED] which should be aggregated with VENTURE's activities for purpose of determining VENTURE as an Oklahoma rural small business venture as defined in 68 O.S. § 2357.61 (5).

VENTURE needs financial assistance for additional capital in order to expand its business [REDACTED]. This capital will be raised by the Fund and invested in VENTURE as provided in the Act. The amount of total capital to be raised by the Fund is \$46,150,000. The amount of equity investment into the Fund will be \$46,150,000 for 45,800 shares of Common membership in the Fund. Certain holders of certain Fund shares will be allocated the Oklahoma Rural Venture Capital Formation Incentive Credits, while other shareholders will not.

The Fund's investment in CAPITAL COMPANY will take the form of equity capital. The \$46,150,000 investment will be in the form of equity capital as a result of the Fund purchasing [REDACTED] Units of CAPITAL COMPANY Series [REDACTED]. The holders of [REDACTED] Fund common shares which will contribute \$6,150,000 to the Fund will earn the entire 30% rural venture capital formation credit of \$13,845,000 ("Credits").

CAPITAL COMPANY will loan \$40,000,000 in subordinated debt to VENTURE and will invest \$6,150,000 into VENTURE's [REDACTED] membership equity capital. The debt will be subordinate to all other debt of VENTURE issued or to be issued to a financial lending institution as required by 68 O.S. § 2357.72(9). The debt will be "near equity" as defined in 68 O.S. § 2357.72(3) and required by 68 O.S. § 2357.74(B)(2) by being convertible dollar for dollar (\$1 for \$1)

into VENTURE's [REDACTED] membership interest upon the consent of CAPITAL COMPANY. Further, [REDACTED] will be required to guarantee the CAPITAL COMPANY loans.

In addition, the Investors and [REDACTED] will grant to each other overlapping call and put options for the [REDACTED] Shares of the Fund owned by the Investors at [REDACTED] per Share plus an amount of Net Income allocated to the [REDACTED]. The options relating to the [REDACTED] Shares are exercisable any time between January 1, 2008 and the fifth anniversary of the Closing. Similar options will be granted for [REDACTED] of the Shares at a price of one dollar (\$1.00) per Share. The options relating to the [REDACTED] Shares are exercisable any time between the closing of the transactions contemplated in this letter ("Closing") and December 24, 2007. Copies of the form of such agreements are also included.

Immediately after the investment, VENTURE will have more than fifty percent (50%) of its assets and more than ninety percent (90%) of its employees located in Oklahoma. VENTURE will conduct the activities resulting in at least seventy-five percent (75%) of its respective gross annual revenues from its principal place of business in [REDACTED], Oklahoma. VENTURE's business activities will be described in the Standard Industrial Classification Manual as Division [REDACTED]; Major Group [REDACTED] Business Services; Industry Group [REDACTED] - [REDACTED]; SIC [REDACTED] - [REDACTED].

The Fund believes that the VENTURE will qualify as a small business as defined by the federal Small Business Administration. The Small Business Administration defines a "small business concern" as a business entity organized for profit, with a place of business located in the United States, which operates primarily within the United States and meets the size standard applicable for the NAICS code in which the business entity operates. The NAICS code for VENTURE is [REDACTED] with a size standard of \$6.5 million dollars in annual revenues. Whether or not a business entity meets the size standards described above is determined by reference to an entity's "annual receipts," which is defined as gross or total income, including cost of goods sold, of a company as reported on the company's Federal income tax return and averaged over the latest three completed fiscal years. The average gross income for VENTURE for the past three tax years (2004, 2005, and 2006) is \$2,414,112. The gross income for the current tax year, through August 31, 2007, is \$4,090,408. When annualized, the current gross income is \$6,135,612, which is less than the size standard for VENTURE NAICS code. Further, VENTURE is an entity organized for profit with a business location in the United States and will operate primarily in the United States. Therefore, the Fund believes that the VENTURE will qualify as a "small business," as defined by the Small Business Administration.

The following documents are enclosed for your review:

- Flow Chart of Investment Structure (Tab A);
- Proforma Financial Statements (Tab B);

- Proposed Offering Terms (Tab C);
- [REDACTED] VENTURE, LLC Operating Agreement (Tab D);
- [REDACTED], LLC Operating Agreement (Tab E);
- [REDACTED], LLC Subscription Agreement (Tab F);
- [REDACTED] Put and Call Option Agreements (Tab G);
- [REDACTED] Put and Call Option Agreements (Tab H)

ADDITIONAL FACTS

In addition to the CAPITAL COMPANY loans, VENTURE will borrow ten million dollars (\$10,000,000) from [REDACTED] ("BUSINESS DEVELOPMENT COMPANY"), which borrowing (according to the terms negotiated in the capital transactions) will be subordinate to the CAPITAL COMPANY loans.

BUSINESS DEVELOPMENT COMPANY is a NASDAQ publicly traded corporation (symbol "[REDACTED]"). It is registered with the Securities and Exchange Commission as a "business development company" under the Investment Company Act of 1940. 15 U.S.C. § 80a-51. See also, 15 U.S.C. § 80a-1 et seq. A business development company by definition is required to provide "significant managerial assistance" to its portfolio companies whose securities comprise at least seventy percent (70%) in value of its total assets. 15 U.S.C. § 80a-2(a)(48). By reason of BUSINESS DEVELOPMENT COMPANY's election to be a business development company, it is exempted from numerous regulatory burdens imposed generally on publicly traded "investment companies." 15 U.S.C. § 80a-6(f).

For United States income tax purposes, BUSINESS DEVELOPMENT COMPANY has elected to be treated as a "regulated investment company" under section 851, et seq., of the Internal Revenue Code of 1986, as amended, commonly known as a "mutual fund."

BUSINESS DEVELOPMENT COMPANY, as a business development company mutual fund, is not a "financial lending institution" as defined in section 2357.72(4) of the Act. That definition states a financial lending institution "means a bank, credit union, savings and loan, commercial finance company or other entity principally engaged in the extension of credit." Such institutions are generally regulated and examined by federal and state "financial institution" regulatory organizations, including those of the Federal Financial Institutions Examination Council, i.e., the Federal Reserve Board of Governors, the FDIC, the National Credit Union Administration, the Comptroller of the Currency and the Office of Thrift Supervision, and also the Oklahoma State Banking Department and the Oklahoma Credit Union Board. BUSINESS DEVELOPMENT COMPANY is not regulated nor examined by any of these organizations.

RULINGS REQUESTED

1. CAPITAL COMPANY meets the definition of a "qualified rural small business capital company" within the meaning of 68 O.S. § 2357.72(8).

It is the ruling of the Tax Policy Division that CAPITAL COMPANY meets the definition of a "qualified rural small business capital company" as defined in 68 Okla. Stat. §2357.72(8) based on the following representations:

1. CAPITAL COMPANY is a limited liability company;
2. CAPITAL COMPANY is organized to provide the direct investment of equity and near-equity funds to companies within this state;
3. The principal place of business of CAPITAL COMPANY is in the state of Oklahoma;
4. The capitalization of CAPITAL COMPANY is greater than One Million Dollars (\$1,000,000.00); and
5. CAPITAL COMPANY has investment of not more than twenty-five percent (25%) of its capitalization in any one company at any time during the calendar year of CAPITAL COMPANY.

2. VENTURE meets the definition of an "Oklahoma rural small business venture" within the meaning of 68 O.S. § 2357.72(6).

Yes, it is the ruling of the Tax Policy Division that VENTURE meets the definition of an "Oklahoma rural small business venture" within the meaning of §2357.72(6) based on the following representations:

1. VENTURE will have at least 50% of its assets or employees located within Oklahoma;
2. VENTURE needs financial assistance for additional capital in order to expand its business [REDACTED];
3. At least seventy-five percent (75%) of VENTURE's gross annual revenues will be a result of activities conducted in [REDACTED], Oklahoma in an area deemed to be a non-metropolitan area;
4. VENTURE is engaged in a lawful business activity under Division [REDACTED] of the Standard Industrial Classification Manual;
5. VENTURE meets the definition of a small business by the federal Small Business Administration; and
6. VENTURE will expend within eighteen (18) months after the date of the qualified investment at least 50% of the investment for the acquisition of tangible or intangible assets which are used in the active conduct of the trade or business.

3. CAPITAL COMPANY's loans to VENTURE will constitute "near-equity security" and "subordinated debt" as defined in 68 O.S. § 2357.72(3) and (9), respectively.

Based upon the facts and other assertions contained in your October 15th and October 25th requests and the attached exhibits, CAPITAL COMPANY's loans to VENTURE will constitute "near-equity security" and "subordinated debt" as defined in 68 O.S. § 2357.72(3) and (9).

4. VENTURE's [REDACTED] membership interest will constitute "equity" as defined in 68 O.S. § 2357.72(3).

Based upon the facts and other assertions contained in your October 15th and October 25th requests and the attached exhibits, VENTURE's [REDACTED] membership interest will constitute "equity" as defined in 68 O.S. § 2357.72(3).

5. The investment by the Fund in CAPITAL COMPANY will meet the definition of a "qualified investment" within the meaning of 68 O.S. § 2357.72(7) and will qualify for the credit against tax provided in 68 O.S. § 2357.73(8).

Based upon the facts and other assertions contained in your October 15th and October 25th requests and the attached exhibits, only the amount of the investment by the Fund in CAPITAL COMPANY which is subsequently invested in VENTURE will qualify for the Oklahoma Tax Credits described in 68 Okla. Stat. §2357.73.

The investment by CAPITAL COMPANY in VENTURE will be a "qualified investment" within the meaning of 68 O.S. §2357.72(7) based, in part, on the following representations:

- 1. The qualified investment will be in the form of equity, near-equity or subordinated debt; and*
- 2. The funds will be used for a legitimate business purpose of VENTURE consistent with its operating agreement.*

6. The amount of the Credits under 68 O.S. §§ 2357.73(8) is 30% of the funds invested by CAPITAL COMPANY in VENTURE.

The amount of the credit is 30% of the qualified investment in CAPITAL COMPANY which is subsequently invested in VENTURE.

7. The Credits resulting from the investments will be available to offset the Oklahoma tax liabilities, as defined in the Act, of the member(s) of the Fund and may be allocated among the members of the Fund, in accordance with the terms of the Fund's operating agreement.

The Tax Policy Division agrees that shareholders, partners or members of a pass-through entity that are entitled to a credit under §2357.73 of Title 68 may receive an allocation of the credits from the pass-through entity, subject to the provisions of §2357.73(G). Once allocated to the shareholders, partners or members, the credits may be claimed to offset Oklahoma tax liabilities as defined in the Act. If the members of the Fund are pass-through entities, the allocation of credits is subject to the provisions of §2357.73(G).

8. The Credits arising from the investments by the Fund will be immediately usable by the members of the Fund, or the ultimate taxpayers if the members are flow-through entities, against any tax liability then due from such investor under 68 O.S. § 2355 (the "Oklahoma income tax"), 68 O.S. § 2370 (the "bank privilege tax") and 36 O.S. §§ 624 and 628 (the "insurance premium tax"), including estimated tax payments.

The tax credits resulting from the qualified investment in VENTURE by CAPITAL COMPANY, once allocated, will be immediately usable by the members of the Fund, or the ultimate taxpayers if the members of the Fund are flow-through entities, against any tax liability then due from such taxpayer under 68 Okla. Stat. § 2355 (the "Oklahoma income tax"), 68 Okla. Stat. § 2370 (the "bank privilege tax"), and 36 Okla. Stat. §§ 624 and 628 (the "insurance premium tax"), including estimated tax payments.

9. BUSINESS DEVELOPMENT COMPANY is not a "financial lending institution" under 68 O.S. § 2357.72(4) and its loan to VENTURE is not a loan to which

CAPITAL COMPANY's loans are required to be subordinated pursuant to 68 OS. § 2357.72(9).

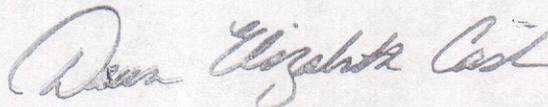
It is the ruling of the Tax Policy Division that BUSINESS DEVELOPMENT COMPANY is not a "financial lending institution" under 68 O.S. § 2357.72(4) and its loan to VENTURE is not a loan to which CAPITAL COMPANY's loans are required to be subordinated pursuant to 68 OS. § 2357.72(9).

This response applies only to the circumstances set out in your requests dated October 15 and October 25 2007. 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 Okla. Stat. §206 of 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 Okla. Stat. §221.

Sincerely,

Oklahoma Tax Commission



Dawn Cash, Director
Tax Policy & Research Division