

# OKLAHOMA TAX COMMISSION

TAX POLICY DIVISION  
DAWN CASH, DIRECTOR

PHONE (405) 521-3133  
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May 18, 2010

Re: LR-10-072  
[REDACTED]

Dear [REDACTED]:

This letter ruling is in response to your letter ruling request dated May 3, 2010, 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 as outlined in your letter, are the specific rulings requested and our responses thereto.

Client, [REDACTED], is an Oklahoma limited liability company, that is being formed as an "Oklahoma rural small business venture" (the "Venture") as defined in the Rural Venture Capital Formation Incentive Act, Tit. 68 O.S. § 2357.71 et. seq.. (the "Act").

The Venture intends to organize another Oklahoma limited liability company, [REDACTED] (the "Fund") for the purpose of allowing investors to make investments through the Fund into either: (i) a "qualified rural small business capital company" as defined in Tit. 68 O.S. § 2357.72(8) ("RSBC"), which will in turn invest such funds into the Venture; or (ii) directly into the Venture. It is intended for all investment proceeds contributed to the Fund to qualify for the Oklahoma tax credits provided for in the Rural Venture Capital Formation Incentive Act, Tit. 68 O.S. § 2357.71 et. seq.

## STATEMENT OF FACTS:

1. The Venture is an Oklahoma limited liability company that is being formed for the purpose of acquiring land and other assets held by [REDACTED] (" [REDACTED] "), an Oklahoma limited liability company and developing said land into a [REDACTED] in [REDACTED] County, Oklahoma. The Venture will acquire the land, purchase equipment associated with the development [REDACTED], construct new facilities, and hire new employees. [REDACTED] is currently owned by the investors in Venture.

██████ was purchased by investors in March of 2010 under an agreement that precluded the investors from making public disclosure of the transaction and required the investors to purchase all units of ██████ instead of the assets. Investors now need to refinance the transaction adding additional capital to complete Venture's business purpose of ██████, purchasing equipment, constructing new facilities ██████, and for working capital associated with the development and construction for the property (the "Project"). Therefore Venture requires financial assistance in order to commence its operations. The Venture will expend 50% or more of the investment proceeds received from RSBC and any direct investment received from the Fund within 18 months from the date the investment(s) are made. For these purposes, amounts spent by Venture to acquire the land from ██████ are not included. The Venture's principle place of business will be located in ██████ County, Oklahoma. At least seventy-five percent (75%) of the Venture's gross annual revenues will be a result of activities conducted in nonmetropolitan areas of the state. The Venture will have within 180 days from the date of investment at least 50% of its employees or assets located in Oklahoma. The Venture will be engaged in a lawful business activity under an Industry Number qualifying in 68 O.S. § 2357.72(6)(d), specifically Division █, Major Group █, Industry Group Number █, Section █ of the Standard Industrial Codes and will qualify as a "small business" as defined by the federal Small Business Administration because it will have annual gross receipts of less than \$7MM and is not affiliated with any similar entity with annual receipts greater than \$7MM.

2. The Fund will be formed as a limited liability company under Oklahoma law. The Fund will raise capital for the purpose of making venture capital investments in the Venture. Investments will be made through a designated series in the RSBC.

3. The Fund will raise all of its capital from investors. The Fund intends to issue two types of securities: (a) Common Units; and (b) Preferred Units. The subscription price for the Common Units may be more or less per unit than the subscription price of the Preferred Units.

4. The Fund intends to issue all of its Common Units to Common Investors in exchange for capital contributions to be made by the Common Investors to the Fund ("Common Unitholders"). Common Units will have all the attributes of traditional equity investments, excluding any allocation of Oklahoma state tax credits.

5. The Fund intends to issue its Preferred Units to Preferred Investors. Investors in the Preferred Units will be entitled to an allocation of Oklahoma Tax Credits as a return on their investment ("Preferred Unitholders").

6. The Operating Agreement of the Fund will provide that all state tax credits earned under the Act will be allocated 100% to the Preferred Unitholders. Distributions will be made 100% to the Preferred Unitholders until the distributions have been sufficient to provide to the Preferred Unitholders a return on their capital and a 20% percent annual return. Distributions will then be made 100% to the Common Unitholders until the cash distributions have been sufficient to provide the Common Investor a return on its capital contribution plus a 20% annual return. Thereafter distributions will be allocated pro-rata among all Members. After the cash distributions to the Preferred Unitholders have provided a return on investment plus a 20% annual return, all tax credits have been properly allocated to the Preferred Unitholders, and after

the Venture has satisfied the investment of proceeds requirement of 68 O.S. § 2357.74B(A)(1), the Fund will have the option to redeem the Preferred Units at 1 % of their original capital contribution.

7. The Fund intends to invest all or a portion of the capital it raises in an RSBC in return for at least 99.99% of all outstanding units of the RSBC's Series X (the "Equity Investment").

8. The RSBC is a "series" Oklahoma limited liability company registered and qualified to do business in Oklahoma with its principle place of business within Oklahoma and having the purpose of making direct investments into companies within Oklahoma. The RSBC will make qualified investments of "equity," "near equity" or "subordinated debt," into the Venture.

9. The Fund through its direct investment in Venture will have the right to elect the governing board for the Venture. The RSBC shall not own any direct or indirect voting interest in the Venture entitled to elect the governing board.

10. Capital Company investments in the Venture will be in the form of "equity and near equity securities" as defined in the Act. Specifically, it is expected that the Capital Company will use the proceeds from the Fund's series investment to make an equity investment into the Venture. The Venture will issue its equity securities within 30 days of the investment into the Venture by the RSBC.

11. The Qualified Investment made by the RSBC will be used for the Project in a manner consistent with its Operating Agreement. The Venture will expend at least 50% of the proceeds received from the Qualified Investment within eighteen (18) months of the date of the Qualified Investment for the acquisition of tangible or intangible assets which are used in the active conduct of the trade or business or for working capital for the active conduct of the trade or business for which the determination of the small business qualification was made as required by 68 O.S. § 2357.72 (6)(e).

12. The Fund, Venture and RSBC will be classified as a "partnership" for federal and state income tax purposes and shall always be operated in a manner consistent with such classification.

13. The RSBC shall satisfy all of the requirements set forth in Tit. 68 O.S. § 2357.72(8) for qualification as a "qualified rural small business capital company" and will comply with the requirements set forth in 68 O.S. § 2357.74 A (A) (2), (4) & (5).

**RULINGS REQUESTED:**

Based on these facts, the Venture respectfully requests a letter ruling from the Tax Policy and Research Division of the Oklahoma Tax Commission that:

1. The Venture will qualify as an "Oklahoma rural small business venture" as defined in 68 O.S. § 2357.72(6).

*It is the ruling of the Tax Policy Division that [REDACTED] meets the definition of an "Oklahoma rural small business venture" within the meaning of §2357.72(6) based on the following representations:*

- a. [REDACTED] will have at least 50% of its assets or employees located in Oklahoma within 180 days after a qualified investment is made;
- b. [REDACTED] needs financial assistance to acquire land, purchase equipment and construct new facilities as described in the letter ruling request;
- c. [REDACTED] will qualify as a small business as defined by the federal Small Business Administration;
- d. At least seventy-five percent (75%) of [REDACTED]'s gross annual revenues will be a result of activities conducted in areas deemed to be non-metropolitan areas;
- e. [REDACTED] is engaged in a lawful business activity under Division [REDACTED] of the Standard Industrial Classification Manual; and
- f. [REDACTED] 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 or for working capital.

2. The Fund will be entitled to the 30% tax credit described in 68 O.S. § 2357.73 resulting from its investment in the RSBC to the extent of the RSBC's investment in Venture.

*Yes. The credit in 68 O.S. § 2357.73 is for qualified investments which are actually invested in an Oklahoma rural small business venture and used in pursuit of a legitimate business purpose.*

3. The Fund will be entitled to the 30% tax credit described in 68 O.S. § 2357.74 resulting from its direct investment in Venture.

*Yes. A shareholder or partner of a qualified rural small business capital company that has made a qualified investment in an Oklahoma rural small business venture may make a direct investment in an Oklahoma rural small business venture to the extent allowable under the provisions of Section 2357.74 of Title 68.*

4. Tax credits generated will be based on 100% of the investment proceeds received by Venture from investments made directly from Fund and investment from the RSBC.

*Yes, the amount of the credit is 30% of the qualified investment in Capital Company which is subsequently invested in [REDACTED] and 30% of the qualified investment made directly by [REDACTED] into [REDACTED] (to the extent allowable under the provisions of Section 2357.74 of Title 68) provided the investment is used in pursuit of a legitimate business purpose.*

5. The tax credits earned by the Fund may be allocated 100% to the Preferred

Unitholders in portion to their pro rata share of the investment.

*The Tax Policy Division agrees that shareholders, partners or members of pass-through entities that are entitled to a credit pursuant to the Rural Venture Capital Formation Incentive Act may receive an allocation of the credits from the pass-through entity pursuant to the limitations provided in 68 O.S. §2357.73.*

6. Upon the statutory requirements being met, the tax credits generated may be immediately used by Preferred Unitholders against any tax then due for the Preferred Unitholder's current tax year as well as future tax years under the carry-forward provisions of the statute.

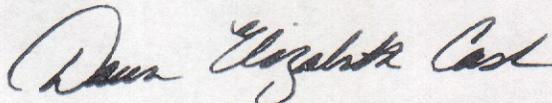
*Shareholders, partners or members of pass-through entities that are entitled to a credit under §§2357.73 and 2357.74 of Title 68 may receive an allocation of the credits from the pass-through entity. Once allocated to the shareholders, partners or members, the credits may immediately be used to offset various Oklahoma tax liability for the same year in which the investment was made, including Oklahoma income taxes, bank privilege taxes and insurance company premium taxes when due. The credit may also be used to offset estimated income taxes; however, if the credit exceeds the amount of taxes due, the amount of the claim not used may be carried forward to a future taxable year but may not be used to offset estimated tax liabilities to generate a refund of the credits.*

This response applies only to the circumstances set out in your request dated May 3, 2010. 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 Elizabeth Cash, Director  
Tax Policy & Research Division