

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 1997

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HOUSE BILL 987

Short Title: Venture Capital Investment Incentive.

(Public)

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Sponsors: Representatives Wilkins, Cansler, Dickson (Cosponsors); Arnold, Baddour, Berry, Brown, Buchanan, Carpenter, Clary, Cole, Crawford, Goodwin, Hall, Hardaway, Hill, Hurley, Ives, Kiser, McCrary, McMahan, Miner, Mitchell, Redwine, Reynolds, Saunders, Sexton, Thompson, Tolson, Wainwright, and Wright.

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Referred to: Insurance, if favorable, Finance.

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April 17, 1997

A BILL TO BE ENTITLED

AN ACT TO STIMULATE A SUBSTANTIAL INCREASE IN VENTURE CAPITAL INVESTMENTS IN NORTH CAROLINA BY ALLOWING AN INSURANCE PREMIUMS TAX CREDIT FOR THESE INVESTMENTS.

The General Assembly of North Carolina enacts:

Section 1. G.S. 53A-35 through G.S. 53A-37 are designated Part 1 of Article 3 of Chapter 53A of the General Statutes, entitled "General Provisions" and the remainder of Article 3 of Chapter 53A of the General Statutes is designated Part 2, entitled "North Carolina Enterprise Corporations".

Section 2. Article 3 of Chapter 53A of the General Statutes, as amended by this act, is further amended by adding a new Part to read:

**"PART 3. CERTIFIED NORTH CAROLINA CAPITAL COMPANIES.**

**"§ 53A-70. Requirements for certification of a certified North Carolina capital company.**

(a) Initial Certification. – In order to be initially certified as a certified North Carolina capital company, a company must satisfy the following requirements:

- 1           (1) It is a partnership, corporation, trust, or limited liability company,  
2 whether for-profit or nonprofit, whose primary business activity is the  
3 investment of cash in approved business ventures.
- 4           (2) Its cash, marketable securities, and other liquid assets equal at least five  
5 hundred thousand dollars (\$500,000).
- 6           (3) Its officers and its board of directors, partners, trustees, or managers are  
7 thoroughly acquainted with the requirements of this Part.
- 8           (4) No insurance company or affiliate of an insurance company is a  
9 managing general partner of the certified North Carolina capital  
10 company or controls the direction of investments of the certified North  
11 Carolina capital company. This subdivision does not preclude an  
12 insurance company or any other party from exercising its legal rights  
13 and remedies, which may include interim management of a certified  
14 North Carolina capital company, in the event that a certified North  
15 Carolina capital company is in default of its statutory obligations or its  
16 contractual obligations to the insurance company or other party.
- 17       (b) Continuing Certification. – To remain certified as a certified North Carolina  
18 capital company, the company must satisfy the following requirements:
- 19           (1) Within three years after the date it was initially certified, at least thirty  
20 percent (30%) of the certified capital invested in the company must be  
21 placed in approved investments.
- 22           (2) Within five years after the date it was initially certified, at least fifty  
23 percent (50%) of the certified capital invested in the company must be  
24 placed in approved investments.
- 25           (3) It shall not invest in a single approved business venture an amount that  
26 is more than fifteen percent (15%) of the total certified capital under the  
27 company's management at the time of the investment.
- 28           (4) No insurance company or affiliate of an insurance company is a  
29 managing general partner of the certified North Carolina capital  
30 company or controls the direction of investments of the certified North  
31 Carolina capital company. This subdivision does not preclude an  
32 insurance company or any other party from exercising its legal rights  
33 and remedies, which may include interim management of a certified  
34 North Carolina capital company, in the event that a certified North  
35 Carolina capital company is in default of its statutory obligations or its  
36 contractual obligations to the insurance company or other party.
- 37       (c) Permanent Certification. – A certified North Carolina capital company that has  
38 satisfied the requirements of G.S. 53A-70(b) and has invested all of its certified capital in  
39 approved investments, as demonstrated by its most recent financial statement and report  
40 filed in accordance with G.S. 53A-71, qualifies for permanent certification and is no  
41 longer required to obtain continuing certification as required in G.S. 53A-71. A certified  
42 North Carolina capital company that has qualified for permanent certification must

1 continue to submit annual financial statements and reports under G.S. 53A-71 for three  
2 years after it qualifies for permanent certification.

3 **"§ 53A-71. Procedure for initial and continuing certification; reports.**

4 (a) Initial Certification. – In order to be initially certified as a certified North  
5 Carolina capital company, a company must file an application with the Department and  
6 pay the initial certification fee. The application shall include any information and  
7 supporting documents required by the Secretary of State to determine whether the  
8 company qualifies for initial certification. Within 60 days after an application is filed, the  
9 Department shall determine whether the applicant qualifies for initial certification and  
10 shall either issue the certification or shall refuse the certification and notify the applicant  
11 in detail of the grounds for the refusal, including suggestions for the removal of those  
12 grounds.

13 The Department shall review and approve or reject applications in the order  
14 submitted. If more than one application is received by the Department on the same day,  
15 all applications received on that day shall be reviewed and approved simultaneously,  
16 except in the case of incomplete applications or applications for which additional  
17 information is requested by the Department and is not supplied by the applicant within  
18 the allowable time limits established by the Department. If more than one applicant is  
19 certified on the same day, the Department shall ensure that all applicants certified on that  
20 day are notified of certification at the same time.

21 (b) Continuing Certification. – A certified North Carolina capital company that has  
22 not qualified for permanent certification must, in order to remain certified, submit an  
23 annual application for continued certification and pay the annual review fee. The request  
24 shall include any information and supporting documents required by the Secretary of  
25 State to determine whether the company qualifies for continued certification.

26 The Department shall conduct an annual review of each certified North Carolina  
27 capital company that has not qualified for permanent certification to determine if the  
28 company is in compliance with the requirements for initial and continuing certification  
29 and to ensure that the company's investments are in compliance with this Part. The  
30 review shall be based upon the company's financial statements and other information  
31 submitted in accordance with this section.

32 (c) Application Forms; Fees. – Applications for initial and continuing certification  
33 under this section shall be in the form required by the Secretary of State. The Secretary  
34 of State shall prepare blank forms for the applications. Each application shall be signed  
35 by the owners, a manager, or an executive officer of the company. There shall be  
36 annexed to the application the affirmation of the person making the application in the  
37 following form: 'Under penalties prescribed by law, I certify and affirm that to the best  
38 of my knowledge and belief this application is true and complete.' A person who submits  
39 a false application is guilty of a Class 1 misdemeanor.

40 The Secretary of State shall charge an applicant a fee of one thousand dollars (\$1,000)  
41 for initial certification as a certified North Carolina capital company and a fee of one  
42 thousand dollars (\$1,000) for annual review for continuing certification as a certified

1 North Carolina capital company. Fees collected under this section shall be applied to the  
2 cost of administering this Part.

3 (d) Periodic Reports. – Each certified North Carolina capital company shall  
4 provide the Department an annual audited financial statement and report that includes an  
5 opinion of an independent certified public accountant. The audit shall address the  
6 methods of operation and conduct of the business of the company to determine whether  
7 the company has complied with this Part and whether the cash invested in the company  
8 has been invested as required by this Part. The audit shall also determine whether each  
9 business in which the company has invested is an approved business venture as defined in  
10 this Article. In addition, each certified North Carolina capital company shall provide the  
11 Department a midyear, unaudited update of its annual financial statement and report. The  
12 reports and updates shall be in the form prescribed by the Secretary of State and shall  
13 include any information required by the Secretary of State about the company and about  
14 the approved business ventures in which it has invested.

15 A certified North Carolina capital company that has not qualified for permanent  
16 certification shall submit the annual financial statement and report and the midyear  
17 update on the due dates specified by the Department. A certified North Carolina capital  
18 company that has qualified for permanent certification is no longer required to submit  
19 midyear updates but shall continue to submit the annual financial statement and report on  
20 the due dates specified by the Department for three years after the company qualifies for  
21 permanent certification. Thereafter, no additional financial statements and reports are  
22 required under this subsection.

23 **"§ 53A-72. Distributions; maximum interest rate.**

24 (a) Distributions. – A certified North Carolina capital company may make  
25 qualified distributions at any time. A certified North Carolina capital company may,  
26 without restriction, make distributions and payments to debt holders with respect to debt  
27 owed them by the company, but no distributions or payments may be made to an equity  
28 holder, or any of its affiliates, that is entitled to a credit under Article 8C of Chapter 105  
29 of the General Statutes until the certified North Carolina capital company has qualified  
30 for permanent certification. A certified North Carolina capital company may make other  
31 distributions only after it has qualified for permanent certification.

32 (b) Maximum Interest Rate. – A certified North Carolina capital company shall not  
33 charge interest on a senior, secured loan at an annual rate that exceeds the prime rate plus  
34 three percent (3%).

35 **"§ 53A-73. Tax credits.**

36 (a) Credit Allowed. – A person who invests cash in a certified North Carolina  
37 capital company is entitled to a tax credit as provided in Article 8C of Chapter 105 of the  
38 General Statutes but, notwithstanding the provisions of Division V of Article 4 of  
39 Chapter 105 of the General Statutes, is not allowed a tax credit under that Division for the  
40 investment. In addition, notwithstanding the provisions of Division V of Article 4 of  
41 Chapter 105 of the General Statutes, a certified North Carolina capital company is not  
42 allowed a tax credit under that Division for its investments.

1       (b) Allocation of Credits. – The Department shall allocate the total amount of  
2 credit allowed pursuant to G.S. 105-228.10E among taxpayers as provided in this section.  
3 A certified North Carolina capital company may apply for allocation of credits on behalf  
4 of its investors no earlier than the first business day after it is certified. The application  
5 shall be in the form required by the Secretary of State and shall provide all of the  
6 following:

7           (1) The name of each investor.

8           (2) The amount each investor has committed to invest in the company.

9           (3) Proof that the investor has committed to invest the funds subject to  
10 allocation of the applicable credits pursuant to this section.

11           (4) The maximum amount of credit the investment would entitle the  
12 investor to under G.S. 105-228.10C for the current taxable year and the  
13 following nine taxable years.

14           (5) Any other information required by the Secretary of State.

15       Upon receipt of a completed application, the Department shall determine the amount  
16 of available credit not yet allocated for each taxable year specified in the application.  
17 Within seven business days after receipt of the application, the Department shall allocate  
18 to the North Carolina capital company, on behalf of the investors named in the  
19 application, the total amount of credit applied for in the application, but only to the extent  
20 of available credit not yet allocated for each taxable year. The Department's allocations  
21 of credit under this section shall be in writing.

22       The Department shall allocate available credit to applicants in the order the  
23 applications are received. If more than one certified North Carolina capital company  
24 submits a completed application on the same day, the Department shall make the  
25 allocations to those applicants simultaneously. If the amount of credit applied for in the  
26 simultaneous applications exceeds the amount of available credit not yet allocated for a  
27 taxable year, the Department shall allocate the available credit for that taxable year  
28 among the simultaneous applicants on a pro rata basis in proportion to the amount of  
29 credit applied for by each.

30 **"§ 53A-74. Decertification of certified North Carolina capital company.**

31       (a) Grounds for Decertification. – Any material violation of this Part shall be  
32 grounds for decertification under this section.

33       (b) Procedure for Decertification. – If the Department determines that a certified  
34 North Carolina capital company is not in compliance with any requirement for continuing  
35 certification, it shall, by written notice, inform the officers of the company and the board  
36 of directors, manager, trustees, or general partners that the company will be decertified in  
37 120 days after the date the notice is mailed unless the company corrects the deficiencies  
38 to bring itself in compliance with the requirements for certification. At the end of the  
39 120-day grace period, if the certified North Carolina capital company is still not in  
40 compliance, the Department shall decertify the company and send a notice of  
41 decertification to the company and to the Department of Revenue and the Department of  
42 Insurance.

1 (c) Effect of Decertification. – If a certified North Carolina capital company is  
2 decertified, no further tax credits for an investment in the company are allowed pursuant  
3 to G.S. 105-228.10D.

4 **"§ 53A-75. Rules; report.**

5 The Secretary of State may adopt rules to implement this Part. The Secretary of State  
6 shall report to the Legislative Research Commission by October 1 of each odd-numbered  
7 year and by February 1 of each even-numbered year the number of certified North  
8 Carolina capital companies certified under this Part, the date each company was created,  
9 the amount and percentage of certified capital invested by each company, the amount of  
10 tax credits allocated to each company, and any other information requested by the  
11 Legislative Research Commission."

12 Section 3. G.S. 53A-37 reads as rewritten:

13 **"§ 53A-37. Definitions.**

14 The following definitions apply in this Article:

15 (1) Affiliate of a certified North Carolina capital company or insurance  
16 company. – Any of the following:

17 a. A person who directly or indirectly beneficially owns (whether  
18 through rights, options, convertible interests, or otherwise),  
19 controls, or holds power to vote ten percent (10%) or more of the  
20 outstanding voting securities or other ownership interests of the  
21 company.

22 b. A person ten percent (10%) or more of whose outstanding voting  
23 securities or other ownership interests are, directly or indirectly,  
24 beneficially owned (whether through rights, options, convertible  
25 interests, or otherwise), controlled or held with power to vote by  
26 the company.

27 c. A person who directly or indirectly controls, is controlled by, or  
28 is under common control with the company.

29 d. A partnership in which the company is a general partner.

30 e. A person who is an officer, a director, or an agent of the  
31 company, or is an immediate family member of an officer, a  
32 director, or an agent of the company.

33 (2) Approved business venture. – A business that satisfies all of the  
34 following conditions as of the time of a certified North Carolina capital  
35 company's first investment in the business:

36 a. It is headquartered in this State, it operates primarily in this State  
37 or does substantially all of its production in this State, and it  
38 employs a majority of its employees in this State.

39 b. It has no more than 300 employees and, during its most recent  
40 fiscal year, it had gross revenues of no more than seven million  
41 dollars (\$7,000,000) on a consolidated basis as determined in  
42 accordance with generally accepted accounting principles.

43 c. It is not a subsidiary of another corporation.

- 1           d.     It satisfies the conditions established in G.S. 105-163.013(b)(3)  
2                 through (6).
- 3           (3)   Approved investment. – The investment of cash by a certified North  
4                 Carolina capital company in such a manner as to acquire capital in a  
5                 business that, at the time of the first investment in the business by a  
6                 certified North Carolina capital company, was an approved business  
7                 venture. The capital acquired may be any debt, equity, or hybrid  
8                 security, whether secured or unsecured, of any nature, including a debt  
9                 instrument or security that has the characteristics of debt but provides  
10                for conversion into equity or equity participation instruments such as  
11                options or warrants.
- 12           (4)   Business. – A corporation, a partnership, an association, a limited  
13                 liability company, or a sole proprietorship operated for profit.
- 14           (5)   Certified capital. – The cash invested in a certified North Carolina  
15                 capital company, either in the form of equity or debt capital, during the  
16                 365-day period after the company has been initially certified as  
17                 provided in Part 3 of this Article. If the certified capital is in the form of  
18                 debt capital, the debt instrument issued by the certified North Carolina  
19                 capital company, at par value or a premium, must have an original  
20                 maturity date of at least five years after the date of issuance and a  
21                 repayment schedule that is no faster than a level principal amortization.
- 22           (6)   Certified North Carolina capital company. – A partnership, corporation,  
23                 trust, or limited liability company whose primary business activity is the  
24                 investment of cash in approved business ventures and that is certified by  
25                 the Secretary of State as provided in Part 3 of this Article.
- 26           (7)   Department. – The Department of the Secretary of State.
- 27           (2)    (8)    Equity security. – Common stock, preferred stock, an interest  
28                         in a partnership, subordinated debt, or a warrant that is convertible  
29                         into, or entitles the holder to receive upon its exercise, common stock,  
30                         preferred stock, or an interest in a partnership.
- 31           (9)    Insurance company. – Defined in G.S. 58-1-5.
- 32           (3)    (10)   Mezzanine finance. – An investment in the equity securities  
33                         or subordinated debt of a Qualified North Carolina Business.
- 34           (11)   Person. – An individual, a corporation, a partnership, an association, a  
35                 trust, a limited liability company, or another legal entity.
- 36           (12)   Qualified distribution. – A distribution or payment to equity owners of a  
37                 certified North Carolina capital company or to their shareholders,  
38                 officers, directors, partners, members, managers, employees, or  
39                 affiliates, in connection with any of the following:
- 40                 a.     Reasonable costs and expenses of forming, syndicating,  
41                         managing, and operating the company, including management  
42                         fees.

b. An increase in State or federal taxes, penalties, or interest of the company's equity owners to the extent the increase relates to the ownership, management, or operation of the company.

(4) (13) Qualified North Carolina Business. – A business whose headquarters and principal business operations are located in North Carolina and which, together with its affiliates on a consolidated basis, had gross income during the immediately preceding fiscal year, determined in accordance with generally accepted accounting principles without taking into account extraordinary items, of less than forty million dollars (\$40,000,000).

(5) (14) Rural areas. – Any county in North Carolina which does not include within its boundaries a city, as defined by G.S. 160A-1(2), with a population greater than one percent (1%) of the population of North Carolina.

(6) (15) Security. – A security as defined in G.S. 78A-2(11).

(7) (16) Subordinated debt. – Indebtedness that is or will be subordinated to other indebtedness of the issuer. Subordinated debt may be convertible into common stock, preferred stock, or an interest in a partnership.

(8) (17) Traditional ~~Financial Institutions.~~ financial institutions. – Corporations or associations chartered under ~~Chapters~~ Chapter 53 or 54B of the General Statutes."

Section 4. Chapter 105 of the General Statutes is amended by adding a new Article to read:

**"ARTICLE 8C.**

**"PREMIUMS TAX CREDIT FOR INVESTMENTS IN  
NORTH CAROLINA SMALL BUSINESSES.**

**"§ 105-228.10A. Purpose.**

The purpose of this Article is to stimulate a substantial increase in venture capital investments in North Carolina by providing an incentive for insurance companies to invest in certified North Carolina capital companies.

**"§ 105-228.10B. Definitions.**

The following definitions apply in this Article:

(1) Certified capital. – Defined in G.S. 53A-37.

(2) Certified North Carolina capital company. – A certified North Carolina capital company created under Article 3 of Chapter 53A of the General Statutes.

**"§ 105-228.10C. Premiums tax credit for investments.**

(a) Credit. – A person who invests certified capital in a certified North Carolina capital company is allowed against the gross premiums tax imposed by G.S. 105-228.5 and G.S. 105-228.8 a credit equal to the amount of certified capital invested by the taxpayer during the taxable year, subject to the limitations provided in this Article. To claim the credit allowed by this section, the taxpayer must provide the Secretary a copy



1 of the certified North Carolina capital company's application for allocation of credit under  
2 G.S. 53A-73, a copy of the Secretary of State's written allocation of credit under G.S.  
3 53A-73, and any other supporting documentation the Secretary requires.

4 (b) Limitations. – The taxpayer may not take the entire credit for the taxable year  
5 the investment is made, but may take up to ten percent (10%) of the aggregate credit  
6 allowed under this section for that taxable year and for each succeeding taxable year until  
7 the entire credit has been used. The amount of credit taken may not exceed the taxpayer's  
8 gross premiums tax liability for a taxable year reduced by the sum of all credits allowable  
9 except payments of tax by or on behalf of the taxpayer. Subject to the ten percent (10%)  
10 limitation, any unused portion of the credit may be carried forward to the five succeeding  
11 taxable years.

12 (c) Transfer of Credit. – A taxpayer may transfer a credit allowed under this  
13 section to another taxpayer. The taxpayer must apply for the approval of the  
14 Commissioner of Insurance before transferring the credit. The application shall be in the  
15 form prescribed by the Commissioner. The application shall identify the proposed  
16 transferor and transferee, state the transferor's tax credit balance before and after the  
17 proposed transfer, state the amount of the credit to be transferred and the proposed date of  
18 the transfer, and include any other information the Commissioner requires regarding the  
19 proposed transfer.

20 The Commissioner of Insurance shall approve the proposed transfer if the application  
21 is accurate and complete and the Commissioner determines that the proposed transfer will  
22 not have an adverse effect on either taxpayer or their policyholders or shareholders.  
23 Within 60 days after receiving an application, the Commissioner shall notify the  
24 applicant that the proposed transfer has been approved or disapproved.

25 The Commissioner of Insurance shall maintain records and monitor all transferred  
26 credits to ensure that transfers do not result in multiple parties claiming the same credit.  
27 The Commissioner shall provide the Secretary complete records of all transferred credits.  
28 **"§ 105-228.10D. Effect of decertification.**

29 If a certified North Carolina capital company is decertified under G.S. 53A-74, no tax  
30 credit or carryforward of a tax credit for an investment in the company is allowed under  
31 this Article for a taxpayer's taxable year beginning in the calendar year the decertification  
32 occurred or for subsequent taxable years. Decertification of a certified North Carolina  
33 capital company does not affect a tax credit allowed under this Article for a taxpayer's  
34 taxable year that began before the calendar year in which the decertification occurred.

35 **"§ 105-228.10E. Annual ceiling; cap.**

36 (a) Annual Ceiling. – The total amount of tax credits that may be taken by all  
37 taxpayers under this Article in a taxable year may not exceed fifteen million dollars  
38 (\$15,000,000). This amount shall be allocated among taxpayers for each taxable year as  
39 provided in G.S. 53A-73.

40 (b) Cap. – The amount of credit allowed a taxpayer under this Article for a taxable  
41 year may not exceed ten percent (10%) of the annual ceiling for that year."

42 Section 5. G.S. 105-228.8(e) reads as rewritten:



1 from creating jobs that would otherwise enhance the economy of the State and provide  
2 livelihoods for North Carolina citizens.

3 (b) The General Assembly finds ~~and declares further~~ that private enterprise and  
4 existing federal and State governmental programs have not adequately alleviated the  
5 severe shortage of mezzanine finance capital and credit available for investments in ~~rural~~  
6 ~~areas in the~~ this State.

7 (c) The General Assembly finds ~~and declares~~ that it is a matter of grave public  
8 necessity that North Carolina Enterprise Corporations be authorized to be created and ~~to~~  
9 ~~be~~ empowered to alleviate these severe shortages of mezzanine finance capital and credit  
10 for investment in rural areas of the State. North Carolina Enterprise Corporations shall  
11 help eliminate barriers to rural economic development by providing mezzanine finance  
12 capital and credit, and other types of financing as appropriate, to businesses in rural areas  
13 that have been unable to obtain sufficient financing through traditional financial  
14 institutions.

15 (d) The General Assembly finds that it is a matter of grave public necessity that  
16 certified North Carolina capital companies be authorized to be created as venture capital  
17 companies whose primary business activity is the investment of cash in small North  
18 Carolina business ventures that are in need of capital for survival, expansion, new  
19 product development, or similar purposes."

20 Section 11. G.S. 53A-38(a) reads as rewritten:

21 "(a) One or more persons, a majority of whom are residents of this State, may, by  
22 filing a certificate of incorporation as provided in subsection (b), incorporate a North  
23 Carolina Enterprise Corporation under the provisions of this ~~Article-Part.~~"

24 Section 12. G.S. 53A-41 reads as rewritten:

25 "**§ 53A-41. Governing law.**

26 Except as otherwise provided in this ~~Article-Part,~~ a North Carolina Enterprise  
27 Corporation shall be governed by Chapter 55 of the General Statutes."

28 Section 13. G.S. 53A-42 reads as rewritten:

29 "**§ 53A-42. Powers.**

30 A North Carolina Enterprise Corporation created under this ~~Article-Part~~ shall have all  
31 the powers conferred on business corporations by Chapter 55 of the General Statutes."

32 Section 14. Sections 4, 5, and 6 of this act and G.S. 53A-73, as enacted by  
33 Section 2 of this act, become effective for taxable years beginning on or after January 1,  
34 1997, and apply to investments made on or after that date. The remainder of this act is  
35 effective when this act becomes law. An application for initial certification as a North  
36 Carolina capital company pursuant to G.S. 53A-71 may not be submitted until the first  
37 Monday that falls at least 45 days after this act becomes law. G.S. 53A-73 and Article  
38 8C of Chapter 105 of the General Statutes, as enacted by this act, are repealed effective  
39 for investments made on or after January 1, 2000.