GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1997

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HOUSE BILL 1412

Short Title: Rollover of Gain/Small Business Sale. (Public)

Sponsors: Representatives Blue, Hensley, Mosley; Allred, Black, H. Hunter, Nichols, and Womble.

Referred to: Finance.

May 21, 1998

A BILL TO BE ENTITLED

AN ACT TO PROVIDE FOR NONRECOGNITION OF CAPITAL GAIN FOR STATE INCOME TAX PURPOSES ON SALES OF CERTAIN SMALL BUSINESSES IF THE OWNER BUYS A NEW SMALL BUSINESS WITHIN TWO YEARS.

The General Assembly of North Carolina enacts:

Section 1. Article 3B of Chapter 105 of the General Statutes is amended by adding a new section to read:

"**§ 105-129.20. Rollover of gain on sale of qualified small business.**

(a) Exclusion of Gain. – If the owner of a qualified small business (old business) sells his or her entire interest in the business and, within a period beginning two years before the date of the sale and ending two years after the date of the sale, purchases and becomes the owner of part or all of another qualified small business (new business), any gain recognized for federal income tax purposes from the sale of the old business is excluded from taxation under Article 4 of this Chapter to the extent the amount realized from the sale of the old business does not exceed the taxpayer's cost of purchasing the new business.

(b) Exchanges. – An exchange of a qualified small business for other property shall be considered a sale or purchase for the purpose of this section.

(c) Restrictions. – The exclusion allowed by this section does not apply in the following cases:

(1) If the taxpayer sells or disposes of the new business before the date of sale of the old business.

(2) If, within two years before the sale of the old business, the taxpayer sold another old business and any part of the gain from the sale of that other business was excluded from taxation pursuant to this section.

(d) Basis of New Business. – The taxpayer's basis in the new business shall be reduced by an amount equal to the amount of gain not recognized on an old business pursuant to this section because of the taxpayer's purchase of the new business."

Section 2. G.S. 105-129.15 reads as rewritten:

"§ 105-129.15. Definitions.

The following definitions apply in this Article:

(1) Business property. – Tangible personal property that is used by the taxpayer in connection with a business or for the production of income and is capitalized by the taxpayer for tax purposes under the Code. The term does not include, however, a luxury passenger automobile taxable under section 4001 of the Code or a watercraft used principally for entertainment and pleasure outings for which no admission is charged.

(2) Cost. – Determined pursuant to regulations adopted under section 1012 of the Code, subject to the limitation on cost provided in section 179 of the Code.

(2a) Reserved.

(2b) Materially participate. – Defined in section 469 of the Code.

(2c) Owner. – A taxpayer who owns part or all of a qualified small business and materially participates in conducting its trade or business.

(3) Purchase. – Defined in section 179 of the Code.

(4) Qualified small business. – A corporation, a partnership, an association, a limited liability company, or a sole proprietorship that meets the following conditions:

a. It is operated for profit.

b. During its most recent fiscal year before its sale or acquisition by the taxpayer, it had gross revenues, as determined in accordance with generally accepted accounting principles, of forty million dollars ($40,000,000) or less on a consolidated basis.

c. It meets the conditions of G.S. 105-163.013(b)(3) through (6)."

Section 3. G.S. 105-130.5(b) is amended by adding a new subdivision to read:

"(17) The amount of the exclusion of gain for sales of qualified businesses allowed under Article 3B of this Chapter, to the extent included in federal taxable income."

Section 4. G.S. 105-134.6(b) is amended by adding a new subdivision to read:

"(15) The amount of the exclusion of gain for sales of qualified businesses allowed under Article 3B of this Chapter."

Section 5. The title of Article 3B of Chapter 105 of the General Statutes reads as rewritten:

"ARTICLE 3B.

Business Tax ~~Credit.~~ Reductions."

Section 6. G.S. 105-129.18 reads as rewritten:

"**§ 105-129.18. Substantiation.**

To claim ~~the credit~~ a tax benefit allowed by this Article, the taxpayer must provide any information required by the Secretary of Revenue. Every taxpayer claiming a ~~credit~~ tax benefit under this Article must maintain and make available for inspection by the Secretary of Revenue any records the Secretary considers necessary to determine and verify the amount of the ~~credit~~ tax benefit to which the taxpayer is entitled. The burden of proving eligibility for the credit and the amount of the ~~credit~~ tax benefit rests upon the taxpayer, and no ~~credit~~ tax benefit may be allowed to a taxpayer that fails to maintain adequate records or to make them available for inspection."

Section 7. G.S. 105-163.013(b)(5) reads as rewritten:

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

Section 8. G.S. 105-241.1(e) reads as rewritten:

"(e) Statute of Limitations. – There is no statute of limitations and the Secretary may propose an assessment of tax due from a taxpayer at any time if (i) the taxpayer did not file a proper application for a license or did not file a return, (ii) the taxpayer filed a false or fraudulent application or return, or (iii) the taxpayer attempted in any manner to fraudulently evade or defeat the tax.

If a taxpayer files a return reflecting a federal determination as provided in G.S. 105-29, 105-130.20, 105-159, 105-160.8, 105-163.6A, or 105-197.1, the Secretary must propose an assessment of any tax due within one year after the return is filed or within three years of when the original return was filed or due to be filed, whichever is later. If there is a federal determination and the taxpayer does not file the required return, the Secretary must propose an assessment of any tax due within three years after the date the Secretary received the final report of the federal determination. If a taxpayer forfeits a tax credit pursuant to G.S. 105-163.014 or Article 3A of this Chapter, the Secretary must assess any tax due as a result of the forfeiture within three years after the date of the forfeiture. If a taxpayer elects under section 1033(a)(2)(A) of the Code not to recognize gain from involuntary conversion of property into money, the Secretary must assess any tax due as a result of the conversion or election within the applicable period provided under section 1033(a)(2)(C) or section 1033(a)(2)(D) of the Code. If a taxpayer sells at a gain the taxpayer's principal residence, the Secretary must assess any tax due as a result of the sale within the period provided under section 1034(j) of the Code. If the owner of a qualified small business as defined in Article 3B of this Chapter sells the business at a gain, the Secretary must assess any tax due as a result of the sale within three years after the taxpayer notifies the Secretary of (i) the taxpayer's cost of purchasing and becoming the owner of a new qualified small business that results in the exclusion of any of the

<u>gain pursuant to Article 3B of this Chapter or (ii) the taxpayer's intent not to purchase or failure to have purchased a new business within the period prescribed in Article 3B of this Chapter.</u>

In all other cases, the Secretary must propose an assessment of any tax due from a taxpayer within three years after the date the taxpayer filed an application for a license or a return or the date the application or return was required by law to be filed, whichever is later.

If the Secretary proposes an assessment of tax within the time provided in this section, the final assessment of the tax is timely.

A taxpayer may make a written waiver of any of the limitations of time set out in this subsection, for either a definite or an indefinite time. If the Secretary accepts the taxpayer's waiver, the Secretary may propose an assessment at any time within the time extended by the waiver."

Section 9. This act becomes effective for taxable years beginning on or after January 1, 1999, and applies to sales and exchanges that occur on or after that date.