

## Testimony—Interim Taxation Committee

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Prepared by Joseph Becker, Auditor III  
Research and Education Section  
North Dakota Office of State Tax Commissioner

Phone: 328-3451  
E-mail: jjbecker@state.nd.us

Chairman Cook and Members of the Committee:

### Introduction

My name is Joseph Becker, and I'm here on behalf of the North Dakota Office of State Tax Commissioner (Tax Department). The Tax Department was asked to appear before the Committee to provide a report on the North Dakota angel fund investment tax credit program.<sup>1</sup> Legislation passed by the 2011 North Dakota Legislature requires the Tax Department to report on the investment and credit activity under the program, including the number of in-state and out-of-state investors and the use of the credit transfer feature.<sup>2</sup>

### Background

The angel fund investment tax credit program was created in 2007.<sup>3</sup> It provides for an income tax credit equal to 45% of an investment made in a North Dakota angel fund, up to a maximum credit per year of \$45,000. The original legislation only required an angel fund to be incorporated in North Dakota. It did not define an angel fund or require any type of reporting.

In 2009, the law was amended to define an angel fund, establish qualifying criteria, including certification by the North Dakota Commerce Department, and to set a ceiling on the credits allowed per fund.<sup>4</sup>

The law was amended again in 2011 to set a ceiling on the credits allowed per investor and allow a one-time transfer of credits earned in the 2011 and 2012 tax years. Starting with investments made in 2011, the legislation also requires an angel fund to report to the Tax

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<sup>1</sup> N.D.C.C. § 57-38-01.26.

<sup>2</sup> S.L. 2011, ch. 461 (House Bill 1057), § 2.

<sup>3</sup> S.L. 2007, ch. 18, § 42.

<sup>4</sup> S.L. 2009, ch. 547, § 1.

Department investments received from investors as well as the name and principal place of business of the enterprises in its investment portfolio.<sup>5</sup>

Finally, in 2013, the law was amended to prohibit an angel fund from investing in real estate or real estate holding companies and to increase the investor credit ceiling.<sup>6</sup>

### **Angel fund investment and tax credit activity report**

Attached to my testimony is a table that provides the required information. It shows the data on a fund-by-fund basis and shows the numbers for North Dakota investors and out-of-state investors.

- The number of investors, amount invested, and tax credits earned are based on the investments made during the period January 1, 2011, through December 31, 2013, as reported on the investment reporting forms the funds filed with the Tax Department.
- The information on tax credits transferred to another taxpayer is based on the statements that the taxpayers involved in the transaction were required to file with the Tax Department at the time of the transfer.

**Required information.** Following is the information required to be included in the report:

1. Number of in-state and out-of-state investors in the angel funds.
  - Number of in-state (North Dakota) investors: 309.
  - Number of out-of-state investors: 27.
2. Amount invested in the angel funds: \$27,057,167.
3. Amount of tax credits accrued (or earned): \$10,266,755.
4. Amount of tax credits transferred to another taxpayer: \$296,264. (The transfer feature only applied to the 2011 and 2012 tax years; it expired at the end of the 2012 tax year.)
5. Amount of tax credits claimed on tax returns (fiscal impact): \$13,289,883.
  - This data was obtained from the 2011, 2012, and 2013 income tax returns.
  - The amount of tax credits claimed on income tax returns was not included in the table itself, but is provided in footnote 4 to the table, because it did not

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<sup>5</sup> S.L. 2011, ch. 461, § 1.

<sup>6</sup> S.L. 2013, ch. 449, § 9.

lend itself to the comparison of information based on investments made in the 2011 through 2013 calendar years. You will note that the amount of tax credits claimed on the returns exceeds the tax credits shown as earned. This is attributable to unused tax credit carryovers from one tax year to another (including those from tax years prior to 2011), how the tax credits were reported on individual income tax returns (which results in overstated data in some cases), and the filing of fiscal year returns by some taxpayers.

**Additional information.** Although not required as part of the report, we included in the report an additional set of columns on the right-hand side of the table to show the number of enterprises in which the angel funds invested their funds. The number of enterprises in each angel fund's investment portfolio is shown, broken down to show the number of enterprises based in North Dakota and the number of enterprises based outside North Dakota. This information was derived from the annual reports that the angel funds are required to file with the Tax Department.

### **Conclusion**

That concludes my testimony, Mr. Chairman. If there are any questions from the Committee, I would be glad to address them.

# Angel Fund Investment Tax Credit Program Summary of Investment and Credit Activity by Certified Angel Funds

For Investments Made During The Period January 1, 2011, through December 31, 2013

Name of Angel Fund	Number of Investors <sup>1</sup>			Amount Invested <sup>2</sup>			Tax Credits Earned <sup>3,4</sup>			Tax Credits Transferred To Another Taxpayer <sup>5</sup> (Only applied to the 2011-12 tax years)			Location and Number of Enterprises In Which Angel Fund Has Invested Its Funds		
	In-State Investors	Out-of-State Investors	Total	In-State Investors	Out-of-State Investors	Total	In-State Investors	Out-of-State Investors	Total	In-State Investors	Out-of-State Investors	Total	In North Dakota	Outside North Dakota	Total
1 Arthur Ventures Growth Fund LLC	6	4	10	\$ 2,273,856	\$ 2,028,141	\$ 4,301,997	\$ 321,405	\$ 238,773	\$ 560,178	\$ 0	\$ 0	\$ 0	4	3	7
2 Arthur Ventures LLC	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
3 Arthur Ventures Growth Fund II LP	0	0	0	0	0	0	0	0	0	0	0	0	0	4	4
4 Aurora Angel Fund LLC	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
5 Edgewood Angel Fund LLC	6	0	6	495,000	0	495,000	222,750	0	222,750	0	0	0	4	0	4
6 Flickertail Capital Ventures LLC	85	5	90	8,795,170	700,000	9,495,170	3,753,077	270,000	4,023,077	130,000	45,000	175,000	9	0	9
7 FM Angel Investment Fund LLC	22	3	25	435,000	60,000	495,000	175,500	27,000	202,500	0	0	0	2	12	14
8 Grow Dakota Angel Fund LLC	5	0	5	315,000	0	315,000	141,750	0	141,750	0	11,764	11,764	10	0	10
9 Harvest Fund I LLLP	9	7	16	150,000	100,000	250,000	67,500	45,000	112,500	0	0	0	0	1	1
10 Leading Edge Angel Fund LLC	22	0	22	2,950,000	0	2,950,000	1,305,000	0	1,305,000	42,000	0	42,000	0	2	2
11 Linn Grove Angel Fund LP	22	2	24	1,220,000	100,000	1,320,000	526,500	45,000	571,500	0	67,500	67,500	3	2	5
12 Northern Plains Investments LLC	0	0	0	0	0	0	0	0	0	0	0	0	1	6	7
13 Rain Venture 1 LLC	14	1	15	660,000	10,000	670,000	297,000	4,500	301,500	0	0	0	9	1	10
14 Rain Venture 2 LLC	43	1	44	1,824,000	10,000	1,834,000	820,800	4,500	825,300	0	0	0	14	6	20
15 Rain Venture 3 LLC	36	0	36	1,611,000	0	1,611,000	724,950	0	724,950	0	0	0	0	0	0
16 Southern Valley Angel Fund LLC	15	3	18	300,000	70,000	370,000	128,250	31,500	159,750	0	0	0	2	8	10
17 Springfield Group Angel Fund LLC	19	0	19	1,950,000	0	1,950,000	846,000	0	846,000	0	0	0	1	0	1
18 Valley Angel Investment Fund LLC	0	0	0	0	0	0	0	0	0	0	0	0	2	10	12
19 Wilbar Holdings LLC	5	1	6	800,000	200,000	1,000,000	225,000	45,000	270,000	0	0	0	2	2	4
<b>Totals—</b>															
<b>In-State Investors</b>	309			\$ 23,779,026			\$ 9,555,482			\$ 172,000			63	57	120
<b>Out-of-State Investors</b>		27			\$ 3,278,141			\$ 711,273			\$ 124,264				
<b>All investors</b>			336			\$ 27,057,167			\$ 10,266,755			\$ 296,264			

**Notes**

<sup>1</sup> The total number of investors will reflect an investor more than once if that investor made an investment in more than one fund.

<sup>2</sup> Investment amounts shown reflect the total amount invested. They do not reflect the following statutory limitations: (1) Annual limit—Only the first \$100,000 invested in a tax year by a taxpayer is eligible for the credit. (2) Lifetime limit—For tax years 2011 and 2012, a taxpayer was allowed no more than \$150,000 in total credits (equivalent to \$333,333 of eligible investments). For tax years 2013 and after, a taxpayer is allowed no more than \$500,000 in total credits (equivalent to \$1,111,111 of eligible investments). (3) Lifetime limit per angel fund—For investments made on or after January 1, 2009, no more than \$5,000,000 in total credits is allowed for total investments made in each angel fund, which is equivalent to \$11,111,111 of eligible investments.

<sup>3</sup> Tax credit amounts shown take into account the statutory limitations on the credit, which are set out in Note 2 above.

<sup>4</sup> Tax credits claimed on individual income tax returns for tax years 2011-2013 totaled \$13,289,883 (\$3,276,820 for 2011, \$6,598,897 for 2012, and \$3,414,166 for 2013). Data from corporation income tax returns is not included due to confidentiality. Due to how credits are reported on returns and unused credit carryovers from prior years, these amounts will not reconcile with the credits earned shown in table.

<sup>5</sup> For credits based on investments made in the 2011 and 2012 tax years only, credits could be transferred or sold to another taxpayer under certain conditions. The transfer feature expired at end of 2012 tax year.