

MAINE STATE LEGISLATURE

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116th MAINE LEGISLATURE

SECOND REGULAR SESSION-1994

Legislative Document

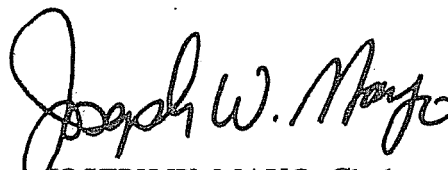
No. 1937

H.P. 1423

House of Representatives, February 24, 1994

An Act to Provide Incentives for Businesses to Create Jobs in the State.

Approved for introduction by a majority of the Legislative Council pursuant to Joint Rule 26.
Reference to the Committee on Taxation suggested and ordered printed.


JOSEPH W. MAYO, Clerk

Presented by Representative WHITCOMB of Waldo.

Be it enacted by the People of the State of Maine as follows:

2
4 Sec. 1. 36 MRSA §5219-J is enacted to read:

6 §5219-J. Small business investment credit

8 1. Definitions. As used in this section, unless the
10 context otherwise indicates, the following terms have the
12 following meanings.

14 A. "Aggregate gross assets" means the amount of cash and
16 the aggregate adjusted bases of other property held by a
18 corporation.

20 B. "Eligible corporation" means a domestic corporation,
22 except:

24 (1) A corporation or a direct or indirect subsidiary
26 of that corporation with respect to which an election
28 under the Code, Section 936 is in effect;

30 (2) A regulated investment company, real estate
32 investment trust or real estate mortgage investment
34 conduit; or

36 (3) A cooperative.

38 C. "Eligible gain" means a gain from the sale or exchange
40 of qualified small business stock held for more than 5 years.

42 D. "Parent-subsidary controlled group" means one or more
44 chains of corporations connected through stock ownership
46 with a common parent corporation when:

48 (1) Stock possessing at least 50% of the total
50 combined voting power of all classes of stock entitled
to vote or at least 50% of the total value of shares of
all classes of stock of each of the corporations,
except the common parent corporation, is owned by one
or more of the other corporations; and

(2) The common parent corporation owns stock
possessing at least 50% of the total combined voting
power of all classes of stock entitled to vote or at
least 50% of the total value of shares of all classes
of stock of at least one of the other corporations
excluding, in computing that voting power or value,
stock owned directly by the other corporations. For
the purposes of this section, the Code, Section
1563(a)(4) does not apply. All corporations that are

2 members of the same parent-subsidary controlled group
3 must be treated as one corporation for purposes of this
4 subparagraph.

6 E. "Pass-through entity" means any of the following:

8 (1) A partnership;

10 (2) An S corporation;

12 (3) A regulated investment company; or

14 (4) A common trust fund.

16 F. "Qualified small business" means a domestic corporation
17 that is a C corporation when:

18 (1) The aggregate gross assets of the corporation or
19 any predecessor of the corporation on or after January
20 1, 1995 and before the issuance did not exceed
21 \$50,000,000;

22 (2) The aggregate gross assets of the corporation
23 immediately after the issuance, determined by taking
24 into account amounts received in the issuance, do not
25 exceed \$50,000,000;

26 (3) At least 80% of the corporation's payroll, as
27 measured by total dollar value, is attributable to
28 employment located in the State; and

29 (4) The corporation agrees to submit reports of assets
30 and payroll to the State Tax Assessor and to
31 shareholders as the State Tax Assessor may require to
32 carry out the purposes of this section.

33 G. "Qualified small business stock" means, except as
34 otherwise provided in this section, stock in a C corporation
35 that is originally issued on or after January 1, 1995 and
36 before January 1, 1999, when:

37 (1) As of the date of issuance, the corporation is a
38 qualified small business; and

39 (2) Except as provided in subsections 7 and 8, the
40 stock is acquired by the taxpayer at its original
41 issue, directly or through an underwriter, in either of
42 the following manners:

43 (a) In exchange for money or other property, not
44 including stock; or

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(b) As compensation for services provided to the corporation, other than services performed as an underwriter of the stock.

H. "Qualified trade or business" means a trade or business other than:

(1) A trade or business involving the performance of services in the fields of health, law, engineering, architecture, accounting, actuarial science, performing arts, consulting, athletics, financial services, brokerage services or a trade or business in which the principal asset of the trade or business is the reputation or skill of one or more of its employees; or

(2) A banking, insurance, financing, leasing, investing or similar business.

I. "Specialized small business investment company" means an eligible corporation that is licensed to operate under the Small Business Investment Act of 1958, Section 301(d), as in effect on May 13, 1993.

2. Exclusion from gross income. For the purposes of this section, a taxpayer may exclude 50% of the amount of gain from the sale or exchange of qualified small business stock held for more than 5 years from that taxpayer's gross income. In the case of a married taxpayer filing a joint return, the amount of gain taken into account under this subsection must be allocated equally between the spouses for purposes of applying subsection 3 to subsequent taxable years.

For purposes of this subsection, marital status must be determined under the Code, Section 7703.

3. Eligible gain. If the taxpayer has eligible gain for the taxable year from one or more dispositions of stock issued by a corporation, the aggregate amount of the gain from dispositions of stock issued by the corporation that may be taken into account under subsection 2 for the taxable year may not exceed the greater of either of the following:

A. Ten million dollars, reduced by the aggregate amount of eligible gain taken into account by the taxpayer under subsection 2 for prior taxable years and attributable to dispositions of stock issued by the corporation. For a married individual filing a separate return, the aggregate amount of the gain from dispositions of stock issued by the corporation may not exceed the greater of paragraph B or

2 \$5,000,000, reduced by the aggregate amount of eligible gain
4 taken into account by the taxpayer under subsection 2 for
prior taxable years and attributable to dispositions of
stock issued by the corporation; or

6 B. Ten times the aggregate adjusted bases of qualified
8 small business stock issued by the corporation and disposed
10 of by the taxpayer during the taxable year. For purposes of
12 this paragraph, the adjusted bases of stock must be
determined without regard to any addition to those bases
after the date on which the stock was originally issued.

14 4. Qualified small business stock. Provisions regarding
qualified small business stock are as follows.

16 A. Stock in a corporation may not be treated as qualified
18 small business stock unless, during substantially all of the
20 taxpayer's holding period for the stock, the corporation
22 meets the active business requirements of subsection 6 and
24 the corporation is a C corporation. Notwithstanding the
provisions of subsection 6, a corporation must be treated as
meeting the active business requirements of subsection 6 for
any period during which the corporation qualifies as a
specialized small business investment company.

26 B. Stock acquired by the taxpayer may not be treated as
28 qualified small business stock if, at any time during the
30 4-year period beginning on the date 2 years before the
32 issuance of the stock, the corporation issuing the stock
purchased, directly or indirectly, any of its stock from the
taxpayer or from a related person, within the meaning of the
Code, Section 267(b) or 707(b), to the taxpayer.

34 C. Stock issued by a corporation may not be treated as
36 qualified small business stock if, during the 2-year period
38 beginning on the date one year before the issuance of the
40 stock, the corporation made one or more purchases of its
stock with an aggregate value, as of the time of the
respective purchases, exceeding 5% of the aggregate value of
all of its stock as of the beginning of the 2-year period.

42 D. When a transaction is treated under the Code, Section
44 304(a) as a distribution in redemption of the stock of a
46 corporation, for purposes of paragraphs B and C, the
48 corporation must be treated as purchasing an amount of its
stock equal to the amount treated as a distribution in
redemption of the stock of the corporation under the Code,
Section 304(a).

2 5. Aggregate gross assets. For purposes of determining
3 aggregate gross assets, the adjusted basis of any property
4 contributed to a corporation, or other property with a basis
5 determined in whole or in part by reference to the adjusted basis
6 of property so contributed, must be determined as if the basis of
7 the property contributed to the corporation immediately after the
8 contribution was equal to its fair market value as of the time of
9 the contribution.

10 6. Qualified trade or business. The following provisions
11 regarding a qualified trade or business apply.

12 A. For purposes of subsection 4, paragraph A, the
13 requirements of this subsection are met by a corporation for
14 any period if, during that period:

15 (1) At least 80% of the value of the assets of the
16 corporation are used by the corporation in the active
17 conduct of one or more qualified trades or businesses
18 in this State; and

19 (2) The corporation is an eligible corporation.

20 B. For purposes of paragraph A, assets used in the
21 following activities must be treated as used in the active
22 conduct of a qualified trade or business when, in connection
23 with a future qualified trade or business, a corporation
24 engages in:

25 (1) Start-up activities described in the Code, Section
26 195(c)(1)(A);

27 (2) Activities resulting in the payment or incurring
28 of expenditures that may be treated as research and
29 experimental expenditures under the Code, Section 174;
30 or

31 (3) Activities with respect to in-house research
32 expenses described in the Code, Section 41(b)(4).

33 A determination under this paragraph must be made without
34 regard to whether a corporation has a gross income from the
35 activities described in this paragraph at the time of that
36 determination.

37 C. For the purposes of this subsection:

38 (1) Stock and debt in a subsidiary corporation must be
39 disregarded and the parent corporation must be deemed
40 to own its ratable share of the subsidiary's assets and
41 liabilities.

2 to conduct its ratable share of the subsidiary's
3 activities;

4 (2) A corporation must be treated as failing to meet
5 the requirements of paragraph A for any period during
6 which more than 10% of the value of its assets in
7 excess of liabilities consists of stock or securities
8 in other corporations that are not subsidiaries of the
9 corporation, other than assets described in paragraph
10 D; and

11 (3) A corporation must be considered a subsidiary if
12 the parent owns more than 50% of the combined voting
13 power of all classes of stock entitled to vote, or more
14 than 50% in value of all outstanding stock, of the
15 corporation.

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17 D. For purposes of paragraph A, subparagraph (1), the
18 following assets must be treated as used in the active
19 conduct of a qualified trade or business:

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21 (1) Assets that are held as a part of the reasonably
22 required working capital needs of a qualified trade or
23 business of the corporation; and

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25 (2) Assets that are held for investment and are
26 reasonably expected to be used within 2 years to
27 finance research and experimentation in a qualified
28 trade or business or increases in working capital needs
29 of a qualified trade or business. For periods after
30 the corporation has been in existence for at least 2
31 years, in no event may more than 50% of the assets of
32 the corporation qualify as used in the active conduct
33 of a qualified trade or business for the purposes of
34 this paragraph.

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36 E. A corporation does not meet the requirements of
37 paragraph A for any period during which more than 10% of the
38 total value of its assets consists of real property that is
39 not used in the active conduct of a qualified trade or
40 business. For purposes of this paragraph, the ownership of,
41 dealing in or renting of real property does not constitute
42 active conduct of a qualified trade or business.

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44 F. For purposes of paragraph A, rights to computer software
45 that produces active business computer software royalties
46 within the meaning of the Code, Section 543(d)(1) must be
47 treated as an asset used in the active conduct of a trade or
48 business.

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2 G. A corporation does not meet the requirements of
4 paragraph A for any period during which more than 20% of the
corporation's total payroll expense is attributable to
employment located outside of the State.

6 7. **Converted stock.** If any stock in a corporation is
8 acquired solely through the conversion of other stock in the
10 corporation that is qualified small business stock in the hands
of the taxpayer, the following apply:

12 A. The stock so acquired must be treated as qualified small
business stock in the hands of the taxpayer; and

14 B. The stock so acquired must be treated as having been
16 held during the period during which the converted stock was
held.

18 8. **Pass-through entities.** Provisions regarding gross
20 income derived through pass-through entities are as follows.

22 A. If any amount included in gross income by reason of
24 holding an interest in a pass-through entity meets the
requirements of paragraph B, the following apply:

26 (1) The amount must be treated as gain described in
subsection 2; and

28 (2) For purposes of applying subsection 3, the amount
30 must be treated as gain from a disposition of stock in
32 the corporation issuing the stock disposed of by the
34 pass-through entity and the taxpayer's proportionate
share of the adjusted basis of the pass-through entity
in the stock must be taken into account.

36 B. An amount meets the requirements of this subsection if
the following apply:

38 (1) The amount is attributable to gain on the sale or
40 exchange by the pass-through entity of stock that is
42 qualified small business stock in the hands of the
44 entity, which is determined by treating the entity as
an individual, and that was held by that entity for
more than 5 years; and

46 (2) The amount is includable in the gross income of
48 the taxpayer by reason of the holding of an interest in
50 the entity that was held by the taxpayer on the date on
which the pass-through entity acquired the stock and at
all times thereafter before the disposition of the
stock by the pass-through entity.

2 C. Paragraph A does not apply to any amount to the extent
4 the amount exceeds the amount to which paragraph A would
6 have applied if the amount was determined by reference to
the interest the taxpayer held in the pass-through entity on
the date the qualified small business stock was acquired.

8 9. Transferred stock. For purposes of this section:

10 A. In the case of a transfer described in paragraph B, the
12 transferee must be treated as meeting the following:

14 (1) Having acquired the stock in the same manner as
16 the transferor; and

18 (2) Having held the stock during any continuous period
20 immediately preceding the transfer during which it was
22 held, or treated as held under this subsection, by the
24 transferor.

26 B. A transfer is subject to this subsection if the transfer
28 is:

30 (1) By gift;

32 (2) At death; or

34 (3) From a partnership to a partner of stock with
36 respect to which requirements similar to the
38 requirements of subsection 8 are met at the time of the
40 transfer without regard to the 5-year holding period
42 requirement.

44 C. The Bureau of Taxation shall adopt rules similar to the
46 rules of the Code, Section 1244(d)(2) to apply for purposes
48 of this section.

D. Other provisions regarding transferred stock are as
follows.

(1) In the case of a transaction described in the
Code, Section 351 or a reorganization described in the
Code, Section 368, if qualified small business stock is
exchanged for other stock that would not qualify as
qualified small business stock but for this paragraph,
the other stock must be treated as qualified small
business stock acquired on the date on which the
exchanged stock was acquired.

2 (2) This section applies to gain from the sale or
4 exchange of stock treated as qualified small business
6 stock by reason of subparagraph (1) only to the extent
8 of the gain that would have been recognized at the time
10 of the transfer described in subparagraph (1) if the
12 Code, Section 351 or 368 had not applied at that time.
14 This subparagraph does not apply if the stock that is
16 treated as qualified small business stock under
18 subparagraph (1) is issued by a corporation that, as of
20 the time of the transfer described in subparagraph (1),
22 is a qualified small business.

24 (3) For purposes of this paragraph, stock treated as
26 qualified small business stock under subparagraph (1)
28 must be so treated for subsequent transactions or
30 reorganizations, except that the limitation of
32 subparagraph (2) must be applied as of the time of the
34 first transfer to which the limitation applied, which
36 is determined after the application of subparagraph (1).

38 (4) In the case of a transaction described in the
40 Code, Section 351, this paragraph applies only if
42 immediately after the transaction the corporation
44 issuing the stock owns directly or indirectly stock
46 representing control, within the meaning of the Code,
48 Section 368(c), of the corporation whose stock was
50 exchanged.

10. Transfer of other property. For purposes of this
section:

A. When the taxpayer transfers property other than money or
stock to a corporation in exchange for stock in the
corporation, the following apply:

(1) The stock must be treated as having been acquired
by the taxpayer on the date of the exchange; and

(2) The basis of the stock in the hands of the
taxpayer may not be less than the fair market value of
the property exchanged; and

B. If the adjusted basis of any qualified small business
stock is adjusted by reason of any contribution to capital
after the date on which the stock was originally issued, in
determining the amount of the adjustment by reason of the
contribution, the basis of the contributed property may not
be treated as less than its fair market value on the date of
the contribution.

11. Short position.

2 A. If the taxpayer has an offsetting short position with
4 respect to any qualified small business stock, subsection 2
does not apply to any gain from the sale or exchange of the
6 stock unless:

8 (1) The stock was held by the taxpayer for more than 5
10 years as of the first day on which there was such a
short position; and

12 (2) The taxpayer elects to recognize gain as if the
14 stock was sold on that first day for its fair market
value.

16 B. For purposes of paragraph A, the taxpayer must be
18 treated as having an offsetting short position with respect
to any qualified small business stock if:

20 (1) The taxpayer has made a short sale of
substantially identical property;

22 (2) The taxpayer has acquired an option to sell
24 substantially identical property at a fixed price; or

26 (3) To the extent provided in rules, the taxpayer has
28 entered into any other transaction that substantially
30 reduces the risk of loss from holding the qualified
32 small business stock. For purposes of this
subparagraph, "taxpayer" is deemed to include a person
who is related, within the meaning of the Code, Section
267(b) or 707(b), to the taxpayer.

34 12. Rulemaking. The State Tax Assessor may adopt rules as
36 appropriate to carry out the purposes of this section, including
rules to prevent the avoidance of the purposes of this section
through split-ups, shell corporations, partnerships or otherwise.

38 13. Application. This section applies to tax years
40 beginning on or after January 1, 1995.

42 STATEMENT OF FACT

44 This bill establishes a small business investment credit
46 modeled after California law.

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50 This document has not yet been reviewed to determine the
52 need for cross-reference, stylistic and other technical
amendments to conform existing law to current drafting standards.