

**GENERAL ASSEMBLY OF NORTH CAROLINA  
SESSION 2003**

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**SENATE DRS35204-LC-73 (03/25)**

Short Title: Information Technology Start-up Incentive. (Public)

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Sponsors: Senator Ballantine.

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Referred to:

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A BILL TO BE ENTITLED

AN ACT TO EXCLUDE FROM INCOME TAX CERTAIN GAINS FROM  
INVESTMENTS IN TECHNOLOGY BUSINESSES AND OTHER QUALIFIED  
SMALL BUSINESSES.

The General Assembly of North Carolina enacts:

**SECTION 1.** This act is the Small Business Exclusion of Gain Act.

**SECTION 2.** G.S. 105-130.5(b) is amended by adding a new subdivision to

read:

"(22) The amount of the exclusion of gain for qualified businesses allowed under Part 5 of this Article, to the extent included in federal taxable income."

**SECTION 3.** G.S. 105-134.6(b) is amended by adding a new subdivision to

read:

"(18) The amount of the exclusion of gain for qualified businesses allowed under Part 5 of this Article."

**SECTION 4.** G.S. 105-163.013 and G.S. 105-163.015 are recodified as G.S. 105-163.010A and G.S. 105-163.010B, respectively.

**SECTION 5.** Part 5 of Article 4 of Chapter 105 of the General Statutes, as amended by this act, reads as rewritten:

"Part 5. Tax ~~Credits~~ Incentives for Qualified Business Investments.

"Subpart 1. General Provisions.

**§ 105-163.010. Definitions.**

The following definitions apply in this Part:

- (1) Affiliate. – An individual or business that controls, is controlled by, or is under common control with another individual or business.
- (2) Business. – A corporation, partnership, limited liability company, association, or sole proprietorship operated for profit.

- 1 (3) Control. – A person controls an entity if the person owns, directly or  
2 indirectly, more than ten percent (10%) of the voting securities of that  
3 entity. As used in this subdivision, the term "voting security" means a  
4 security that (i) confers upon the holder the right to vote for the  
5 election of members of the board of directors or similar governing  
6 body of the business or (ii) is convertible into, or entitles the holder to  
7 receive upon its exercise, a security that confers such a right to vote. A  
8 general partnership interest is a voting security.
- 9 (4) Equity security. – Common stock, preferred stock, or an interest in a  
10 ~~partnership, partnership or limited liability company~~, or subordinated  
11 debt that is convertible into, or entitles the holder to receive upon its  
12 exercise, common stock, preferred stock, or an interest in a  
13 ~~partnership, partnership or limited liability company~~.
- 14 (5) Financial institution. – A business that is (i) a bank holding company,  
15 as defined in the Bank Holding Company Act of 1956, 12 U.S.C. §§  
16 1841, et seq., or its wholly owned subsidiary, (ii) registered as a  
17 broker-dealer under the Securities Exchange Act of 1934, 15 U.S.C. §§  
18 78a, et seq., or its wholly owned subsidiary, (iii) an investment  
19 company as defined in the Investment Company Act of 1940, 15  
20 U.S.C. §§ 80a-1, et seq., whether or not it is required to register under  
21 that act, (iv) a small business investment company as defined in the  
22 Small Business Investment Act of 1958, 15 U.S.C. §§ 661, et seq., (v)  
23 a pension or profit-sharing fund or trust, or (vi) a bank, savings  
24 institution, trust company, financial services company, or insurance  
25 company. The term does not include, however, a business, other than a  
26 small business investment company, whose net worth, when added to  
27 the net worth of all of its affiliates, is less than ten million dollars  
28 (\$10,000,000). The term also does not include a business that does not  
29 generally market its services to the public and is controlled by a  
30 business that is not a financial institution.
- 31 (5b) Information technology. – Providing goods or services relating to  
32 electronic data processing, telecommunications, microprocessors, the  
33 Internet, software, information processing, or automated office  
34 systems.
- 35 (6) North Carolina Enterprise Corporation. – A corporation established in  
36 accordance with Article 3 of Chapter 53A of the General Statutes or a  
37 limited partnership in which a North Carolina Enterprise Corporation  
38 is the only general partner.
- 39 (7) Pass-through entity. – An entity or a business, including a limited  
40 partnership, a general partnership, a joint venture, a Subchapter S  
41 Corporation, or a limited liability company, all of which is treated as  
42 owned by individuals or other entities under the federal tax laws, in  
43 which the owners report their share of the income, losses, and credits  
44 from the entity or business on their income tax returns filed with this

1 State. For the purpose of this Part, an owner of a pass-through entity is  
2 an individual or entity who is treated as an owner under the federal tax  
3 laws.

4 (8) Qualified business venture. – A business that (i) engages primarily in  
5 manufacturing, processing, warehousing, wholesaling, research and  
6 development, or a service-related industry, and (ii) is registered with  
7 the Secretary of State under ~~G.S. 105-163.013~~. G.S. 105-163.010A.

8 (9) Qualified grantee business. – A business that (i) is registered with the  
9 Secretary of State under G.S. 105-163.010A ~~G.S. 105-163.013~~, and (ii)  
10 has received during the preceding three years a grant or other funding  
11 from a federal agency under the Small Business Innovation Research  
12 Program administered by the United States Small Business  
13 Administration or from an organization that meets any of the following  
14 qualifications:

15 a. It is a domestic or foreign corporation that (i) is tax-exempt  
16 pursuant to section 501(c)(3) of the Code, (ii) has as its  
17 principal purpose the stimulation of the development of the  
18 biotechnology industry, and (iii) in furtherance of that purpose  
19 has received, or is a successor in interest to an organization that  
20 has received, direct appropriations from the State in at least  
21 three fiscal years.

22 b. It is a domestic or foreign corporation that (i) is tax-exempt  
23 pursuant to section 501(c)(3) of the Code, (ii) has as its  
24 principal purpose the stimulation of the development of the  
25 microelectronics and communication industries, and (iii) in  
26 furtherance of that purpose has received, or is a successor in  
27 interest to an organization that has received, direct  
28 appropriations from the State in at least three fiscal years.

29 c. It is an institute that (i) is administratively located within a  
30 constituent institution of The University of North Carolina, (ii)  
31 is financed in part by a domestic or foreign corporation that is  
32 tax-exempt pursuant to section 501(c)(3) of the Code, (iii) has  
33 as a principal purpose the stimulation of economic development  
34 based on the advancement of science, engineering, and  
35 technology, and (iv) funds, either directly or in collaboration  
36 with other entities, small businesses engaging in developing  
37 technology.

38 (9b) Qualified North Carolina business. – A qualified business venture or a  
39 qualified grantee business.

40 (10) Real estate-related business. – A business that is involved in or related  
41 to the brokerage, selling, purchasing, leasing, operating, or managing  
42 of hotels, motels, nursing homes or other lodging facilities, golf  
43 courses, sports or social clubs, restaurants, storage facilities, or  
44 commercial or residential lots or buildings is a real estate-related

1 business, except that a real estate-related business does not include (i)  
2 a business that purchases or leases real estate from others for the  
3 purpose of providing itself with facilities from which to conduct a  
4 business that is not itself a real estate-related business or (ii) a business  
5 that is not otherwise a real estate-related business but that leases,  
6 subleases, or otherwise provides to one or more other persons a  
7 number of square feet of space which in the aggregate does not exceed  
8 fifty percent (50%) of the number of square feet of space occupied by  
9 the business for its other activities.

10 (10a) Related person. – A person described in one of the relationships set  
11 forth in section 267(b) or 707(b) of the Code.

12 (11) Security. – A security as defined in Section 2(1) of the Securities Act  
13 of 1933, 15 U.S.C. § 77b(1).

14 (12) Selling or leasing at retail. – ~~A business is selling or leasing at retail if~~  
15 ~~the business either (i) sells or leases any product or~~Any of the  
16 following:

17 a. Selling or leasing any service of any nature from a store or  
18 other location open to the public ~~generally or (ii) sells or leases~~  
19 ~~products or generally.~~

20 b. Selling or leasing services of any nature by means other than to  
21 or through one or more other businesses.

22 c. Reselling or leasing at retail products that are purchased or  
23 leased at wholesale and then resold or leased substantially  
24 unmodified.

25 (13) Service-related industry. – A business is engaged in a service-related  
26 industry, whether or not it also sells a product, if it provides services to  
27 customers or clients and does not as a substantial part of its business  
28 engage in a business described in G.S. 105-163.010A(b)(4)~~G.S.~~  
29 ~~105-163.013(b)(4)~~. A business is engaged as a substantial part of its  
30 business in an activity described in G.S. 105-163.010A(b)(4)~~G.S.~~  
31 ~~105-163.013(b)(4)~~ if (i) its gross revenues derived from all activities  
32 described in that subdivision exceed twenty-five percent (25%) of its  
33 gross revenues in any fiscal year or (ii) it is established as one of its  
34 primary purposes to engage in any activities described in that  
35 subdivision, whether or not its purposes were stated in its articles of  
36 incorporation or similar organization documents.

37 (14) Subordinated debt. – Indebtedness that is not secured and is  
38 subordinated to all other indebtedness of the issuer issued or to be  
39 issued to a financial institution other than a financial institution  
40 described in subdivisions (5)(ii) through (5)(v) of this section. ~~Except~~  
41 For the purposes of Subpart 2 of this Part only, except as provided in  
42 G.S. 105-163.014(d1), any portion of indebtedness that matures earlier  
43 than five years after its issuance is not subordinated debt.

44 "**§ 105-163.010A. Registration.**

1 (a) Repealed by Session Laws 1993, c. 443, s. 4.

2 (b) Qualified Business Ventures. – In order to qualify as a qualified business  
3 venture under this Part, a business must be registered with the Securities Division of the  
4 Department of the Secretary of State. To register, the business must file with the  
5 Secretary of State an application and any supporting documents the Secretary of State  
6 may require from time to time to determine that the business meets the requirements for  
7 registration as a qualified business venture. A business meets the requirements for  
8 registration as a qualified business venture if all of the following are true as of the date  
9 the business files the required application:

10 (1) Repealed by Session Laws 1996, Second Extra Session, c. 14, s. 7.

11 (1a) Reserved for future codification purposes.

12 (1b) Either (i) it was organized after January 1 of the calendar year in which  
13 its application is filed or (ii) during its most recent fiscal year before  
14 filing the application, it had gross revenues, as determined in  
15 accordance with generally accepted accounting principles, of five  
16 million dollars (\$5,000,000) or less on a consolidated basis.

17 (2) Repealed by Session Laws 1996, Second Extra Session, c. 14, s. 7.

18 (3) It is organized to engage primarily in manufacturing, processing,  
19 warehousing, wholesaling, research and development, information  
20 technology, or a service-related industry.

21 (4) It does not engage as a substantial part of its business in any of the  
22 following:

23 a. Providing a professional service as defined in Chapter 55B of  
24 the General Statutes.

25 b. Construction or contracting.

26 c. Selling or leasing at retail.

27 d. The purchase, sale, or development, or purchasing, selling, or  
28 holding for investment of commercial paper, notes, other  
29 indebtedness, financial instruments, securities, or real property,  
30 or otherwise make investments.

31 e. Providing personal grooming or cosmetics services.

32 f. Offering any form of entertainment, amusement, recreation, or  
33 athletic or fitness activity for which an admission or a  
34 membership is charged.

35 (5) It was not formed for the primary purpose of acquiring all or part of  
36 the ~~stock~~ stock, other ownership interest, or assets of one or more  
37 existing businesses.

38 (6) It is not a real estate-related business.

39 The effective date of registration for a qualified business venture whose application  
40 is accepted for registration is 60 days before the date its application is filed. No credit or  
41 exclusion of gain is allowed under this Part for an investment made before the effective  
42 date of the registration or after the registration is revoked. For the purpose of this  
43 Article, if a taxpayer's investment is placed initially in escrow conditioned upon other

1 investors' commitment of additional funds, the date of the investment is the date  
2 escrowed funds are transferred to the qualified business venture free of the condition.

3 To remain qualified as a qualified business venture, the business must renew its  
4 registration annually as prescribed by rule by filing a financial statement for the most  
5 recent fiscal year showing gross revenues, as determined in accordance with generally  
6 accepted accounting principles, of five million dollars (\$5,000,000) or less on a  
7 consolidated basis and an application for renewal in which the business certifies the  
8 facts required in the original application.

9 Failure of a qualified business venture to renew its registration by the applicable  
10 deadline ~~shall result~~ results in revocation of its registration effective as of the next day  
11 after the renewal deadline, but ~~shall~~ does not result in forfeiture of tax credits previously  
12 allowed to taxpayers who invested in the business except as provided in G.S.  
13 105-163.014. The Secretary of State shall send the qualified business venture notice of  
14 revocation within 60 days after the renewal deadline. A qualified business venture may  
15 apply to have its registration reinstated by the Secretary of State by filing an application  
16 for reinstatement, accompanied by the reinstatement application fee and a late filing  
17 penalty of one thousand dollars (\$1,000), within 30 days after receipt of the revocation  
18 notice from the Secretary of State. A business that seeks approval of a new application  
19 for registration after its registration has been revoked must also pay a penalty of one  
20 thousand dollars (\$1,000). A registration that has been reinstated is treated as if it had  
21 not been revoked.

22 If the gross revenues of a qualified business venture exceed five million dollars  
23 (\$5,000,000) in a fiscal year, the business must notify the Secretary of State in writing  
24 of this fact by filing a financial statement showing the revenues of the business for that  
25 year.

26 (c) Qualified Grantee Businesses. – In order to qualify as a qualified grantee  
27 business under this Part, a business must be registered with the Securities Division of  
28 the Department of the Secretary of State. To register, the business must file with the  
29 Secretary of State an application and any supporting documents the Secretary of State  
30 may require from time to time to determine that the business meets the requirements for  
31 registration as a qualified grantee business. The requirements for registration as a  
32 qualified grantee business are set out in G.S. 105-163.010(9).

33 The effective date of registration for a qualified grantee business whose application  
34 is accepted for registration is the filing date of its application. No credit or exclusion of  
35 gain is allowed under this Part for an investment made before the effective date of the  
36 registration or after the registration is revoked.

37 To remain qualified as a qualified grantee business, the business must renew its  
38 registration annually as prescribed by rule by filing an application for renewal in which  
39 the business certifies the facts ~~listed in this subsection~~ required for initial registration.

40 (d) Application Forms; Rules; Fees. – Applications for registration, renewal of  
41 registration, and reinstatement of registration under this section shall be in the form  
42 required by the Secretary of State. The Secretary of State may, by rule, require  
43 applicants to furnish supporting information in addition to the information required by  
44 subsections (b) and (c) of this section. The Secretary of State may adopt rules in

1 accordance with Chapter 150B of the General Statutes that are needed to carry out the  
2 Secretary's responsibilities under this Part. The Secretary of State shall prepare blank  
3 forms for the applications and shall distribute them throughout the State and furnish  
4 them on request. Each application shall be signed by the owners of the business or, in  
5 the case of a corporation, by its president, vice president, treasurer, or secretary. must be  
6 signed by the owners, a manager, or an executive officer of the business. There shall be  
7 annexed to the application the affirmation of the person making the application in the  
8 following form: "Under penalties prescribed by law, I certify and affirm that to the best  
9 of my knowledge and belief this application is true and complete." A person who  
10 submits a false application is guilty of a Class 1 misdemeanor.

11 The fee for filing an application for registration under this section is one hundred  
12 dollars (\$100.00). The fee for filing an application for renewal of registration under this  
13 section is fifty dollars (\$50.00). The fee for filing an application for reinstatement of  
14 registration under this section is fifty dollars (\$50.00).

15 An application for renewal of registration under this section shall indicate whether  
16 the applicant is a minority business, as defined in G.S. 143-128, and shall include a  
17 report of the number of jobs the business created during the preceding year that are  
18 attributable to investments that qualify under this section for a tax credit and the average  
19 wages paid by each job. An application that does not contain this information is  
20 incomplete and the applicant's registration may not be renewed until the information is  
21 provided.

22 (e) Revocation of Registration. – If the Securities Division of the Department of  
23 the Secretary of State finds that any of the information contained in an application of a  
24 business registered under this section is false, it shall revoke the registration of the  
25 business. The Secretary of State shall not revoke the registration of a business solely  
26 because it ceases business operations for an indefinite period of time, as long as the  
27 business renews its registration each year as required under G.S. 105-163.010A. ~~G.S.~~  
28 ~~105-163.013.~~

29 (f) Transfer of Registration. – A registration as a qualified business venture or  
30 qualified grantee business may not be sold or otherwise transferred, except that if a  
31 qualified business venture or qualified grantee business enters into a merger,  
32 conversion, consolidation, or other similar transaction with another business and the  
33 surviving company would otherwise meet the criteria for being a qualified business  
34 venture or qualified grantee business, the surviving company retains the registration  
35 without further application to the Secretary of State. In such a case, the qualified  
36 business venture or qualified grantee business shall provide the Secretary of State with  
37 written notice of the merger, conversion, consolidation, or similar transaction and the  
38 name, address, and jurisdiction of incorporation or organization of the surviving  
39 company.

40 (g) Report by Secretary of State. – The Secretary of State shall report to the  
41 Revenue Laws Study Committee by October 1 of each year all of the businesses that  
42 have registered with the Secretary of State as qualified business ventures and qualified  
43 grantee businesses. The report shall include the name and address of each business, the  
44 location of its headquarters and principal place of business, a detailed description of the

1 types of business in which it engages, whether the business is a minority business as  
2 defined in G.S. 143-128, the number of jobs created by the business during the period  
3 covered by the report, and the average wages paid by these jobs.

4 **"§ 105-163.010B. Sunset.**

5 ~~This Subpart 2 of this Part is repealed effective for investments made on or after~~  
6 ~~January 1, 2004. Subpart 3 of this Part is repealed effective for investments made on or~~  
7 ~~after January 1, 2008.~~

8 "Subpart 2. Tax Credits for Qualified Business Investments.

9 **"§ 105-163.011. Tax credits allowed.**

10 (a) No Credit for Brokered Investments. – No credit is allowed under this section  
11 for a purchase of equity securities or subordinated debt if a broker's fee or commission  
12 or other similar remuneration is paid or given directly or indirectly for soliciting the  
13 purchase.

14 (b) Individuals. – Subject to the limitations contained in G.S. 105-163.012, an  
15 individual who purchases the equity securities or subordinated debt of a qualified  
16 business venture or a qualified grantee business directly from that business is allowed as  
17 a credit against the tax imposed by Part 2 of this Article for the taxable year an amount  
18 equal to twenty-five percent (25%) of the amount invested. The aggregate amount of  
19 credit allowed an individual for one or more investments in a single taxable year under  
20 this Part, whether directly or indirectly as owner of a pass-through entity, may not  
21 exceed fifty thousand dollars (\$50,000). The credit may not be taken for the year in  
22 which the investment is made but shall be taken for the taxable year beginning during  
23 the calendar year in which the application for the credit becomes effective as provided  
24 in subsection (c) of this section.

25 (b1) Pass-Through Entities. – This subsection does not apply to a pass-through  
26 entity that has committed capital under management in excess of five million dollars  
27 (\$5,000,000) or to a pass-through entity that is a qualified grantee business, a qualified  
28 business venture, or a North Carolina Enterprise Corporation. Subject to the limitations  
29 provided in G.S. 105-163.012, a pass-through entity that purchases the equity securities  
30 or subordinated debt of a qualified grantee business or a qualified business venture  
31 directly from the business is eligible for a tax credit equal to twenty-five percent (25%)  
32 of the amount invested. The aggregate amount of credit allowed a pass-through entity  
33 for one or more investments in a single taxable year under this Part, whether directly or  
34 indirectly as owner of another pass-through entity, may not exceed seven hundred fifty  
35 thousand dollars (\$750,000). The pass-through entity is not eligible for the credit for the  
36 year in which the investment by the pass-through entity is made but shall be eligible for  
37 the credit for the taxable year beginning during the calendar year in which the  
38 application for the credit becomes effective as provided in subsection (c) of this section.

39 Each individual who is an owner of a pass-through entity is allowed as a credit  
40 against the tax imposed by Part 2 of this Article for the taxable year an amount equal to  
41 the owner's allocated share of the credits for which the pass-through entity is eligible  
42 under this subsection. The aggregate amount of credit allowed an individual for one or  
43 more investments in a single taxable year under this Part, whether directly or indirectly  
44 as owner of a pass-through entity, may not exceed fifty thousand dollars (\$50,000).



1 If an owner's share of the pass-through entity's credit is limited due to the maximum  
2 allowable credit under this section for a taxable year, the pass-through entity and its  
3 owners may not reallocate the unused credit among the other owners.

4 (c) Application. – To be eligible for the tax credit provided in this section, the  
5 taxpayer must file an application for the credit with the Secretary on or before April 15  
6 of the year following the calendar year in which the investment was made. The  
7 Secretary may grant extensions of this deadline, as the Secretary finds appropriate, upon  
8 the request of the taxpayer, except that the application may not be filed after September  
9 15 of the year following the calendar year in which the investment was made. An  
10 application is effective for the year in which it is timely filed. The application shall be  
11 on a form prescribed by the Secretary and shall include any supporting documentation  
12 that the Secretary may require. If an investment for which a credit is applied for was  
13 paid for other than in money, the taxpayer shall include with the application a certified  
14 appraisal of the value of the property used to pay for the investment. The application for  
15 a credit for an investment made by a pass-through entity must be filed by the  
16 pass-through entity.

17 (d) Penalties. – The penalties provided in G.S. 105-236 apply in this Part.

18 **"§ 105-163.012. Limit; carry-over; ceiling; reduction in basis.**

19 (a) The credit allowed a taxpayer under G.S. 105-163.011 may not exceed the  
20 amount of income tax imposed by Part 2 of this Article for the taxable year reduced by  
21 the sum of all other credits allowable except tax payments made by or on behalf of the  
22 taxpayer. The amount of unused credit allowed under G.S. 105-163.011 may be carried  
23 forward for the next five succeeding years. The fifty thousand dollar (\$50,000)  
24 limitation on the amount of credit allowed a taxpayer under G.S. 105-163.011 does not  
25 apply to unused amounts carried forward under this subsection.

26 (b) The total amount of all tax credits allowed to taxpayers under G.S.  
27 105-163.011 for investments made in a calendar year may not exceed six million dollars  
28 (\$6,000,000). The Secretary of Revenue shall calculate the total amount of tax credits  
29 claimed from the applications filed pursuant to G.S. 105-163.011(c). If the total amount  
30 of tax credits claimed for investments made in a calendar year exceeds six million  
31 dollars (\$6,000,000), the Secretary shall allow a portion of the credits claimed by  
32 allocating a total of six million dollars (\$6,000,000) in tax credits in proportion to the  
33 size of the credit claimed by each taxpayer.

34 (c) If a credit claimed under G.S. 105-163.011 is reduced as provided in this  
35 section, the Secretary shall notify the taxpayer of the amount of the reduction of the  
36 credit on or before December 31 of the year following the calendar year in which the  
37 investment was made. The Secretary's allocations based on applications filed pursuant  
38 to G.S. 105-163.011(c) are final and shall not be adjusted to account for credits applied  
39 for but not claimed.

40 (d) The taxpayer's basis in the equity securities or subordinated debt acquired as a  
41 result of an investment in a qualified business venture or qualified grantee business shall  
42 be reduced for the purposes of this Article by the amount of allowable credit.  
43 "Allowable credit" means the amount of credit allowed under G.S. 105-163.011 reduced  
44 as provided in subsection (c) of this section.

1 "§ 105-163.013. Recodified as G.S. 105-163.010A.

2 "§ 105-163.014. Forfeiture of credit.

3 (a) Participation in Business. – A taxpayer who has received a credit under this  
4 Part for an investment in a qualified business venture or qualified grantee business  
5 forfeits the credit if, within three years after the investment was made, the taxpayer  
6 participates in the operation of the qualified business venture or qualified grantee  
7 business. For the purpose of this section, a taxpayer participates in the operation of a  
8 qualified business venture or a qualified grantee business if the taxpayer, the taxpayer's  
9 spouse, parent, sibling, or child, or an employee of any of these individuals or of a  
10 business controlled by any of these individuals, provides services of any nature to the  
11 qualified business venture or qualified grantee business for compensation, whether as an  
12 employee, a contractor, or otherwise. However, a person who provides services to a  
13 qualified business venture or a qualified grantee business, whether as an officer, a  
14 member of the board of directors, or otherwise does not participate in its operation if the  
15 person receives as compensation only reasonable reimbursement of expenses incurred in  
16 providing the services, participation in a stock option or stock bonus plan, or both.

17 (b) False Application. – A taxpayer who has received a credit under this Part for  
18 an investment in a qualified business venture or a qualified grantee business forfeits the  
19 credit if the registration of the qualified business venture or qualified grantee business is  
20 revoked because information in the registration application was false at the time the  
21 application was filed with the Secretary of State.

22 (c) Repealed by Session Laws 1996, Second Extra Session, c. 14, s. 7.

23 (d) Transfer or Redemption of Investment. – A taxpayer who has received a  
24 credit under this Part for an investment in a qualified business venture or a qualified  
25 grantee business forfeits the credit in the following cases:

26 (1) Within one year after the investment was made, the taxpayer transfers  
27 any of the securities received in the investment that qualified for the  
28 tax credit to another person or entity, other than in a transfer resulting  
29 from one of the following:

30 a. The death of the taxpayer.

31 b. A final distribution in liquidation to the owners of a taxpayer  
32 that is a corporation or other entity.

33 c. A merger, conversion, consolidation, or similar transaction  
34 requiring approval by the owners of the qualified business  
35 venture or qualified grantee business under applicable State  
36 law, to the extent the taxpayer does not receive cash or tangible  
37 property in the merger, conversion, consolidation, or other  
38 similar transaction.

39 (2) Except as provided in subsection (d1) of this section, within five years  
40 after the investment was made, the qualified business venture or  
41 qualified grantee business in which the investment was made makes a  
42 redemption with respect to the securities received in the investment.

43 In the event the taxpayer transfers fewer than all the securities in a manner that  
44 would result in a forfeiture, the amount of the credit that is forfeited is the product

1 obtained by multiplying the aggregate credit attributable to the investment by a fraction  
2 whose numerator equals the number of securities transferred and whose denominator  
3 equals the number of securities received on account of the investment to which the  
4 credit was attributable. In addition, if the redemption amount is less than the amount  
5 invested by the taxpayer in the securities to which the redemption is attributable, the  
6 amount of the credit that is forfeited is further reduced by multiplying it by a fraction  
7 whose numerator equals the redemption amount and whose denominator equals the  
8 aggregate amount invested by the taxpayer in the securities involved in the redemption.  
9 The term "redemption amount" means all amounts paid that are treated as a distribution  
10 in part or full payment in exchange for securities under section 302(a) of the Code.

11 (d1) Certain Redemptions Allowed. – Forfeiture of a credit does not occur under  
12 this section if a qualified business venture that engages primarily in motion picture film  
13 production makes a redemption with respect to securities received in an investment and  
14 the following conditions are met:

- 15 (1) The redemption occurred because the qualified business venture  
16 completed production of a film, sold the film, and was liquidated.
- 17 (2) Neither the qualified business venture nor a related person continues to  
18 engage in business with respect to the film produced by the qualified  
19 business venture.

20 (e) Effect of Forfeiture. – A taxpayer who forfeits a credit under this section is  
21 liable for all past taxes avoided as a result of the credit plus interest at the rate  
22 established under G.S. 105-241.1(i), computed from the date the taxes would have been  
23 due if the credit had not been allowed. The past taxes and interest are due 30 days after  
24 the date the credit is forfeited; a taxpayer who fails to pay the past taxes and interest by  
25 the due date is subject to the penalties provided in G.S. 105-236.

26 "**§ 105-163.015. Recodified as G.S. 105-163.010B.**

27 "Subpart 3. Exclusion of Gain for Qualified Business Investments.

28 "**§ 105-163.020. Exclusion of gain allowed.**

29 (a) Any gain recognized for federal income tax purposes from the sale or  
30 exchange of qualified securities is excluded from taxation under this Article if the sale  
31 or exchange occurs on or after January 1, 2006.

32 (b) A taxpayer that is an owner of a pass-through entity may exclude from the  
33 taxpayer's income taxable under this Article an amount equal to the taxpayer's allocated  
34 share of the exclusion for which the pass-through entity is eligible under subsection (a)  
35 of this section.

36 "**§ 105-163.021. Qualified securities.**

37 (a) Qualified Security. – Except as otherwise provided in this section, any equity  
38 security or subordinated debt instrument issued by a qualified North Carolina business  
39 is a qualified security if it satisfies all of the following conditions:

- 40 (1) It is originally issued by the business on or after January 1, 2003.
- 41 (2) As of the date of issuance, the issuing business is a qualified North  
42 Carolina business.
- 43 (3) The security or instrument is acquired by the taxpayer at its original  
44 issue in exchange for any tangible or intangible property or benefit to

1                   the business, including cash, promissory notes, services performed,  
2                   contracts for services to be performed, or other equity securities of the  
3                   business.

4           (b) Registration. – Securities of a qualified North Carolina business acquired  
5 more than 60 days before the effective date of its registration are not qualified  
6 securities. Revocation of the registration of a qualified North Carolina business pursuant  
7 to G.S. 105-163.010A does not affect the exclusion of gain from qualified securities  
8 acquired while the registration was in effect or within 60 days before it became  
9 effective.

10          (c) Effect of Redemptions and Other Distributions. – An equity security or  
11 subordinated debt instrument is not a qualified security to the extent the taxpayer  
12 purchased it with the proceeds of a redemption, dividend, or distribution made by the  
13 business that issued the security or instrument. For the purpose of this subsection, when  
14 a business makes a redemption, dividend, or distribution during the four-year period  
15 beginning two years before the issuance of securities or instruments to a taxpayer, the  
16 taxpayer is considered to have used the proceeds of the redemption, dividend, or  
17 distribution toward the purchase of the securities or instruments. A redemption,  
18 dividend, or distribution occurs when the business issuing the security or instrument  
19 does one of the following:

20               (1) Purchases, directly or indirectly, any of its outstanding equity  
21 securities or subordinated debt, other than qualified securities, from the  
22 taxpayer or a related person.

23               (2) Declares a dividend or makes a distribution with respect to any of its  
24 outstanding equity securities or subordinated debt, other than qualified  
25 securities, to the taxpayer or a related person. This subdivision does  
26 not apply, however, to a distribution in connection with one of the  
27 following:

28                   a. The reimbursement to the taxpayer of the reasonable costs of  
29 forming, syndicating, managing, and operating the business.

30                   b. An increase in the taxpayer's taxes, penalties, or interest to the  
31 extent the increase is caused by the allocation to the taxpayer of  
32 income of the business.

33          The repayment of principal on subordinated debt is a purchase of the debt except to  
34 the extent the repayment is repayment of principal due on the subordinated debt at its  
35 maturity pursuant to the terms of the subordinated debt instrument. If a transaction is  
36 treated under section 304(a) of the Code as a distribution in redemption of the equity  
37 securities of a business, that business has, for the purpose of this subsection, purchased  
38 an amount of its equity securities equal to the amount treated as such a distribution  
39 under section 304(a) of the Code.

40          (d) Conversion of Other Securities. – Any equity security or subordinated debt  
41 instrument issued by a business and acquired by the taxpayer solely through the  
42 conversion of another equity security or subordinated debt instrument that was issued by  
43 the business and was a qualified security in the hands of the taxpayer is considered, for

1 the purpose of this section, a qualified security in the hands of the taxpayer and acquired  
2 by the taxpayer on the date the taxpayer acquired the converted qualified security.

3 (e) Transfers. – In the case of a transfer by gift, by death, or from a pass-through  
4 entity to one of its owners, the transferee is considered, for the purpose of this section,  
5 to have acquired the qualified security in the same manner as the transferor and to have  
6 held it during any continuous period immediately preceding the transfer during which it  
7 was held or treated as held by the transferor.

8 In the case of a transaction described in section 351 of the Code or a reorganization  
9 described in section 368 of the Code, if qualified securities are exchanged for other  
10 securities, the other securities are considered, for the purpose of this section, qualified  
11 securities acquired on the date the exchanged qualified securities were acquired. In the  
12 case of a transaction described in section 351 of the Code, the newly acquired securities  
13 are considered qualified securities, however, only if, immediately after the transaction,  
14 the corporation issuing the securities owns, directly or indirectly, securities representing  
15 control, within the meaning of section 368(c) of the Code, of the corporation whose  
16 securities were exchanged.

17 **"§ 105-163.022. Limitations.**

18 (a) Contributions and Exchanges of Property. – In the case of a transaction  
19 described in section 351 or 721 of the Code or a reorganization described in section 368  
20 of the Code, if a taxpayer contributes property to or exchanges property with a qualified  
21 North Carolina business, the following rules apply:

22 (1) Qualified securities exchanged for property. – Except as otherwise  
23 provided in subdivision (3) of this subsection, a taxpayer who transfers  
24 property to a business in exchange for qualified securities in the  
25 business must, for purposes of determining North Carolina taxable  
26 income, recognize gain equal to the amount by which the fair market  
27 value of the property exceeded the taxpayer's basis in the property on  
28 the date the property was exchanged for the qualified securities. This  
29 gain must be recognized for the years for which the taxpayer claims an  
30 exclusion of gain under this Part with respect to the disposition of  
31 qualified securities received in exchange for the property.

32 (2) Contributions to capital. – Except as otherwise provided in subdivision  
33 (3) of this subsection, if the adjusted basis of a qualified security is  
34 adjusted due to a contribution to capital after the date the qualified  
35 security was issued originally, for purposes of determining North  
36 Carolina taxable income, the taxpayer must recognize gain equal to the  
37 amount by which the fair market value of the contributed property  
38 exceeded the taxpayer's basis in the property on the date the property  
39 was contributed. This gain must be recognized for the years for which  
40 the taxpayer claims an exclusion of gain under this Part with respect to  
41 the disposition of the qualified securities.

42 (3) Disposition of contributed property. – If a qualified North Carolina  
43 business disposes of property contributed to it, the disposition occurs  
44 before the taxpayer who contributed the property claims an exclusion

1                   of gain pursuant to this Part with respect to qualified securities affected  
2                   by the contribution, and the taxpayer recognizes gain from the  
3                   disposition, then for purposes of subdivisions (1) and (2) of this  
4                   subsection, the taxpayer's basis in the contributed property is increased  
5                   by any gain the taxpayer recognized from the disposition.

6           (b)   Short Positions. – If a taxpayer has an offsetting short position with respect to  
7           any qualified securities, there is no exclusion of gain under this Part from the sale or  
8           exchange of the qualified securities unless the taxpayer established the short position on  
9           or after January 1, 2006, and elects to recognize gain as if the qualified securities were  
10           sold at fair market value on the date the taxpayer first established the short position. For  
11           the purposes of this subsection, a taxpayer has an offsetting short position with respect  
12           to qualified securities if one of the following conditions is satisfied:

13                   (1)   The taxpayer or a related person has made a short sale of substantially  
14                   identical property.

15                   (2)   The taxpayer or a related person has acquired an option to sell  
16                   substantially identical property at a fixed price.

17                   (3)   The taxpayer has entered into any other transaction that the Secretary  
18                   has identified in guidelines adopted under this section as one that  
19                   substantially reduces the risk of loss from holding the qualified  
20                   securities.

21           (c)   Guidelines. – The Secretary of Revenue must adopt guidelines identifying  
22           transactions that substantially reduce the risk of loss from holding qualifying securities  
23           for the purpose of subsection (b) of this section. In addition, the Secretary must adopt  
24           guidelines identifying activities and situations designed to avoid the purpose of this Part  
25           through split-ups, shell corporations, partnerships, or otherwise. There is no exclusion  
26           of gain otherwise allowable under this Part to the extent a taxpayer has engaged in an  
27           activity or created a situation identified by the Secretary in guidelines as one that is  
28           designed to avoid the purpose of this Part."

29           **SECTION 6.** This act is effective when it becomes law. Notwithstanding the  
30 provisions of G.S. 105-163.010A as recodified by this act, if a qualified North Carolina  
31 business files its application for registration within 60 days after the effective date of  
32 this act and the application is accepted, the effective date of the registration is the later  
33 of January 1, 2003, or the date the business first issues equity securities or subordinated  
34 debt.