GENERAL ASSEMBLY OF NORTH CAROLINA
SESSION 2009

H **1**

HOUSE BILL 2001

Short Title:	Small Business Start-Up Tax Relief.	(Public)
Sponsors:	Representatives Gibson; Adams, Bordsen, Faison, E. Floyd, Gill, Hall, Stewart, Tarleton, and Wray.	
Referred to:	Commerce, Small Business, and Entrepreneurship, if favorable, Finance.	

May 26, 2010

A BILL TO BE ENTITLED

AN ACT TO ENCOURAGE INNOVATIVE SMALL START-UP BUSINESSES TO GROW AND EXPAND IN NORTH CAROLINA; TO REQUIRE ANNUAL TRANSACTION REPORTS; AND TO ENCOURAGE REFORM IN PROCUREMENT STANDARDS.

The General Assembly of North Carolina enacts:

SECTION 1. G.S. 105-130.5(b) is amended by adding a new subdivision to read:

"(b) The following deductions from federal taxable income shall be made in determining State net income:

…

<u>(26)</u> <u>The amount of any exclusion of gain for qualified businesses allowed under Part 5 of this Article, to the extent included in federal taxable income, less the amount of the credits recaptured pursuant to G.S. 105-163.021; provided, however, that a taxpayer is not required to claim this exclusion.</u>"

SECTION 2. G.S. 105-134.6(b) is amended by adding a new subdivision to read:

"(b) Deductions. – The following deductions from taxable income shall be made in calculating North Carolina taxable income, to the extent each item is included in taxable income:

…

<u>(21)</u> <u>The amount of the exclusion of gain for qualified businesses allowed under Part 5 of this Article, less the amount of the credits recaptured pursuant to G.S. 105-163.021; provided, however, that a taxpayer is not required to claim this exclusion.</u>"

SECTION 3. Part 5 of Article 4 of Chapter 105 of the General Statutes is amended by adding the following new section to read:

"<u>**§ 105-163.020. Exclusion of gain allowed.**</u>

<u>(a)</u> <u>Election. – A taxpayer may elect to exclude from the taxpayer's income taxable under this Article any gain or other taxable income recognized for federal income tax purposes from the sale or exchange of qualified securities.</u>

<u>(b)</u> <u>Pass-Through Entity. – Except as provided in subsection (c) of this section, a taxpayer that is an owner of a pass-through entity may exclude from the taxpayer's income taxable under this Article an amount equal to the taxpayer's allocated share of the exclusion for which the pass-through entity is eligible under subsection (a) of this section.</u>

<u>(c)</u> <u>Qualified Grantee Pass-Through Entity. – If a taxpayer is an owner of a pass-through entity that was a qualified grantee business at the time of the taxpayer's investment in the pass-through entity, the taxpayer may exclude from the taxpayer's income taxable under this Article an amount equal to the gain or other taxable income recognized as a</u>

result of the taxpayer's ownership in the pass-through entity, multiplied by a fraction, the numerator of which is the total amount invested by the pass-through entity in qualified businesses and the denominator of which is the total amount invested by the pass-through entity. For purposes of this subsection, the amounts invested by a pass-through entity shall be the amounts invested immediately before the pass-through entity's sale or exchange producing the gain or taxable income excluded under this subsection.

"**§ 105-163.021. Recapture of credit.**

If a taxpayer claims an exclusion of gain from income pursuant to G.S. 105-163.020, the income tax of the taxpayer for the tax year for which the exclusion is claimed shall be increased by the amount of all credits previously claimed by the taxpayer pursuant to G.S. 105-163.011 with respect to qualified securities that (i) have been sold or exchanged and (ii) the gain from which has been excluded pursuant to G.S. 105-163.020.

"**§ 105-163.022. Qualified securities.**

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

(1) It is originally issued by the business on or after January 1, 2011.
(2) As of the date of issuance, the issuing business is a qualified business.
(3) The security or instrument is acquired by the taxpayer at its original issue in exchange for any tangible or intangible property or benefit to the business, including cash, promissory notes, services performed, contracts for services to be performed, or other equity securities of the business.
(4) It is held by the taxpayer for a continuous period of more than one year.
(5) No broker's fee or commission or other similar remuneration is paid or given directly or indirectly for soliciting the purchase.
(6) If the security or instrument was purchased by a pass-through entity, the entity met the requirements of G.S. 105-163.011(b1) at the time of purchase.

(b) Registration. – Securities of a qualified business acquired before the effective date of its registration are not qualified securities. Revocation of the registration of a qualified business pursuant to G.S. 105-163.013 does not affect the exclusion of gain from qualified securities acquired while the registration was in effect if all conditions for registration are satisfied.

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

(1) Purchases, directly or indirectly, any of its outstanding equity securities or subordinated debt, other than qualified securities, from the taxpayer or a related person.
(2) Declares a dividend or makes a distribution with respect to any of its outstanding equity securities or subordinated debt, other than qualified securities, to the taxpayer or a related person. This subdivision does not apply, however, to a distribution in connection with one of the following:
    a. The reimbursement to the taxpayer of the reasonable costs of forming, syndicating, managing, and operating the business.

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

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

(d) Exception for Certain Transactions. – The following transactions are not treated as a redemption or distribution for the purposes of subsection (c) of this section:

(1) Any deemed liquidation of a business pursuant to section 708(b)(1)(A) of the Code by reason of the business becoming a disregarded entity for federal tax purposes, to the extent there is not actual distribution of money or other property to the taxpayer of a related person.

(2) Any deemed distribution or redemption by reason of a technical termination of a business pursuant to section 708(b)(1)(B) of the Code to the extent there is no actual distribution of money or other property to the taxpayer or a related person.

(e) Conversion of Other Securities. – Any equity security or subordinated debt instrument issued by a business and acquired by the taxpayer solely through the conversion of another equity security or subordinated debt instrument that was issued by the business and was a qualified security in the hands of the taxpayer is considered, for the purpose of this section, a qualified security in the hands of the taxpayer and acquired by the taxpayer on the date the taxpayer acquired the converted qualified security.

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

In the case of a transaction described in section 351 or 721 of the Code or a reorganization described in section 368 of the Code, if qualified securities are exchanged for other securities, the other securities are considered, for the purpose of this section, qualified securities acquired on the date the exchanged qualified securities were acquired. In the case of a transaction described in section 351 or 721 of the Code, the newly acquired securities are considered qualified securities, however, only if, immediately after the transaction, the business issuing the securities owns, directly or indirectly, securities representing control, within the meaning of section 368(c) of the Code, of the business whose securities were exchanged.

"**§ 105-163.023. Limitations.**

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

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

to the disposition of qualified securities received in exchange for the property.

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

(3) Disposition of contributed property. – If a qualified business disposes of property contributed to it, the disposition occurs before the taxpayer who contributed the property claims an exclusion of gain pursuant to this Part with respect to qualified securities affected by the contribution, and the taxpayer recognizes gain from the disposition, then for purposes of subdivisions (1) and (2) of this subsection, the taxpayer's basis in the contributed property is increased by any gain the taxpayer recognized from the disposition.

(b) Transactions That Substantially Reduce the Risk of Loss. – If a taxpayer has entered into any transaction that substantially reduces the risk of loss from holding the qualified securities, there is no exclusion of gain under this Part from the sale or exchange of the qualified securities unless the taxpayer entered into the transaction on or after January 1, 2011, and elects to recognize gain as if the qualified securities were sold at fair market value on the date the taxpayer first entered into that transaction. The following are examples of a transaction that substantially reduces the risk of loss from holding the qualified securities:

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

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

SECTION 4. Part 4 of Article 5 of Chapter 105 of the General Statutes is amended by adding a new section to read:

"**§ 105-164.16A. Annual transaction reports.**

(a) Definitions. –

(1) Reserved.

(2) Reserved.

(3) Franchise. – An agreement or license from an owner of a trademark or trade name permitting another to sell a product or service under that name or mark.

(4) Franchisee. – A person granted a franchise by a franchisor.

(5) Franchisor. – A person that grants a franchise to a franchisee.

(6) Reserved.

(7) Reserved.

(8) Liability policy. – Defined in G.S. 20-279.21.

(b) Annual transaction report. – A taxpayer listed in subsection (c) of this section must submit an annual report by May 1 of each year to the Secretary. The report must include the following information:

(1) The name and address of a recipient of consideration paid by an insurer or of a franchisee.

(2) The date of each transaction.

(3) If the report is by an insurer, the amount of consideration paid, itemized by recipient, and the total consideration paid during the period covered by the report.

(4) If the report is by a franchisor, the gross sales of each franchise located in this State, as reported by the franchisee to the franchisor; the total amount of sales by the franchisor to the franchisee, itemized by franchisee; and the income of each franchise located in this State, as reported by the franchisee to the franchisor.

(c) Taxpayers covered. – The following persons must file an annual transaction report required by subsection (b) of this section:

(1) An insurer that is licensed to issue a motor vehicle liability policy and that paid, during the period covered by the annual transaction report, consideration under a liability policy for servicing or repair in this State on behalf of an insured.

(2) A franchisor making a wholesale or retail sale to a franchisee during the period covered by the annual transaction report."

SECTION 5. Article 3 of Chapter 143 of the General Statutes is amended by adding a new section to read:

"**§ 143-48.5. Procurement reform.**

(a) Findings. – The North Carolina General Assembly finds the following:

(1) A Multiple Award Schedule contract is one that allows multiple vendors to be awarded a State contract for goods or services by providing their total catalogue for lines of equipment and attachments to eligible purchasers, including State agencies, departments, institutions, public school districts (K-12), political subdivisions, and higher education facilities.

(2) A Multiple Award Schedule contract allows multiple vendors to compete and be awarded a contract based upon the value of their products or services.

(3) A properly administered Multiple Award Schedule contract allows the State to evaluate vendors based on a variety of factors including discounts, total life cycle costs, service, warranty, distribution channel, and past vendor performance.

(4) Under appropriate circumstances, Multiple Award Schedule contracts result in competitive pricing, transparency, administrative savings, expedited procurement, and flexibility for State purchasers.

(b) Policy. – The North Carolina Department of Administration shall consider the use of Multiple Award Schedule contracts when issuing Requests for Proposal for State term contracts."

SECTION 6. Sections 1, 2, and 3 of this act are effective for taxable years beginning on or after January 1, 2010. Section 4 of this act becomes effective January 1, 2011. The remainder of this act is effective when it becomes law.