AN ADVENTURE FOR THE IOWA LEGISLATOR: VENTURE CAPITAL IN THE VALUE-ADDED INDUSTRY—A COMPREHENSIVE LOOK AT THE IOWA AGRICULTURAL FINANCE CORPORATION

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I. INTRODUCTION

Over the past decade, farmers have been faced with shrinking profit margins for the commodities they produce. Prices of raw agricultural commodities have remained constant or decreased for a number of reasons, largely beyond the scope of this Note. With the ever-decreasing prices farmers are able to bring in for commodities sold and the never-ending expansion of corporate owned farms, Iowa Legislators felt compelled to take steps to provide small, family-owned farmers in the value-added industry the ability to compete on the same footing as larger corporations. In recognizing the need, and the potential profitability that

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Iowans could realize from the value-added agricultural sector, the legislature enacted the Iowa Agricultural Industry Finance Act in 1998 ("Act").[1]

Generally, the Act provides a $25 million state loan to qualifying Iowa ventures in the value-added agricultural or biotechnology sector. The legislation is unique for two reasons. First, the Act provides public money in the form of a loan to support private venture opportunities. Second, the legislation has created a vehicle whereby Iowa farmers and agricultural producers are able to gain ownership in the companies that the state funded through the loan program. In essence, the Act allows for the formation of private companies with state funds – which the legislature relinquishes political control over – so long as the companies act within the established parameters of the legislation.

The purpose of the Act is to provide an interest free loan to value-added agricultural producers or biotechnology interests and allow them to pay back the money over a twenty-five year period; in the end, the farmers would then completely own the value-added ventures that were funded by the $25 million state loan.[2] Although the intent of the legislature in enacting the Iowa Agricultural Finance Act has not drawn any serious criticism, the manner through which the money has been placed into private qualifying value-added ventures has drawn sharp criticism.

The purpose of this Note is to provide the reader with an overview of the Iowa Legislature's intent in implementing the Act. Further, the steps necessary to obtain financing under the Act will be discussed, as well as implications of the Act on economic development in Iowa. Finally, the author will discuss potential problems that have arisen since enactment of the Act, as well as look at several allegations of impropriety pertaining to the fund as it currently operates.

II. WHY VALUE-ADDED & ITS IMPORTANCE TO THE IOWA ECONOMY

A. *Value-Added Defined*

The term 'value-added' describes the process of taking raw agricultural commodities and processing them into new or different forms.[3] The value-added concept is quite simple; take a product and add value to the product to increase overall profits on the sale of the commodity. For example, instead of selling soybeans straight out of the field, value can be added to the soybeans by process-

1. Iowa Agricultural Industry Finance Act, IOWA CODE §§ 15E.201-15E.211 (2003).
2. *See id.* § 15E.203 (2003).
3. Scott Flynn, *Putting the New Generation Cooperative in Perspective Within the Value-Added Industry*, 85 IOWA L. REV. 1473, 1474 (2000) (citations omitted).

ing them into soy-diesel.[4] Adding value to a commodity need not only come in forms of production of the commodity, value can also be added to products by implementing a new method to market the commodity. For example, a peach and pecan farmer wishing to add value to his commodities might accomplish such by creating special gift bags which contain peaches, peach pies, pecans, or pecan brittle.[5] The key to a successful value-added commodity is to identify a specialty, or "niche", market where there is a demand for value-added products. After a niche market has been identified, the value-added commodity can be sold to members of the niche group, thereby generating higher profits than the commodity alone would be able to yield.[6] "[T]he further into the value chain you can get, the more a company . . . can . . . produce what customers want and control gross margins."[7] Value-added processes will play such a large role in the future of the Iowa economy that some analysts predict "[t]he era of farmers making a decent profit from selling raw materials is over. They're going to have to learn to add value" if they want to compete in today's economy.[8]

Specifically, as value-added pertains to the Iowa Agricultural Industry Finance Act, there is an underlying requirement that the entity which receives proceeds from the state loan be an organization that either processes or markets agricultural or biotech goods.[9] This precludes the possibility of non-agricultural or non-biotechnology entities from receiving funding under the Act.

Additionally, there is an underlying requirement that loan proceeds expended on the "construction, expansion, or acquisition of an agricultural products processing facility" shall be used for a facility located in the State of Iowa.[10] Biotechnology organizations that receive proceeds from the loan are not required to have their principal office located in Iowa, but are required to be located in Iowa, and increase the value of agricultural commodities while creating wealth for Iowa residents.[11]

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4. See Rod Smith, Added-Value Needs Real, Protected Expectations, FEEDSTUFFS, June 3, 2002, at 28.

5. *See* Lorraine Hanover, *Choose Right Approach to Value-Added*, RESOURCE: ENGINEERING & TECHNOLOGY FOR A SUSTAINABLE WORLD, AGRITECH '99 SPECIAL EDITION, June 1999, at 34.

6. *See* Jerry Perkins, *Farmer of Future Needs a New Understanding,* DES MOINES REG., Mar. 28, 1999, at 10M.

7. Smith, *supra* note 4, at 31.

8. Hanover, *supra* note 5, at 34.

9. *See* Iowa Agricultural Industry Finance Act, IOWA CODE § 15E.209 (2003); *see also* IOWA AGRIC. FIN. CORP., 2001 ANN. REP.: VENTURE CAPITAL FOR GROWING IOWA 20 (2001) [hereinafter IAFC: 2001 ANN. REP.].

10. IOWA CODE § 15E.209.1.b(1) (2003).

11. *See id.* § 15E.202.14 (2003).

Finally, the Act specifically prohibits disbursement of loan proceeds to a habitual offender under Iowa Code Section 455B, pertaining to confinement feeding operations[12], large corporate-owned farms[13], as well as the refinancing of certain ventures.[14]

B. *Creation of the IAFC*

In 1998, the Iowa Legislature concluded that the ability of farmers in Iowa to prosper in the twenty-first century would, in large part, be based on their ability to process and market agricultural commodities because of the rapidly changing economic conditions of the world market.[15] Specifically, the legislature found that there is an increasing world demand for *high value* agricultural products.[16] In recognizing the important role that value-added commodities play in both the national and world economies, and determining that traditional sources of financing for valued-added industries were inadequate to meet the demands of the changing environment, the Iowa Legislature enacted the Iowa Agricultural Finance Corporation Act ("Act").[17] The purpose of the legislation is to encourage "local agricultural producer-led ventures to expand production and processing of high value agricultural products" by providing them with an interest free loan to accomplish said ends.[18] The benefits to Iowa of the legislation is discussed in greater detail later in the Note.[19]

In order to effectuate the legislation, the Act authorized a qualified entity to incorporate under Iowa law,[20]and at the same time, authorized limited state financial support to companies that incorporated under the Iowa Agricultural Industry Finance Act.[21] Thus, any qualified entity that incorporated under Chapter 490 of the Iowa Code could call itself an Iowa Agricultural Industry Finance Corporation ("IAFC").[22] Shortly after passage of the Iowa Agricultural Industry

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12. *Id.* § 15E.208.4.a(2) (2003).

13. *See id.* § 15E.202.5.b(2)(a) (2003) (excluding large corporate owned farms from the definition of agricultural producer).

14. *See id.* § 15E.209.3 (2003).

15. *See id.* § 15E.203 (2003).

16. *Id.* § 15E.203.2 (2003).

17. *See id.* § 15E.201-15E.211 (2003).

18. *Id.* § 15E.203.2 (2003).

19. *See infra* II. C. (discussing direct and indirect benefits to be derived from the legislation).

20. *Id.* § 15E.206 (2003); see also Rod Smith, *From Networked Pork Production to Soyfoods, Iowa Fund Links Producers to Downstream Value*, FEEDSTUFFS, June 3, 2002, at 1.

21. IOWA CODE § 15E.208 (2003).

22. *Id.* § 15E.205.1 (2003).

Finance Act, the IAFC was formed under the legislation.[23] The name that the corporation chose for itself was the Iowa Agricultural Industry Finance Corporation, which can become confusing because that is also the type of corporation that it is. It would be tantamount to an entity calling itself Limited Liability Company because that is the *type* of legal entity that it is. After the Iowa Department of Economic Development determined the IAFC fulfilled the requirements of the Act, it was then able to begin dispersing proceeds of the $25 million loan to the IAFC.[24]

One important aspect of the legislation is that the Act does not create a specific Iowa Agricultural Finance Corporation; instead, it *allows* for the creation of such a corporation.[25] Thus, an Iowa Agricultural Finance Corporation is not an entity of the state, it is a private entity. The purpose of the IAFC is to act as a vehicle, through which the state is able to place the $25 million loan into the hands of private, qualifying, value-added or biotechnology industries. The Act is "absolutely unique, in Iowa and the U.S.", in that it "funded a corporation to carry out a government mission but without government oversight."[26] The significance of the manner in which the Act allowed for creation of a private corporation is important for two reasons.

First, the Iowa Constitution prohibits the State from investing in or being a shareholder of any private individual or entity organization.[27] The Iowa Constitution also prohibits any private entity from becoming a state agency or public entity.[28]

Second, and more importantly, by allowing only for the incorporation of an IAFC, the state relinquished political control over the organization; it is for virtually all purposes a private entity free from state control, so long as the IAFC acts consistently with the mandates of the Iowa legislature.[29] It is important that the legislature relinquished political control over the IAFC for numerous reasons. When a capital fund is controlled by political bodies, there may be political pres-

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23. *See* IOWA AGRIC. FIN. CORP., ARTICLES OF INCORPORATION (1998), *available at* http://www.sos.state.ia.us/CorpImages/VolumeW180K/W00184909.tif. [hereinafter IAFC: ARTICLES].

24. S*ee* Letter from Melanie Johnson, Legal Counsel, Iowa Department of Economic Development to Iowa Agricultural Finance Corporation (June 25, 1999) (on file with author).

25. *See* Smith, *supra* note 20, at 26 (stating "the law did not create the corporation itself"); *see also* IOWA CODE § 15E.204.3 (2003) ("an Iowa agricultural industry finance corporation is a private business corporation and not a public corporation or instrumentality of the state").

26. Smith, *supra* note 20, at 26.

27. IOWA CONST. art. VII, § 1; *see also* Iowa Code § 3.14 (2003); IOWA AGRIC. FIN. CORP., 2002 ANN. REP.: TAKING RISKS FOR IOWA'S SUCCESS 4 (2002).

28. IOWA AGRIC. FIN. CORP., 2002 ANN. REP.: TAKING RISKS FOR IOWA'S SUCCESS 4 (2002) [hereinafter IAFC: 2002 ANN. REP.].

29. Smith, *supra* note 20, at 26.

sures to make investments in particular communities or specific entities.[30] If legislative bodies pressure fund managers to place capital in particular areas or entities, it is probable that the fund will not have the desired effect of stimulating economic growth. Further, when venture capital funds are controlled by governmental agencies, it is difficult to attract talented fund managers to the program.[31] It becomes particularly essential for venture capital funds to have talented managers, when one of the objectives is to leverage the public money with private dollars, which the IAFC intended to do from early on.

C. *IAFC Picks a Partner*

In 1999, just a little over a year after the IAFC came into existence, the board of directors of IAFC partnered with Cybus Capital Advisors, L.L.C. ("Cybus") to form a limited partnership; this created the tecTERRA Food Capital Fund I, L.P. ("tecTERRA").[32] Both Cybus and IAFC are co-general partners of the tecTERRA fund.[33] The partnership makes investments in qualified value-added ventures through equity investments or debt securities in furtherance of the Act.[34]

IAFC chose to partner with Cybus for several reasons. At least one of the purposes of the partnership was to satisfy provisions of the Act requiring that IAFC investments be diverse.[35] By partnering with Cybus, a national investment banker specializing in agricultural investments, IAFC was able to take advantage of an already established network and staff of individuals experienced in capital placement.[36]

Additionally, by partnering with Cybus, it was possible for the IAFC to leverage the $25 million state loan with private funds and thereby create a capital pool of approximately $43 million.[37] Further, the directors of the IAFC felt that it was important to find a partner with a strong Iowa presence.[38] Cybus, with its principal office located in Des Moines, appeared to be the perfect fit.

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30. *See* David L. Barkley & Deborah M. Markley, *Nontraditional Sources of Venture Capital for Rural America*, RURAL AM., May 2001, at 19, 24.

31. *Id.*

32. *See* TECTERRA FOOD CAPITAL FUND I, L.P., AGREEMENT OF LIMITED PARTNERSHIP OF THE TECTERRA FOOD CAPITAL FUND I, L.P. 6 (1999).

33. *Id.* at 4.

34. See *id.* at 7.

35. *See* Letter from Melanie Johnson to Iowa Agricultural Finance Corporation, *supra* note 24.

36. *See* TECTERRA FOOD CAPITAL FUND, IOWA AGRICULTURAL FINANCE CORPORATION, IAFC UPDATE: FAYETTE PUBLIC FORUM 3 (Dec. 1, 1999).

37. *See* IAFC: 2001 ANN. REP., *supra* note 9, at 20.

38. *See id.* at 5.

Although Cybus Capital Advisors, L.L.C. was only created in 1999, Cybus Capital Markets, the parent company, has been active for several years. Cybus is a private investment banking company that assists agricultural related companies in obtaining growth capital.[39] Cybus has placed over $2 billion in agricultural related entities since 1999.[40] Notably, however, Cybus had never actually managed a venture fund; they had only been responsible for placing investments.[41]

Each of the co-general partners, Cybus and IAFC, was assigned specific duties under the partnership agreement. Cybus was required to contribute $120,000 to the partnership.[42] IAFC was required to contribute $55,000 to the partnership.[43] Regarding the remaining twenty-five million dollar loan, tecTERRA had the power to make capital calls as opportunities developed and it became time to place the capital in qualifying value-added or biotechnology ventures.[44] Until a capital call was issued, however, IAFC would retain any portion of the loan not already under call, the main portion of which the IAFC has invested in interest-bearing securities.[45]

Cybus Capital Advisors, L.L.C. acts as the manager of the tecTERRA fund,[46] and has the sole power to formulate, direct and recommend investment strategies.[47] However, because investment decisions must be approved by all of the general partners to the fund, IAFC gets to accept or reject any deal that it deems consistent or inconsistent with the Act.[48] IAFC's ability to reject deals is important to the manner in which tecTERRA was formed, because IAFC is the sole entity charged with satisfying the conditions of the Act.[49] Cybus, as a private entity – under no contractual relationship with the Iowa Department of Economic Development – has no responsibility to assure compliance with the Act.[50]

After the partnership was formed, tecTERRA began soliciting funds from the private sector of the economy to create a larger base of capital to invest

39. *See id.*; *see also* CYBUS CAPITAL, WHO WE ARE, *at* http://www.cybus.com/What_is_Cybus_Capital/body_what_is_cybus_capital.html (last visited July 28, 2004).
40. TECTERRA FOOD CAPITAL FUND, *supra* note 36, at 3.
41. *See* IOWA AGRIC. FIN. CORP., ANSWERS TO FINANCE COMMITTEE INQUIRY 6 (2000).
42. TECTERRA FOOD CAPITAL FUND I, L.P., *supra* note 32, at 9.
43. *Id*.
44. *Id.* at 11.
45. *Id.*
46. *Id.* at 4.
47. *Id.* at 15.
48. *Id.*
49. *See id.*
50. *See id.*

into qualified companies, thereby leveraging the $25 million state loan.[51] Initially, IAFC wanted to utilize private institutional investors to a much greater extent than has actually materialized. It was the hope of the IAFC to partner with institutional investors and create a pool of approximately one-hundred million dollars in both debt and equity which could be invested in qualifying ventures.[52] The IAFC envisioned a one-hundred million dollar "self sustaining investment fund, able to meaningfully aid Iowa's value-added economy with both capital and management expertise."[53] Although the IAFC ultimately fell short of the desired one-hundred million dollar capital pool, the total amount of capital available to tecTERRA at the end of 2002 was forty-three million dollars.[54] Twenty-five million of the forty-three million dollar total capital pool comes from the loan that the state of Iowa provided.[55] Approximately eighteen million dollars under tecTERRA management comes from private entities, including Pioneer Hi-Bred, DuPont, West Central Coop, Iowa Farm Bureau, and Archer Daniels Midland.[56] Although forty-three million dollars was the approximation of capital available, the total amount invested by tecTERRA as of June 30, 2003, was only $38.5 million.[57]

Institutional investors serve a larger purpose than merely leveraging the fund: "tecTERRA is structured so that [these] private institutional investors provide a guaranteed quarterly payment to IAFC sufficient to service repayment of the IDED loan."[58] The ability to begin repayment of the loan will become critical in 2004, when IAFC becomes obligated to begin making $1 million yearly repayments on the loan.[59] The tecTERRA partnership agreement allows for these private institutional investors to become Class A limited partners.[60] Specifically,

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51. *See* Alan Guebert, *Members to Farm Bureau*: *Show Us the Money*, THE FARM AND FOOD FILE, Apr. 16, 2000, *available at* http://www.defenders.org/fb/showusmoney.html.

52. IOWA AGRIC. FIN. CORP., 1999 ANN. REP. 3 (1999) [hereinafter IAFC: 1999 ANN. REP.].

53. *Id.*

54. IAFC: 2002 ANN. REP., *supra* note 28, at 7.

55. *Id.*

56. *See* Guebert, *supra* note 51 (stating that Pioneer Hi-Bred, DuPont, and West Central Coop contributed $1 million each; Farm Bureau contributed $5 million; Farm Bureau Mutual Insurance contributed $1 million; and Archer Daniels Midland contributed an undisclosed amount of money).

57. IOWA AGRIC. FIN. CORP., 2003 ANN. REP.: PERSISTENCE PAYS OFF 8 (2003) [hereinafter IAFC: 2003 Ann. Rep.].

58. IOWA AGRIC. FIN. CORP., FISCAL COMMITTEE PRESENTATION: 2000 IAFC ACCOMPLISHMENTS, INVOLVING IOWA PRODUCERS IN FOOD, FIBER AND BIOTECHNOLOGY 9 (2000) [hereinafter IAFC: 2000 FISCAL COMM. PRESENTATION].

59. *See generally* IOWA CODE § 15E.208.3.b (2003) (stating that repayment of the loan begins 6 years after all disbursements are made).

60. *See* TECTERRA FOOD CAPITAL FUND I, L.P., *supra* note 32, at 10.

there are 300 Class A Limited Partnership Units available to private investors, each unit costing $100,000, and a minimum purchase requirement of five units, which can be waived at the sole discretion of Cybus.[61]

Cybus, as the fund manager, is entitled to a 2.25% management fee during the commitment period.[62] The annual minimum management fee paid to Cybus to manage the tecTERRA fund is $750,000.[63] At the expiration of the commitment period, June 4, 2004 or when all commitments have been called, the management fee for the fund will drop to 1.75%.

To better understand the impact of the structure of the tecTERRA fund, one must look down the road to see what happens at the point tecTERRA cashes out of their investments. tecTERRA is a limited partnership with a limited duration of ten years.[64] Although the duration of the partnership can be extended by a majority in interest vote of the general partners for one year periods, the extensions shall not exceed a maximum of three additional years in aggregate.[65] Thus, absent some extraordinary event or agreement between the partners, tecTERRA will dissolve at the earliest in 2009, and at the latest in 2012.[66] Upon dissolution, the assets of tecTERRA will be used first to satisfy any outstanding liabilities to creditors (excluding any loans the IAFC might make to tecTERRA); next to establish a reserve for any potential future liabilities; third to repay any outstanding loans to any partner; and finally, any amount left is then distributed to the partners in accordance with their capital account balance.[67]

At this point, the IAFC will remain in existence, and will continue to pay down the twenty-five million dollar loan balance to the state of Iowa. It is also within the realm of possibility that IAFC would partner with Cybus, or a similar entity again, and create a second fund.[68] It is hoped that the ventures into which IAFC made investments will be stable enough at this point to contribute to repayment of the loan, or continue to purchase equity units in IAFC as the case may be. The technical process is complicated, and will vary from venture to venture based upon the manner which the initial deal was structured. In the end the IAFC is left with nothing, as all of its interests are transferred to agricultural producers and biotechnology entities that received proceeds of the state loan. At the

61. *Id.*
62. TECTERRA FOOD CAPITAL FUND I, L.P., *supra* note 32, at 25.
63. *Id.*
64. *Id.* at 7; *see also* IAFC: 2000 FISCAL COMM. PRESENTATION, *supra* note 58, at 2.
65. TECTERRA FOOD CAPITAL FUND I, L.P., *supra* note 32, at 7.
66. *Id.* at 1.
67. *Id.* at 43.
68. IAFC: 1999 ANN. REP., *supra* note 52, at 3 (talking about desire to leverage initial $25 million and create a $100 million self sustaining investment fund); *see also* IAFC: 2001 ANN. REP., *supra* note 9, at 7.

end of the twenty-five year repayment period, IAFC would be dissolved, and the value-added entities would be left holding one hundred percent of the stock in the ventures they had created to the extent of the twenty-five million dollar loan. The institutional investors will continue to hold an equity interest in the ventures, reflective of their eighteen million dollar contribution to the tecTERRA Fund I.

D. *What Value-Added Means for the Iowa Economy*

The underlying purpose behind the loan from the State of Iowa to the IAFC was to generate investments in valued-added companies that will produce value not only at the level of creating or growing agricultural products, but also to allow producers to participate in downstream value.[69] In fact, the impetus for the original legislation was to provide a group of Iowa businessmen with the ability to construct a meat packing plant near Des Moines.[70] At the time, there were only a handful of meat processors in the state of Iowa, and agricultural producers had little choice on where to take their animals to market.[71] Agricultural producers would have to set up a date to take their cattle to market weeks in advance, and were quoted market rates for that day on how much profit they would generate per pound.[72] Meanwhile, the market would fluctuate and in many cases, the farmers would have been able to realize a greater profit if they did not have to schedule taking cattle to market weeks in advance.[73]

The benefits to be derived from the legislation can be broken down into two broad categories; indirect benefits to agricultural producers and residents of Iowa, and direct benefits to agricultural producers and networks who participate in the ventures created.[74] The indirect benefit of the legislation is more far reaching, having a greater effect on agricultural producers, and residents of Iowa, as a whole.[75] Indirect benefits include the creation of jobs in Iowa, an increase in tax revenues to municipalities where ventures are located, and improved local markets leading to higher commodity prices.[76] Another indirect benefit to be derived from the legislation is the retention of wealth in Iowa.[77] Simply, when Iowa agricultural producers have to send raw commodities to other states for processing,

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69. *See* Smith, *supra* note 20, at 26.
70. *See* IOWA AGRI. FIN. CORP., *supra* note 41, at 8.
71. Interview with Geri Huser, Iowa State Representative for the 66th District, in Des Moines, Iowa (Sept. 25, 2002).
72. *Id.*
73. *Id.*
74. IAFC: 1999 ANN. REP., *supra* note 52, at 5.
75. *Id*.
76. *Id.*
77. *Id*.

Iowa is loosing any revenues associated with processing or production. By enabling the creation of processing facilities, the legislation also enables the retention of wealth.

The legislation also contemplates direct benefits to Iowa agricultural producers. Simply, the agricultural producers (e.g., farmers and networks) who help create a value-added venture should share in the ownership of the venture.[78] In fact, such ownership was more than contemplated by the legislation, it was actually required.[79] "Agricultural producers must hold at least fifty-one percent of the corporation's common stock and at least fifty-one percent of the corporation's voting stock."[80] This producer ownership idea is an essential element of the legislation, because the legislature intended for the small farmer to derive the bulk of benefits from the twenty-five million dollar interest free loan, not agribusiness.[81] "The ultimate shareholders of IAFC are agricultural producers who participate in IAFC investments."[82]

III. SOURCES OF FUNDING TO SUPPORT VALUE-ADDED INDUSTRY

A. *Traditional Sources of Capital*

Traditionally, there have been a number of means through which a company can finance either start-up or expansions of their agricultural business. For example, there has always been an ability to receive financing from banks in a traditional loan situation, which, in the end, will transfer all ownership of the business to the owner; the bank will not retain any equity. This, of course, requires the borrower to pay high interest rates, and would also not be the most viable option for higher risk ventures.

Venture capital, on the other hand, allows for a company to receive funding that does not have to be repaid like a traditional loan, but instead transfers equity in the company to private investors. Venture capital has been called "the rocket fuel of America's entrepreneurial engine."[83] While venture capital has been a traditional source of funding for businesses, either at the start-up or mezzanine level, venture capital has not been a wide source of funding in the agricul-

78. *Id.* at 1, 5 (stating that one of IAFC's primary goals is to assist agricultural producers obtain equity interests in IAFC value-added ventures).

79. IOWA CODE § 15E.205(1)(a) (2003).

80. *Id.* § 15E.205(1)(a).

81. *Id.* § 15E.203(2).

82. IAFC: 2000 FISCAL COMM. PRESENTATION, *supra* note 58, at 2.

83. JEFFREY A. TIMMONS, NEW VENTURE CREATION: ENTREPRENEURSHIP FOR THE 21ST CENTURY 9 (5th ed. 1999).

tural sector.[84] In fact, in the year 2000, ninety-one percent of venture capital investments were in technology and internet related companies, according to one national survey.[85]

One question that arises when looking at the tecTERRA fund is trying to classify exactly where it falls in the spectrum of investment capital. While it is clear from the legislation that the Iowa legislature did not intend to create a venture capital fund, but instead offer repayable loans to Iowa business, it is not so clear that tecTERRA, or at least the Cybus half of tecTERRA partnership, would not classify as an investment in companies as venture capital. While IAFC will not ultimately hold any portion of ownership in the ventures tecTERRA invests in, upon dissolution of the partnership, Cybus, and the other limited partners, will retain equity in the companies that tecTERRA has invested in.

B. *Non-Traditional Sources of Capital*

Generally speaking, three types of non-traditional sources of capital have come about during the 1990s and succeeding years. The three types of non-traditional capital sources can be broken down into three separate categories: Publicly funded, publicly managed programs; publicly funded, privately managed programs; and community level equity funds.[86] The IAFC most closely resembles the second type.

IV. COMPANIES CREATED UNDER THE TECTERRA FUND

A. *How to Qualify to Receive Money from the Fund*

The tecTERRA Food Capital Fund does not make investments into just any value-added entity; as with any other venture capital source, they have strict requirements on what types of companies they are willing to invest in.[87] Specifically, and consistent with legislative intent, the venture that receives money from the fund must involve the acquisition, construction, or expansion of a facility in the State of Iowa that processes agricultural commodities, the majority of which are produced in Iowa.[88] In giving a $25 million loan to the value-added sector, the legislature wanted to ensure that the entity receiving funding would generate expected benefits for Iowa.[89] In addition to value-added products, the fund is

84. *See* Barkley & Markley, *supra* note 30, at 19.
85. *Id.*
86. *Id.* at 21-25.
87. *See* IOWA CODE § 15E.208 (2003).
88. IAFC: 2001 ANN. REP., *supra* note 9, at 20.
89. *See* IOWA CODE § 15E.203 (2003).

also permitted to invest in biotechnology ventures that involve the use of plant or animal genetics and is an Iowa entity, with operations located in Iowa.[90]

The Act also directs the IAFC – through mandates in the legislation – to exercise diligence and care in the selection of projects that it invests in.[91] The IAFC must exercise "customary and acceptable business and lending standards and practices in selecting persons and projects designated for financing."[92]

Beyond the aforementioned requirements of the Act, tecTERRA has established several guidelines of their own. tecTERRA seeks to invest in companies that are already in the value-added industry; simply put, they do not want to invest in start-up companies with no proven track record.[93] As tecTERRA discovered, it can be difficult to find agricultural related companies that are *willing* to share control with outside investors.[94]

The ideal investment for tecTERRA capital is in companies that are "primarily mid to later stage, privately owned companies ready for growth."[95] Because start up companies have high risk associated with them, and do not have proven track records, it would be somewhat imprudent for tecTERRA to invest in start-ups, which they tend to shy away from.[96] Not only does tecTERRA have to act prudently so that IAFC will be able to repay the loan to the State of Iowa, it also has fiduciary obligations to act wisely on behalf of private equity investors in the fund.[97]

B. *Entities that Have Received Money from the Fund*

To date, the tecTERRA fund has invested with five different companies, and the IAFC has acted independently in one additional venture.[98] It is important to draw a distinction at this point between investments made by tecTERRA, and

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90. IAFC: 2001 Ann. Rep., *supra* note 9, at 20.

91. IOWA CODE § 15E.207.1 (2003).

92. *See id.*

93. IAFC: 2001 ANN. REP., *supra* note 9, at 15 (stating that IAFC exercises "prudent business judgment to generate profits to repay the loan").

94. Clark Kauffman, *Investments Drain State Money*, DES MOINES REG., Apr. 27, 2003, at 4A.

95. tecTERRA Food Capital Fund, *supra* note 36, at 4.

96. *See id.* at 5 (stating that because IAFC has an obligation to repay the loan to the State of Iowa, the risk that tecTERRA can undertake in startup companies is very limited).

97. *See* IAFC: 2001 ANN. REP., *supra* note 9, at 18 (2001) (stating that tecTERRA also has an obligation to return market rates of return to equity investors); *see also* IOWA AGRIC. FIN. CORP., *supra* note 41, at 4 (stating that targeted rate of return for outside investors is 23%).

98. *See* IAFC: 2003 ANN. REP., *supra* note 57, at 9.

investments made *directly* by IAFC.[99] For each investment made by tecTERRA, IAFC has consistently provided fifty-eight percent of the total funding, with institutional investors being responsible for the remaining forty-two percent of monies invested.[100] For this, IAFC receives class B limited partnership shares from tecTERRA, in proportion to the fifty-eight percent contributed.[101] In some situations, noted where appropriate, IAFC has contributed additional funding, separate and independent, of the tecTERRA contribution. This is what is referred to as a direct investment by IAFC. Sometimes the direct investment is in the form of a loan or a convertible debenture, other times it may be reflected by way of equity.[102] In any situation, where IAFC makes a direct investment, they are shouldering one-hundred percent of the load, independent of the investment made by tecTERRA.[103]

The first entity that tecTERRA has contributed capital to is Sioux-Preme Packing Company, located in Sioux Center, Iowa.[104] In September 2000 tecTERRA made a $5 million investment into the company, which is a pork slaughter and fabrication company.[105] Sioux-Preme has established a network where producers grow hogs for niche groups.[106] There is a demand for niche hogs, including hogs that are raised without antibiotics, or are not kept in farrowing crates.[107] In investing in Sioux-Preme, tecTERRA mandated that at least fifty percent of the hogs processed at Sioux-Preme come from Iowa. Initially, there was not an adequate supply of niche hog producers in Iowa, and Sioux-Preme instead processed commodity hogs.[108] This lack of niche hogs has subsided in recent years however, particularly because Sioux-Preme is now a contract processor for the Niman Ranch brand of natural pork.[109] As a result of IAFC's involvement, select Iowa niche pork producers were able to collectively acquire a

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99. *See, e.g., id.* at 24 (stating that tecTERRA has invested $7,008,532 in Rudi's Bakery and that IAFC has directly invested $1,700,000 as a co-investor).

100. Kauffman, *supra* note 94, at 4A.

101. TECTERRA FOOD CAPITAL FUND, *supra* note 32, at 9.

102. *See* IOWA AGRIC. FIN. CORP., 2002 ANN. REP. FIN. STATEMENT 9 (2002) (showing that IAFC provided two loans to Wildwood Harvest, the first one which was converted to equity by Wildwood and the second one, with the option to convert, which was currently a loan) [hereinafter IAFC: 2002 FIN. STATEMENT].

103. *See id.*

104. *Id.*

105. *Id.*

106. Rod Smith, *Sioux-Preme Gives Means to Share in Value Creation*, FEEDSTUFFS, June 3, 2002, at 1.

107. *See id.* at 22.

108. IAFC: 2001 ANN. REP., *supra* note 9, at 25.

109. IAFC: 2003 ANN. REP., *supra* note 57, at 28.

six-percent interest in Sioux-Preme common stock.[110] Unlike other IAFC projects, Sioux-Preme has not needed additional injections of capital.[111] Sioux-Preme is rightfully regarded as one of IAFC's success stories, providing a market for niche hog farmers, as well as the direct benefit of ownership interest in the business to select Iowa pork producers.[112]

The second company which IAFC has invested in, both directly and through the tecTERRA fund, is Stauffer Life Sciences, Inc. ("Stauffer"). tecTERRA made an initial investment of three million dollars in Stauffer, the IAFC's representation being $1,744,186, in March 2001.[113] Subsequently, the tecTERRA capital was transferred to ProdiGene Iowa, Inc., a wholly owned subsidiary of ProdiGene, Inc.[114] ProdiGene is not a value-added venture, but instead falls under the second prong of the Act, in that it is a biotechnology venture.[115] ProdiGene is a company "involved in the commercialization of genetically modified corn as a source for hard-to-produce proteins in high-value markets such as human and veterinary medicines, industrial enzymes and alternative fuels."[116] The benefits expected from biotechnology recipients are similar to the expected benefits from value-added agricultural producers. It was initially expected that ProdiGene would produce jobs in Iowa, increase the tax base, and additionally allow for Iowa agricultural producers to participate in the production of seed corn.[117]

As can be expected with a growing business, ProdiGene required additional capital contributions subsequent to receiving the initial three million dollars. One of the problems that was quickly unearthed was that there was not an agreement in place which *required* ProdiGene to grow corn in Iowa, but instead only utilize commercially reasonable efforts in doing so.[118] Although it is unclear

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110. *Id.*

111. *See id.*

112. *See id.*; *see also* Jerry Perkins, *State Ag Fund Director Defends Record*, DES MOINES REG., Feb. 27, 2004, at 6D.

113. *Id.*

114. IAFC: 2002 ANN. REP., *supra* note 28, at 31.

115. *See* IOWA CODE § 15E.202.7 (2003) (defining a biotechnology enterprise as an enterprise "organized under the laws of this state using biological techniques for the development of specialized plant or animal characteristics for beneficial nutritional, commercial, or industrial purposes").

116. IAFC: 2001 ANN. REP., *supra* note 9, at 27.

117. *Id.*

118. Kauffman, *supra* note 94, at 4A (stating that after initial $3,000,000 investment, ProdiGene was growing corn in Illinois, Nebraska, Minnesota, and Texas, but not Iowa); *see also* IAFC: 2001 ANN. REP., *supra* note 9, at 27 (stating that Stauffer "is required to use *commercially reasonable efforts* to involve Iowa agricultural producers in the production of parent seed corn") (emphasis added).

when it occurred, and different documents reflect different figures, tecTERRA contributed an additional $2.25 million to ProdiGene between December 31, 2001, and June 24, 2002.[119] With the $2.25 million additional contribution, tecTERRA required ProdiGene to commit to grow at least twenty-five percent of its corn in Iowa through 2010, subject to regulatory approval.[120] On June 24, 2002, tecTERRA contributed an additional $750,000 to ProdiGene, and there was an additional $750,000 conditionally committed to ProdiGene.[121] Shortly thereafter, ProdiGene suffered another major setback, when a soybean crop in Nebraska became contaminated with genetically engineered corn, grown by ProdiGene, potentially running afoul of the Plant Protection Act.[122] Although ProdiGene did not admit culpability, it agreed to pay $250,000 and pay for the cost of the destruction of the contaminated soybeans, estimated at three million dollars.[123] Subsequent regulatory actions made it very difficult for ProdiGene to grow genetically modified corn in Iowa.

All in all, tecTERRA had invested upwards of $6 million in ProdiGene, with approximately $4.2 million attributed to IAFC's portion.[124] ProdiGene was certainly one of the more controversial of IAFC's investments, largely because it lacked strong ties to Iowa and did not produce either direct or indirect benefits for Iowans as expected.[125] A majority of ProdiGene's equity was purchased by an affiliate of Stine Seeds, International Oilseeds Distributors, based in Adel, Iowa.[126] IAFC has described itself as the "marriage broker" between ProdiGene and Stine Seeds, apparently bringing the two parties together.[127] tecTERRA remains a minority shareholder in ProdiGene.[128]

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119. *Compare* IAFC: 2002 ANN. REP., *supra* note 28, at 31 (stating that tecTERRA completed a $750,000 investment on June 24, 2002, and that "tecTERRA had previously invested $5.25 million in ProdiGene affiliate, Stauffer Life Sciences"); *with* IOWA AGRIC. FIN. CORP., 2001 ANN. REP. ADDENDUM: VENTURE CAPITAL FOR GROWING IOWA (stating that after December 31, 2001, but prior to June 24, 2002, "tecTERRA had previously invested $3,000,000 in a ProdiGene affiliate, Stauffer Life Sciences") [hereinafter IAFC: 2001 ANN. REP. ADDENDUM].

120. Kauffman, *supra* note 94, at 4A.

121. IAFC: 2002 ANN. REP., *supra* note 28, at 31.

122. Kauffman, *supra* note 94, at 4A; Press Release, USDA, USDA Announces Actions Regarding Plant Protection Act Violations Involving ProdiGene, Inc. (Dec. 6, 2002), *available at* http://www.usda.gov/news/releases/2002/12/0498.htm; Philip Brasher, *ProdiGene Must Pay $3 Million in Corn Case,* DES MOINES REG., Dec. 7, 2002, at 1A.

123. Press Release, USDA, *supra* note 122.

124. IAFC: 2003 ANN. REP., *supra* note 57 at 26; Kauffman, *supra* note 95, at 4A.

125. Bert Dalmer, *Lawmakers Question Ag Fund's Job Record*, DES MOINES REG., Oct. 3, 2004, at 12A; Clark Kauffman, *Investors Set to Buy Firm Aided by State*, DES MOINES REG., June 6, 2003; Kauffman, *supra* note 95, at 1A,4A.

126. IAFC: 2003 ANN. REP., *supra* note 58, at 26.

127. Perkins, *supra* note 112, at 6D.

128. IAFC: 2003 ANN. REP., *supra* note 57, at 26.

The third project that the tecTERRA fund has invested in is Wildwood Harvest, Inc. ("Wildwood"). Wildwood is the product of a merger between Iowa-based Midwest Harvest Corporation and California-based Wildwood Natural Foods, Inc.[129] Tom Lacina founded Midwest Harvest in 1998 and grew organic soybeans and produced tofu, but was unsure of how to enter the national market.[130] Wildwood Natural Foods was a broader-line, established soyfoods producer, looking for a Midwest organic soybean producer.[131] Wildwood is currently positioned to continue growth in the "growing dairy analog business, offering soymilk, tofu, and other organic soy products."[132]

Initially, tecTERRA provided $1.795 million to Wildwood; the IAFC's portion of that figure, $1,043,605, much needed capital for the merged Wildwood, enabled it to build a new production facility in Grinnell, Iowa.[133] A simultaneous commitment was made in September 2001 by IAFC to Wildwood of $1.5 million in loans, convertible to preferred stock, at Wildwood's option.[134] The amount committed was actually loaned to Wildwood in two separate transactions, one million dollars in November 2001, and the additional five-hundred thousand dollars loaned in January 2002.[135] The one million dollar loan was converted to preferred stock by Wildwood in June 2002, and the five-hundred thousand dollar loan was converted in October 2002.[136] IAFC purchased an additional 805,000 shares of preferred stock between June 30, 2002, and June 30, 2003, for $805,000.[137] Thus, IAFC *directly* invested in Wildwood for $2,305,000 (fourteen percent) and tecTERRA invested $5.1 million in Wildwood (fifty-one percent).[138] As of June 30, 2003, the $2,305,000 worth of preferred stock that IAFC held directly in Wildwood had a value of $230,500, as valued by IAFC.[139] When considering the drastic difference between the figures, it is important to keep in mind that there is not a ready market to transfer the securities on, which is reflected by the low valuation.[140]

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129. *Id.* at 29.

130. Rod Smith, *Wildwood Offers Producers Examples of Opportunities for Adding Value, Diversifying,* FEEDSTUFFS, June 3, 2002, at 1.

131. *Id.* at 30.

132. IAFC: 2003 ANN. REP., *supra* note 57, at 30.

133. *Id.*; *see also* IAFC: 2001 ANN. REP., *supra* note 9, at 29.

134. IAFC: 2001 ANN. REP., *supra* note 9, at 29; IAFC: 2002 FIN. STATEMENT, *supra* note 102, at 9.

135. IAFC: 2001 ANN. REP., *supra* note 9, at 29.

136. IOWA AGRIC. FIN. CORP., 2003 ANN. REP. FIN. STATEMENT 9-10 (2003) [hereinafter IAFC: 2003 FIN. STATEMENT].

137. *Id.*

138. *Id.* at 10; IAFC: 2003 ANN. REP., *supra* note 57, at 29.

139. IAFC: 2003 FIN. STATEMENT, *supra* note 136, at 7.

140. *Id.*

Wildwood benefits Iowans in several ways, both directly and indirectly. First, tecTERRA requires Wildwood to use at least fifty percent Iowa soybeans in their value-added industry.[141] It is anticipated that Wildwood will "indirectly benefit all Iowa soybean producers by stimulating increased demand and new markets for food-grade soybeans."[142] The partnership will also enable what was formerly Midwest Harvest to reach into the West Coast health food market, an opportunity it would not likely have had absent tecTERRA's and IAFC's involvement.[143] In addition to the use of Iowa soybeans and increased marketing opportunities, tecTERRA anticipates the creation of new jobs in Iowa, as well as an increase in the tax base.[144]

The IAFC attributed a large portion of a $1.7 million loss in 2003 to Wildwood Harvest.[145] Although Wildwood is not considered as successful as Sioux-Preme Packing, it is considered one of IAFC's success stories.[146] The bottom line is that Wildwood is still active and is well positioned in the dairy analog business, and shows potential in the rapidly growing industry.[147] Finally, recall one of the main goals of the Iowa legislature was to enable Iowa agricultural producers to own a stake in the business that IAFC assisted in establishing.[148] Wildwood is now partially owned by agricultural producers who founded Midwest Harvest and the possibility likely exists in the future for other Iowa agricultural producers to become owners.[149]

One project that has plagued IAFC with controversy and bad publicity is Rudi's Bakery, Inc. ("Rudi's"), one of the United States leading producers of organic bread, headquartered in Boulder, Colorado.[150] Rudi's received an initial investment of $2.2 million from the tecTERRA fund in February 2000[151] and an additional investment of $2.8 million in late 2000, IAFC's share of the total $5 million investment being $2,906,977.[152] In addition, IAFC purchased 275,175 shares of convertible voting stock in Rudi's directly for $275,175.[153] The funds were used to build a thirty-five thousand square foot baking plant in North Lib-

141. IAFC: 2001 ANN. REP., *supra* note 9, at 29.
142. IAFC: 2003 ANN. REP., *supra* note 57, at 30.
143. *Id.*
144. *Id.*
145. Perkins, *supra* note 112, at 1D.
146. Dalmer, *supra* note 125, at 12A.
147. IAFC: 2003 ANN. REP., *supra* note 57, at 30.
148. *Id.* at 29.
149. *See Id.* at 30.
150. Rod Smith, *Rudi's Bakery Represents Other Part of Venture Capital 'Life'*, FEEDSTUFFS, June 3, 2002, at 21.
151. IAFC: 2000 FISCAL COMM. PRESENTATION, *supra* note 58, at 6.
152. IAFC: 2001 ANN. REP., *supra* note 9, at 23.
153. *Id.* at 44, note 4.

erty, Iowa.[154] Rudi's began actually producing bread in August 2001.[155] It was anticipated that Rudi's would employ one hundred people at above-average wages in order to produce organic bread.[156] A hiccup developed early on, however, after it was discovered that the wheat needed for organic processing is not the same type of wheat grown in Iowa, nor could it be, because of climatic differences.[157] Rudi's CEO Mark Retzloff stated in April 2003 that the mistake was not a unilateral one; both Rudi's officials and IAFC officials failed to "recognize that Rudi's needed hard, red winter wheat, which is not grown in Iowa."[158] Rudi's Bakery shut down, just six months after opening, in February 2002.[159] For the majority of 2002, the multi-million dollar, thirty-five thousand square foot facility that was to employ one-hundred workers at above average wages, was used as a warehouse and employed three people.[160]

IAFC attributed the shut down of Rudi's to lower-than-expected sales, but also noted that the "[s]uccess [of Rudi's] depends upon securing alternative or additional uses for the North Liberty facility."[161] By early 2003, tecTERRA had pumped or committed approximately $4.7 million of *additional* capital into Rudi's, and IAFC had directly provided an *additional* $1.5 million in bridge financing, not ready to cut the floundering Rudi's loose.[162] Five hundred thousand dollars of that $1.5 million loan was converted to equity in Rudi's Bakery in May 2003, while seven hundred thousand more dollars of it was converted to a royalty agreement.[163] Rudi's never did resume operations in Iowa.[164] Most of the plant's baking equipment was shipped to Boulder, Colorado, after the North Liberty, Iowa, plant closed.[165]

In June 2003, Iowa Farm Bureau committed up to four million dollars in equity financing to Rudi's to help the company with cash flow problems,[166] acquiring a majority stake in ownership.[167] The building in North Liberty was set to be sold to The Molina Vector Investment Trust ("REIT"), with closing scheduled

154. IAFC: 2002 ANN. REP., *supra* note 28, at 19.
155. *Id.*
156. IAFC: 2001 ANN. REP., *supra* note 9, at 25.
157. *Id.* at 24.
158. Kauffman, *supra* note 94, at 4A.
159. IAFC: 2002 ANN. REP.., *supra* note 28, at 19.
160. *See* Patt Johnson, *Iowa Bakery to Shut off Production,* DES MOINES REG., Feb. 14, 2002, at D1.
161. IAFC: 2002 ANN. REP., *supra* note 28, at 20.
162. *See id.* at 28.
163. IAFC: 2003 FIN. STATEMENT, *supra* note 136, at 9, note 4.
164. *See* IAFC: 2003 ANN. REP., *supra* note 57, at 24.
165. Kauffman, *supra* note 125.
166. *Id.*
167. IAFC: 2003 ANN. REP., *supra* note 57, at 24.

for June 30, 2004.[168] The trust had intended on leasing the space to a new venture, Dare Devil Shells, which manufactures pizza crusts.[169] As of September 1, 2004, REIT had failed to close on the transaction, and IAFC vowed to "pursue all business and legal remedies to either close the sale or resell the property and collect damages."[170] Dare Devil is expected to deliver several of the indirect benefits to Iowans that Rudi's would have,[171] including one hundred jobs.[172] Notably, however, Dare Devil will not be linked to Iowa growers or producer networks, which would result in the direct benefit of Iowan ownership as required under the Act.

IAFC's most recent investment was in Ag Waste Recovery Systems ("AWRS").[173] The investment was made directly by IAFC, and was in the amount of $150,000.[174] The investment was made during the early stages of the business, and the principal purpose of the investment was to allow AWRS to bring new technology to market.[175] AWRS is a venture that processes swine manure, to "enhance both the economics of farming and reduce the negative environmental impacts of current swine production methodologies."[176] AWRS is expected to produce both direct and indirect benefits for Iowans, including the creation of jobs, preservation of existing jobs both on and off the farm in swine production, and potentially leading to wealth growth and retention in rural Iowa.[177]

Lastly, IAFC has had an ongoing relationship with Iowa Quality Beef Supply Network ("IQB") since 2000.[178] IQB was selected as a possible entity to receive funding because it would allow Iowa to retain cattle production, by providing marketing opportunities for farmers and a means to process raw commodities, animals.[179] In May 2001, IAFC entered into a loan commitment agreement with IQB, to directly loan IQB ten million dollars, upon IQB's compliance with certain prerequisites, namely, determining where to locate the proposed facility.[180] Suffice it to say that the commitment never came to fruition, although the

168. IOWA AGRIC. FIN. CORP., 2003 ANN. REP. ADDENDUM: PERSISTENCE PAYS OFF (2003) [hereinafter IAFC: 2003 ANN. REP. ADDENDUM].

169. *Id.*

170. *Id.*

171. *See supra*, section II., D.

172. IAFC: 2003 ANN. REP., *supra* note 57, at 24.

173. *Id.* at 31.

174. *Id.*

175. *Id.*

176. *Id.*

177. *Id.* at 32.

178. IAFC: 2000 FISCAL COMM. PRESENTATION, *supra* note 58, at 6.

179. *Id.*

180. *Id.*; *see also* IAFC: 2001 ANN. REP., *supra* note 9, at 32.

possibility of financing continued to exist.[181] In 2003, the General Assembly enacted legislation which would permit IAFC to make a direct secured loan to IQB, and such loan was then to be assigned to the IDED.[182] IAFC did indeed make the loan, and in exchange was relieved of their liability for the first three years of repayment of the loan.[183] Because the amendment provides that the assignment shall apply all amounts due under the loan, including principal, interest, and fees to which the IAFC would have been entitled, the transaction ends up canceling out $3,482,761 of the IAFC's twenty-five million dollar loan.[184] The first one million dollar installment was set to be due in October 2004.[185] Now, depending on the agreement that the IAFC and IDED hammer out, IAFC could end up making a $518,000 repayment in October 2007, and then begin making one million dollar repayments in October 2008.[186]

C. *Criticisim and Problems of the tecTERRA Arrangement*

The IAFC initially came under fire in 2000, by a surprising individual – Derryl McLaren – the past chairman of the Iowa Senate Appropriations Committee who supported the bill from the very beginning.[187] McLaren explains that the bill was intended as a loan to help small agricultural producers; yet, in McLaren's opinion, the only group that the money appears to be benefiting is a group of influential agribusiness investors.[188] McLaren has called the activities of tecTERRA a "near scandal."[189] In 2003, Representative Mark Kuhn, whom also initially supported the legislation, joined McLaren's camp of discontent Iowa Legislators, calling for an audit and an investigation into the IAFC.[190]

However, there are also several legislators who stand behind IAFC's track record. One of those supporters, Dwayne Alons, noted that venture capital

181. IAFC: 2001 ANN. REP., *supra* note 9, at 33 (stating that IAFC anticipates the need to extend the commitment period); IAFC: 2002 ANN. REP., *supra* note 28, at 36 (stating that IAFC is working on a financing package and possibly new commitment terms with IQB).

182. S.F. 459 (Iowa 2003).

183. IAFC: 2003 ANN. REP., *supra* note 57, at 33.

184. S.F. 459 (Iowa 2003); IAFC: 2003 FIN. STATEMENT, *supra* note 136, at 5.

185. IAFC: 2002 ANN. REP., *supra* note 28, at 3.

186. See S.F. 459 (Iowa 2003); *see also* Dalmer, *supra* note 125, at 12A.

187. *See* Guebert, *supra* note 51.

188. *Id.*; see also Kauffman, *supra* note 94, at 4A (stating that "[c]ritics say [the IAFC] is routing millions of public dollars out of Iowa and into the coffers of private companies that have yet to help Iowa's economy").

189. Randy Mudgett, *Legislators Critical of Loan Program*, FARM NEWS, Feb. 25, 2000, at 1.

190. Lynn Okamoto, *Legislators Rake Iowa Ag Fund*, DES MOINES REG., Mar. 28, 2003, at 2D; *see also* Dalmer, *supra* note 125, at 1A, 12A.

inherently involves some degree of risk, which the Iowa Legislature knew when creating the IAFC.[191] Representative Stewart Iverson agrees, noting that "[w]hen something goes South, to stand around and criticize is the easiest thing in the world to do."[192] Supporters of IAFC insist that the IAFC has attracted private investors to Iowa and forged partnerships between Iowa farmers and national companies.[193]

IAFC has steadfastly resisted any suggestion of impropriety. IAFC insists that since "[t]he state regularly makes loans to advance economic development, doing so to advance economic development through venture capital is no less appropriate."[194] Instead of merely looking at the manner in which the fund is structured, IAFC proposes that instead, individuals need to look further down the road at the potential economic incentives this fund has created for Iowa business.[195]

To at least some degree, the Iowa Legislature disagreed with IAFC's use of the twenty-five million dollar loan.[196] After IAFC partnered with Cybus to form tecTERRA, a subpoena was issued requiring IAFC to appear before the Iowa Fiscal Bureau.[197] The Fiscal Bureau wanted answers to whether the IAFC had complied with legislative intent.[198] At least some members of the Fiscal Bureau were not happy with the formation of tecTERRA pointing out that what the original twenty-five million dollar loan was intended to be used for, and how it was actually being used, were inconsistent with the Act.[199]

Some members of the Iowa legislature and IAFC are also at odds about what the legislature required of the IAFC in acting prudently and exercising diligence in selecting projects that were to receive funding.[200] IAFC insists that acting prudently means finding projects that have an estimated return on investment of twenty to twenty-five percent.[201] IAFC feels it is necessary not only to receive

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191. *See* Okamoto, *supra* note 190, at 2D.

192. Dalmer, *supra* note 125, at 12A.

193. Kauffman, *supra* note 94, at 4A..

194. Letter from Dan Winegarden, President, IAFC, to Kyle Jackson (Feb. 7, 2003) (on file with author).

195. *See generally id*.

196. *See* FISCAL COMMITTEE, IOWA LEGISLATIVE COUNCIL, FISCAL COMMITTEE MINUTES 5 (1999).

197. *See id.* at 7.

198. *See id.* at 5-6; *see also* IOWA AGRIC. FIN. CORP., *supra* note 41, at 1.

199. *See* FISCAL COMMITTEE, IOWA LEGISLATIVE COUNCIL, *supra* note 196, at 6 (stating when "Representative Shoultz asked Senator McLaren if the Legislature should take the money back, Senator McLaren responded, yes.")

200. *Compare* IOWA CODE § 15E.207 (2003), *with* IOWA AGRIC. FIN. CORP., *supra* note 41, at 2-3.

201. IOWA AGRIC. FIN. CORP., *supra* note 41, at 3.

such a rate of return to ensure the state loan will be repaid timely, but also to ensure that tecTERRA is able to provide an adequate rate of return to the private, institutional, Class A Limited Partners.[202]

Such a position however, is susceptible to criticism, because the Iowa Legislature made clear that any organization to incorporate under the Iowa Agricultural Finance Corporation Act was not to hold ownership in investments it made.[203] The intent of the legislature was to transfer ownership of the companies not to a group of corporate investors, but instead to the agricultural producers who helped build the company.[204] To the extent that tecTERRA and institutional investors will hold equity in ventures that the loan from the State of Iowa helped create, there are certainly grounds to support McLaren's allegations.

Some of the criticism of the IAFC may be unfounded. From inception of the legislation, it was known that one of the goals of the legislation was to leverage the fund.[205] Regarding the legislation, "[i]t is believed this initial $25 million will be leveraged into over $100 million through interest, selling stock, and attracting private investments."[206] Without the help of institutional investors, whom would necessarily require a return on their investment, how was the twenty-five million dollars to be leveraged? A further explanation might be that some of the criticism is politically motivated.[207] By and large, Republican members of the General Assembly have been much more receptive to giving the IAFC more time to determine how best to deal with problems, which Democratic leadership has not been eager to do.[208]

V. CONCLUSION

The IAFC has provided value-added agricultural producers a unique opportunity to compete in a once foreign market. Through the $25 million loan, the state has accomplished some of the primary goals of the legislation. It has enabled the creation or expansion of several value-added industries, that without the legislation, likely would not have been possible. At least two of the value-added ventures, Sioux-Preme Packing and Wildwood Harvest, appear to be reaching

202. IAFC: 2001 ANN. REP., *supra* note 9, at 18.
203. *See* IOWA CODE § 15E.207.2.
204. *See id.* § 15E.203.2; *see also* IAFC: ARTICLES, *supra* note 23, at 1 (stating that it is the intent of the IAFC to "develop and expand the [IAFC] so it is substantially owned by agricultural producers").
205. 1998 House Democratic Research Staff, End of Session Summary, at 94 (on file with author).
206. *Id.*
207. *See* Dalmer, *supra* note 125, at 12A; Okamoto, *supra* note 190, at 2D.
208. *See* Dalmer, *supra* note 125, at 12A; Okamoto, *supra* note 190, at 2D.

goals more promptly than originally anticipated and both have provided producer and network ownership opportunities. The failure of Rudi's Bakery is unfortunate, but with venture capital, such risks are inevitable. If you never try, you will never succeed.

The controversy surrounding the IAFC is unfortunate, but some of the controversy and resistance on the part of Iowa Legislature is well-founded. Both Cybus and institutional investors stand to profit handsomely from their relationship with IAFC. In addition, the agricultural producers whom the legislation was intended to benefit are only gaining limited ownership in those entities that IAFC is investing in, certainly not reflective of the twenty-five million dollar State loan.

On the other hand, it would have been impossible for IAFC to leverage the initial twenty-five million dollars without forging such relationships. The decision to partner with Cybus could have more far-reaching effects for Iowa than the legislature originally anticipated. In Iowa, the "lack of venture capital money and expertise is consistently identified as a barrier to future economic success."[209] Iowa is consistently ranked one of the worst states in the nation for venture capital availability,[210] and in 2003 was ranked dead last in a ranking of the best states to run a small business in.[211] By giving Cybus the chance to prove that venture capital works in Iowa, it is possible that other venture capital sources will become more interested in assisting agricultural producers, so long as the current endeavors are successful.

What steps the Iowa Legislature will take in the future are yet to be seen, but it is certain that we have not heard the last of IAFC. Notably, it will be difficult for the Iowa Legislature to take the loan proceeds back, as has been suggested before, so long as IAFC is not in violation of any provisions of the Act. The Act was passed with the idea of relinquishing governmental control, and therefore, it is not clear exactly what, if anything, will ultimately be done.

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209. Letter from Dan Winegarden, *supra* note 194.

210. *See* Lynn Okamoto & Jonathan Roos, *Legislature Approves Bill to Revive Economy*, DES MOINES REG., Jan. 25, 2002, at 1A.

211. Phillip Harper, *Best and Worst States to Run a Small Biz*, MICROSOFT.COM SMALL BUSINESS CENTER (Feb. 8, 2003) (on file with author).