

CHAPTER 4

INVESTMENT TAX CREDITS RELATING TO INVESTMENTS IN A FUND OF FUNDS
ORGANIZED BY THE IOWA CAPITAL INVESTMENT CORPORATION

123—4.1(15E) Contingent tax credits relating to investments in Iowa fund of funds. Contingent tax credits are available for designated investors in the Iowa fund of funds organized by the Iowa capital investment corporation in accordance with Iowa Code section 15E.65. Tax credit certificates related to the contingent tax credits will be issued by the Iowa capital investment board. If the tax credit certificates are redeemed, a taxpayer may claim a credit against the taxpayer's tax liability for personal net income tax imposed under Iowa Code chapter 422, division II; business tax on corporations imposed under Iowa Code chapter 422, division III; taxation of financial institutions imposed under Iowa Code chapter 422, division V; taxation of insurance companies imposed under Iowa Code chapter 432; or taxation of credit unions imposed under Iowa Code section 533.24.

123—4.2(15E) Definitions. The following definitions are applicable to this chapter:

"Act" means Iowa Code sections 15E.61 through 15E.69.

"Actual return" means the actual aggregate amount of moneys or the fair market value of property received from a fund of funds by a designated investor, with respect to an investment amount for which a certificate is issued, including amounts received as returns of invested capital or returns on invested capital and amounts received in excess of invested capital, in whatever form received for the period from the date of the closing to the applicable maturity date.

"Board" means the Iowa capital investment board created under Iowa Code section 15E.63.

"Certificate" or *"tax credit certificate"* means a document constituting a contract between the state of Iowa and a holder and evidencing a tax credit that has been issued and, subject to the contingencies described on the certificate, that may become available to the holder.

"Certificate register" means the register to be maintained by the department recording the name, address, and taxpayer identification number of each holder and the maximum potential amount of the tax credits represented by each certificate issued to each holder.

"Closing" means a time when a certificate is issued to a designated investor in exchange for a commitment to contribute cash to the capital of a fund of funds.

"Commitment" or *"commits"* means either a binding obligation undertaken at a closing to invest in a fund of funds in the future or an actual investment made in a fund of funds, but without counting the same amount twice.

"Contingencies" shall mean the conditions under which a tax credit may be claimed and shall include each of the following:

1. The condition that the tax credits may only be used to the extent that the actual return on the investment amount associated with the certificate is less than the applicable scheduled return on such investment amount, and then only to the extent such tax credit becomes a verified tax credit;

2. The condition that the amount of the total verified tax credits represented by such certificate that first may be claimed during any redemption year will be limited to the amount verified by the board to the department;

3. The condition that no amount of the tax credit may be claimed prior to a maturity date stated on the certificate; and

4. The condition that receipt by the designated investor of an actual return on the investment amount associated with the certificate equal to the scheduled return on such investment amount will result in the cancellation of the tax credit certificate.

"Day" means any weekday Monday through Friday that is not a legal holiday in the state of Iowa.

"Department" means the Iowa department of revenue.

"Designated investor" means a natural person or an entity, other than the Iowa capital investment corporation or the revolving fund, that has committed to contribute capital to a fund of funds, and such person's or entity's successors and assignees.

"Fiscal year" means the fiscal year for the state of Iowa.

“Fund of funds” means any private, for-profit limited partnership or limited liability company established by the Iowa capital investment corporation to which a designated investor commits to make a capital contribution.

“Holder” means a holder of a tax credit certificate, either as a designated investor or as a transferee of a designated investor, as reflected on the certificate register.

“Investment amount” means the amount of cash contributed by a designated investor to a fund of funds with respect to which a certificate has been issued.

“Iowa capital investment corporation” means the private, nonprofit corporation created pursuant to Iowa Code section 15E.64.

“Maturity date” means a specific date or dates specified in a certificate, representing the earliest date on which a holder of the certificate may use it to satisfy tax liabilities.

“Percentage of return” means the percentage represented by the quotient of (1) the actual return for a designated investor on the investment amount associated with a certificate divided by (2) the scheduled return for such designated investor on such investment amount.

“Portfolio entity” means a venture capital fund or direct investment entity in which a fund of funds makes an investment.

“Redeem” means, with respect to a certificate, to present such certificate to the department as payment for tax liabilities due or to become due on or after the date of such presentation.

“Redemption year” means each calendar year for which verified tax credits associated with a certificate may first be utilized to reduce tax liabilities.

“Revolving fund” means the private, for-profit limited liability company established by the Iowa capital investment corporation as a revolving fund of funds pursuant to Iowa Code section 15E.65.

“Scheduled return” means the scheduled return, whether in money or property, (including returns of and returns on investment) with respect to an investment amount associated with a certificate issued to a designated investor in a fund of funds determined in accordance with the limited partnership agreement or the operating agreement of such fund of funds for the period from the date of the closing to the applicable maturity date. If relevant for determining the amount of the scheduled return, the board shall presume that a verified tax credit will be transferred at 100 percent of the amount stated on the verified tax credit. It shall be the burden of a designated investor to show that the verified tax credit cannot be transferred without discounting the amount stated on such credit.

“Tax credit” means a contingent tax credit authorized pursuant to Iowa Code section 15E.66 that is available against tax liabilities up to the amount stated on the certificate for such tax credit.

“Tax liabilities” means those tax liabilities identified in rule 123—4.1(15E).

“Verified tax credits” means tax credits that have been verified by the board to the department and to the holder of the certificate that represents such tax credits. In the event that the verified tax credits are different from the amount certified by the Iowa capital investment corporation, the amount verified by the board shall control.

[ARC 0076C, IAB 4/4/12, effective 4/4/12]

123—4.3(15E) Report of the Iowa capital investment corporation. No less than ten days prior to each closing, the Iowa capital investment corporation shall deliver a written report to the board and to the department containing the following information:

1. A copy of the certificate of limited partnership or articles of organization of the fund of funds for which the closing is scheduled, certified by the Iowa secretary of state;
2. A summary of the terms of the anticipated investments in such fund of funds as contained in the limited partnership agreement or the operating agreement of the fund of funds; and
3. A statement of the anticipated date of the closing.

No less than two days prior to each closing, the Iowa capital investment corporation shall deliver to the board a signed statement of an officer of the Iowa capital investment corporation certifying the names, addresses and taxpayer identification numbers of the persons expected to be designated investors at the closing, the total amount of the capital commitments expected to be received at the closing, the maximum amount of tax credits to be represented by each certificate to be issued at the closing, the date

of the anticipated closing, the maturity date or dates for each certificate to be issued at the closing, the contingencies applicable to the tax credits, and the calculation formula for determining the scheduled return.

123—4.4(15E) Allocation and issuance of certificates. Certificates shall be issued only by the board and only with respect to an actual capital commitment to a fund of funds.

Following receipt of the certification of the Iowa capital investment corporation pursuant to rule 123—4.3(15E), the board shall issue a certificate to each such designated investor at the closing. The maximum amount of tax credits represented by each certificate shall be calculated in accordance with the limited partnership agreement or operating agreement of the applicable fund of funds. The board shall not issue certificates if, in the aggregate, the maximum amount of tax credits represented by all issued and uncanceled certificates at any time would exceed \$60 million (less the aggregate amount of any tax credits that have been used to reduce tax liabilities) calculated in accordance with Iowa Code section 15E.66.

A tax credit certificate shall contain, or incorporate by reference to another document, each of the following:

1. The name, address, and tax identification number of the holder;
2. The investment amount committed upon issuance of that certificate and (if applicable) the class of interests issued to the designated investor that has committed to make such investment amount;
3. All of the contingencies applicable to the tax credits;
4. The date of issue of the certificate;
5. The maximum amount of the tax credit represented by the certificate;
6. The maturity date or dates of the certificate;
7. The calculation formula for determining the scheduled return;
8. The calculation formula for determining the amount of the tax credit that may be used to reduce tax liabilities;
9. If the certificate is issued upon a transfer after verification in accordance with 123—4.5(15E), the amount of the verified tax credits represented by such certificate and the redemption year(s) for which they may be used to reduce tax liabilities; and
10. A statement that, although the certificate is not considered a security pursuant to Iowa Code chapter 502, the certificate constitutes a security as such term is defined in Iowa Code section 554.8102(1)“o” solely for purposes of the creation, perfection, priority and enforcement of security interests.

[ARC 9030B, IAB 8/25/10, effective 9/29/10]

123—4.5(15E) Procedures for verification of tax credits.

4.5(1) At any time after the applicable maturity date for a certificate, the holder may present such certificate to the Iowa capital investment corporation for certification. Within ten days after receipt of such certificate, the Iowa capital investment corporation shall certify to the board the percentage of return for the designated investor for such certificate. If the percentage of return is less than 100 percent, the Iowa capital investment corporation shall certify the resulting total amount of tax credits to be verified for use by the holder of such certificate in accordance with the terms of the limited partnership agreement or the operating agreement of the fund of funds. The Iowa capital investment corporation shall give notice of such percentage of return and such amount of tax credits to the holder of such certificate at the holder's address as it appears on the certificate register.

4.5(2) The Iowa capital investment corporation, and any entity with which the corporation has entered into agreements pursuant to the investments and financial transactions described in Iowa Code chapter 15E, division VII, shall provide all documents that the board finds are, or may become, necessary for the board to verify the amount of tax credits to be issued pursuant to this chapter. Such documents include but are not limited to the following:

- a. Financial transactions related to the Iowa capital investment corporation, the Iowa fund of funds, designated investors, lenders, or portfolio entities.

b. Financial documents, loan agreements, and security instruments to which any of the Iowa capital investment corporation, the Iowa fund of funds, designated investors, lenders, or a portfolio entity is a party.

c. Investment agreements to which any of the Iowa capital investment corporation, the Iowa fund of funds, designated investors, lenders, or a portfolio entity is a party.

d. All legal documents and correspondence related to the documents described in paragraphs 4.5(2) “a” through 4.5(2) “c” to which any of the Iowa capital investment corporation, the Iowa fund of funds, designated investors, lenders, or a portfolio entity is a party.

e. All documents and financial information necessary to calculate the actual return, the scheduled return, and the percentage of return.

f. Any other documents the board deems necessary to assess compliance with Iowa Code chapter 15E, division VII, or this chapter or to correctly verify the amount of tax credits related to a certificate issued pursuant to this chapter.

4.5(3) Within 30 days of the receipt of all documents and information pursuant to subrule 4.5(2), the board shall establish and verify the amount of tax credits related to that certificate, if any, that may be initially used in each redemption year so that no more than \$20 million in tax credits, in the aggregate, may become useable to reduce tax liabilities in any fiscal year (provided that such \$20 million limitation shall not limit the carryforward of tax credits otherwise authorized by the Act or these rules). Except to the extent specifically required by the \$20 million annual limitation, all tax credits relating to a verified certificate shall be useable to satisfy tax liabilities for a tax year beginning on or after the maturity date and ending at the expiration of the carryforward period specified in rule 123—4.10(15E).

4.5(4) The board shall issue to the holder of such certificate a verification setting forth (a) the amount of verified tax credits represented by such certificate (if any) and (b) the amount of verified tax credits represented by such certificate that may first become useable to reduce tax liabilities in any redemption year (if any).

4.5(5) If the verified certificate has more than one maturity date, the board shall issue to the holder a certificate for the verified tax credits. The verified certificate will contain no contingencies. The board shall issue one or more balance certificates for any maturity dates for which tax credits are not then being verified.

4.5(6) Certificates being verified for a maturity date shall be verified pro rata with all other certificates being verified for the same maturity date.

4.5(7) If a contingent certificate has more than one maturity date, the most recent maturity date prior to the date on which the certificate was presented to the board for verification shall be the maturity date used for purposes of verification under this rule.

[ARC 0076C, IAB 4/4/12, effective 4/4/12]

123—4.6(15E) Contractual nature of certificates; irrevocability of tax credits. Upon the issuance of a certificate, the entitlement of a holder to use the tax credits represented by the certificate shall be final and permanent, subject only to the contingencies expressly stated or incorporated by reference in the certificate, and such entitlement shall not be subject to any further condition, reduction, modification, amendment, change, revocation, or recapture.

The entitlement of a holder to claim tax credits represented by a certificate shall constitute a contract between the state of Iowa on the one hand and such holder and the holder’s successors and assignees on the other hand which shall not be subject to modification, amendment, change or rescission without prior written consent of the holder as of the date of any such purported action. No such modification, amendment, change or rescission to which a holder may have agreed shall be binding upon any of the successors or assignees of such holder unless it is stated in the text of the certificate issued to such successor or assignee.

The entitlement of a holder to claim tax credits represented by such certificate shall not be affected in any way or become subject to forfeiture or recapture by:

1. Action or inaction of the holder or designated investor;

2. The transfer by the designated investor of all or any portion of the designated investor's interest in a fund of funds;

3. The determination after the closing that a fund of funds was not organized or did not make its investments in accordance with the requirements of the Act or these rules;

4. The invalidity or illegality for any reason of the existence or functions of the board, the revolving fund, a fund of funds or the Iowa capital investment corporation or the investments made by a fund of funds or one or more of the portfolio entities;

5. The bankruptcy, insolvency, reorganization, merger, consolidation, dissolution or liquidation of the board, the revolving fund, any fund of funds, the Iowa capital investment corporation or any portfolio entity for any reason; or

6. The level, timing, or degree of success of any fund of funds or any portfolio entities, or the extent to which venture capital funds that are portfolio entities are invested in Iowa venture capital projects, or are successful in accomplishing any economic development objective.

If the legal existence of the board, the revolving fund, a fund of funds, the Iowa capital investment corporation or the department is ended or some or all of its respective functions are transferred to another entity at any time prior to the full use of 100 percent of the tax credits that could potentially be represented by all of the certificates, the board or its successor (or the state of Iowa if the legal existence of the board ends or the board ceases to have the requisite authority and there is no successor with such authority) shall adopt such rules as may be necessary to ensure the continuity and effectiveness of the entitlement of each holder to use the tax credits represented by such holder's certificate.

Upon the closing, a certificate shall be binding on the board, the department, and the state of Iowa, and the tax credits represented thereby shall not be modified, terminated, or rescinded or subject to recapture.

123—4.7(15E) Transfer of tax credit certificates. Certificates shall be transferable by the holders and any subsequent holders to any transferee or transferees.

Transfer of a certificate may be effected only by the holder's surrender of the certificate to the board with an endorsement in favor of the transferee, or transferees, and a statement containing the name, address and tax identification number of the transferee, and a written request for the board to issue a replacement certificate or certificates in the name of the transferee(s) (as well as, in any case where the transferor requests that more than one replacement certificate be issued, a statement by the transferor that sets forth the aggregate amount of tax credits represented by the transferred certificate that are to be represented by each replacement certificate).

Within ten days after the surrender and endorsement of a certificate, the board shall issue a replacement certificate or certificates in the name of the transferee(s). Once a transferor of a certificate has surrendered a certificate to the board, such transferor may no longer use the tax credits represented by such certificate.

A holder shall have the right to pledge and grant security interests in certificates and tax credits held by such holder as collateral for loans to or other obligations of such holder.

123—4.8(15E) Cancellation of tax credits upon receipt of scheduled return. Tax credits represented by a certificate are subject to cancellation only as provided in the certificate and upon receipt by the designated investor of an actual return equal to the designated investor's scheduled return with respect to such certificate. At the time of each distribution to a designated investor in a fund of funds, the Iowa capital investment corporation shall determine the amount of tax credits related to each certificate that have been canceled and have become null and void by reason of such distribution, if any, and shall certify such amount to the board. After any such certification, the board shall certify to the holder of each such certificate, at the holder's address as shown on the certificate register, and to the department the amount of tax credits that are deemed to have been canceled and to be null and void. If at any time prior to a verification of a certificate the actual return of a designated investor shall equal the designated investor's scheduled return with respect to such certificate, and all other conditions for cancellation contained in the certificate have been met, the Iowa capital investment corporation shall so certify to the board. After any

such certification, the board shall certify to such holder at the holder's address as shown on the certificate register and to the department that such certificates shall be deemed to have been canceled and to be null and void. Tax credits that are canceled may be reissued with respect to the same or another fund of funds.

123—4.9(15E) Lost or mutilated tax credit certificates. Upon receipt of evidence satisfactory to the board of the loss, theft, destruction or mutilation of any certificate, and in case of any such loss, theft or destruction, upon delivery of any indemnity agreement satisfactory to the board, or in case of any such mutilation, upon surrender and cancellation of such certificate, the board shall issue and deliver to the holder a replacement certificate within ten days.

123—4.10(15E) Claiming the tax credits. The holder shall attach a copy of the verification or (if the applicable certificate has been transferred after the date of such verification) a copy of the certificate issued to such holder to any tax return in which verified tax credits are used to reduce tax liabilities. Verified tax credits may be carried forward by the holder for use in any of the seven calendar years following the initial redemption year. Verified tax credits may be used to make estimated tax payments insofar as the holder may take the amount of the tax credit into account in calculating the holder's estimated annual tax liability, thus reducing or eliminating the amount of estimated tax that would otherwise be payable. Verified tax credits not used after the expiration of such seven-calendar-year period shall be deemed to have been canceled and to be null and void and may be reissued in respect to the same or another fund of funds.

The following nonexclusive examples illustrate how this rule applies:

EXAMPLE 1: Holder X has redeemed Holder X's tax credit certificate and received verification from the board authorizing the use of the following amounts of tax credits to reduce tax liabilities in the indicated years: 2010: \$700,000; 2011: \$140,000; 2012: \$70,000. Holder X has zero Iowa tax liability in 2010, \$900,000 of tax liabilities in 2011 and \$100,000 of tax liabilities in 2012. Holder X may carry forward the \$700,000 in tax credits that were first useable in 2010. Holder X may use up to \$840,000 of tax credits in 2011 and \$70,000 in 2012.

EXAMPLE 2: Holder X has redeemed Holder X's tax credit certificate and received verification from the board authorizing the use of tax credits to reduce tax liabilities that are the same as in Example 1. Holder X has zero in Iowa taxable income in each of the years 2010 through 2014. Holder X may carry forward the \$700,000 of tax credits attributable to 2010 and use such tax credits in years 2015, 2016 and 2017 (i.e., up to seven tax years after 2010). To the extent that the \$700,000 of tax credits attributable to 2010 is not used by 2017, Holder X may no longer use such tax credits. Holder X may carry forward the \$140,000 of tax credits attributable to 2011 and use such tax credits in years 2015, 2016, 2017 and 2018 (i.e., up to seven tax years after 2011). To the extent that the \$140,000 of tax credits attributable to 2011 is not used by 2018, Holder X may no longer use such tax credits. Holder X may carry forward the \$70,000 of tax credits attributable to 2012 and use such tax credits in years 2015, 2016, 2017, 2018 and 2019 (i.e., up to seven tax years after 2012). To the extent that the \$70,000 of tax credits attributable to 2012 is not used by 2019, Holder X may no longer use such tax credits.

EXAMPLE 3: Holder X has redeemed Holder X's tax credit certificate and received verification from the board authorizing the use of tax credits to reduce tax liabilities that are the same as in Example 1. In 2011, Holder X actually uses \$840,000 of tax credits to reduce an equal amount of tax liabilities (reducing Holder X's tax liabilities in 2011 to zero). In 2014, as a result of an audit, Holder X's tax liabilities for 2011 are changed to \$700,000. That adjustment creates \$140,000 in tax credits that were not actually useable in 2011. Holder X may use this \$140,000 of tax credits in years 2012 through 2018.

If a holder is a partnership (whether general, limited or limited liability), limited liability company that has not elected to be taxed as a corporation for federal income tax purposes, or a corporation for which a valid Iowa "S" election is in effect, and such holder has no tax liability because only the partners, members or shareholders of such holder are subject to the tax liabilities imposed by the state of Iowa and described in section 15E.62(6) of the Act, the holder may allocate the tax credits represented by the holder's certificate among the holder's partners, members or shareholders. Such allocation shall be

made on the basis of the pro rata share of earnings from the partnership, limited liability company, or S corporation calculated in accordance with the organizational documents of the holder.

If a holder is an estate or trust, the tax credits represented by the holder's certificate shall be allocated to such estate or trust or to such other person to whom the income of such estate or trust is taxed in proportion to each such person's actuarial interest in such estate or trust.

123—4.11(15E) Notification to the department of revenue. Upon the issuance, distribution, redemption, or transfer of tax credit certificates, the board shall provide copies of the tax credit certificates or replacement certificates to the department of revenue.

123—4.12(15E) Other provisions. The department shall maintain the certificate register at its principal office. The certificate register shall be open to inspection by holders during the department's normal business hours. The department shall, upon request, issue confirmation as to the ownership of a certificate or entitlement to tax credits. The certificate registry is the conclusive record of holders and their entitlements to tax credits.

All notices, requests, and submissions required to be sent to the board shall be sent to the Iowa Capital Investment Board in care of the Iowa Department of Revenue, 1305 E. Walnut Street, Hoover State Office Building, Des Moines, Iowa 50319.

Each fund of funds shall principally make investments in venture capital funds managed by investment managers who have made a commitment to consider equity investments in businesses located within the state of Iowa and who have committed to maintain a physical presence within the state of Iowa. For purposes of this requirement, a physical presence in Iowa includes, but is not limited to, having an office or other business location in Iowa or having employees or representatives present in Iowa on a regular and continuing basis.

123—4.13(15E) Redemption date and priority of tax credits with respect to limited partnership interests in the Iowa fund of funds, Fund A. Rescinded IAB 4/13/05, effective 3/25/05.

123—4.14(15E) Scheduled return and tax credits represented by certificates issued with respect to Class C limited partnership interests in Fund A. Rescinded IAB 4/13/05, effective 3/25/05.

123—4.15(15E) Scheduled return and tax credits represented by certificates issued with respect to Class A limited partnership interests in the Iowa fund of funds, Fund A. Rescinded IAB 4/13/05, effective 3/25/05.

123—4.16(15E) Scheduled return and tax credits represented by certificates issued with respect to Class D limited partnership interests in Fund A. Rescinded IAB 4/13/05, effective 3/25/05.

These rules are intended to implement Iowa Code chapter 15E as amended by 2010 Iowa Acts, Senate File 2380.

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