

GENERAL ASSEMBLY OF NORTH CAROLINA  
SESSION 2009

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HOUSE DRH11105-MC-307 (05/13)

Short Title: Small Business Start-Up Tax Relief.

(Public)

Sponsors: Representative Gibson.

Referred to:

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:

...

(26) 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."

**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:

...

(21) 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."

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

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

(a) 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.

(b) 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.

(c) 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



1 taxable under this Article an amount equal to the gain or other taxable income recognized as a  
2 result of the taxpayer's ownership in the pass-through entity, multiplied by a fraction, the  
3 numerator of which is the total amount invested by the pass-through entity in qualified  
4 businesses and the denominator of which is the total amount invested by the pass-through  
5 entity. For purposes of this subsection, the amounts invested by a pass-through entity shall be  
6 the amounts invested immediately before the pass-through entity's sale or exchange producing  
7 the gain or taxable income excluded under this subsection.

8 **"§ 105-163.021. Recapture of credit.**

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

14 **"§ 105-163.022. Qualified securities.**

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

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

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

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

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

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

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

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

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

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

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

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

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

39                  **"§ 105-163.023. Limitations.**

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

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

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

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

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

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

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

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

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

33 **"§ 105-164.16A. Annual transaction reports.**

34 (a) Definitions. –

35 (1) Reserved.

36 (2) Reserved.

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

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

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

42 (6) Reserved.

43 (7) Reserved.

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

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

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

50 (2) The date of each transaction.

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

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

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

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

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

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

19           "**§ 143-48.5. Procurement reform.**

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

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

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

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

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

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

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