

CAPCO

Frequently Asked Questions

Q: What is CAPCO?

A: The Certified Capital Company program, or CAPCO, is a legislatively enacted statute that assists states in management of capital formation or economic development objectives. It is a powerful state economic development tool that significantly leverages long term state tax credits into private venture capital funds that must invest in small business, resulting in more jobs and an increased tax base.

Q: How does CAPCO work?

A: The Certified Capital Company program, or CAPCO, is an economic development tool used by states to help small local businesses find the financial support they need to open or expand. CAPCO programs provide state “premium tax credits” to insurance companies who invest in CAPCOs, typically a venture capital firm with strong local knowledge and industry expertise. The funds invested in CAPCOs by insurance companies are in turn invested into growing in-state companies that typically have had difficulty finding financing from traditional sources, such as banks or traditional VCs.

CAPCOs invest the certified capital in Alabama “Qualified Technology Businesses” and “Qualified Diversity Businesses” subject to the following statutory criteria:

- (1) CAPCO must make qualified investment in amount cumulatively equal to a least 35 percent of its certified capital before the third anniversary of its allocation date.
- (2) CAPCO must make qualified investments in qualified technology business in amount equal to at least 50 percent of its certified capital before the fifth anniversary of its allocation date.
- (3) Premium tax credits may be forfeited for failure to meet investment timeline.
- (4) Distributions cannot be made until 100 percent of the certified capital is invested.
- (5) Qualified companies must be based in Alabama, have less than 100 employees and cannot be in retail sales, real estate, insurance, banking or provide professional services such as attorneys, accountants, or physicians.
- (6) Qualified companies must have a reasonable expectation of creating new permanent jobs in Alabama.

Q: What is a “QUALIFIED DIVERSITY BUSINESS”?

A: “Qualified Diversity Business” means any qualified technology business that meets the requirements of either subparagraph below and provides written certification thereof to a CAPCO:

- (1) The voting securities or other voting interests of the qualified technology business are at least fifty-one percent (51%) owned by one or more targeted individuals and its management and daily business operations are controlled by one or more of the targeted individuals who own it; or
- (2) The qualified technology business has its headquarters located in a low-income community, a historically underutilized business zone or an enterprise zone (as defined by the State or Federal statutes).

Q: How is CAPCO different from other state-sponsored loan pools or venture capital programs?

A: At its core, the CAPCO program is an economic development tool; alternative programs focus on rate of return rather than in-state job creation and economic development. Accordingly, it is designed to create jobs and increase state tax bases, as opposed to other state sponsored venture capital programs that simply serve as investment vehicles for state government. CAPCOs keep and grow investment dollars within the state sponsoring the program.

To fully understand the compensation for CAPCO managers, it is important to recognize the risk and return model for CAPCOs is different from the traditional venture capital firm. Unlike traditional firms, CAPCOs are governed by specific restrictions and mandates regarding the types of investments they can make. Accordingly, CAPCOs are required to invest 100 percent certified capital before any profits can be realized. CAPCO managers receive an industry standard 2.5 percent management fee.

Q: What kinds of restrictions are placed on CAPCO investments?

A: Unlike traditional venture capital firms, program limitations and restrictions mandate that CAPCOs must invest 100 percent of funds raised, including money taken out as management fee. In short, CAPCOs assume greater risk than traditional firms and are limited further in both range and size of investment. Finally, as CAPCOs are economic development tools, they are encouraged to invest in a broad range of companies throughout the state.

Q: Can Alabama CAPCOs invest in companies outside the state?

A: No. As CAPCOs are state-sponsored economic development tools whose purpose is to make investments in entrepreneurial companies, and ultimately create jobs and increase state tax bases; CAPCOs keep and grow investment dollars within the state sponsoring the program.