

QUALIFIED EQUITY AND SUBORDINATED DEBT INVESTMENTS TAX CREDIT

**23 VAC 10-110-225 Qualified Equity and Subordinated Debt Investments Tax Credit.**

23 VAC 10-110-225 Qualified Equity and Subordinated Debt Investments Tax Credit; Definitions.

The following words and terms, when used in this regulation, shall have the following meaning, unless the context clearly indicates otherwise:

"Equity" means common stock or preferred stock, regardless of class or series, of a corporation; a partnership interest in a limited partnership; or a membership interest in a limited liability company, any of which is not required or subject to an option on the part of the taxpayer to be redeemed by the issuer within five years from the date of issuance.

"Family member" means spouse, child, grandchild, parent, sibling or any other person who is related to the taxpayer by blood, marriage, or adoption.

"Primarily engaged in business in the Commonwealth" means 50% or more of the entity's gross receipts are derived from sources within Virginia.

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"Qualified business" means a business which (i) has annual gross revenues of no more than five million dollars in its most recent tax year, (ii) is commercially domiciled in the Commonwealth, (iii) is primarily engaged in business or does substantially all of its production in the Commonwealth, and (iv) is not primarily engaged, or is not primarily organized to engage, in any of the following types of businesses:

1. Banks;
2. Savings and loan institutions;
3. Credit or finance;
4. Financial, broker or investment;
5. Businesses organized for the primary purpose of rendering professional services as defined in Chapter 7 (§ 13.1-542 et seq.) of Title 13.1;
6. Accounting;
7. Government, charitable, religious or trade institutions or organizations;
8. Conventional coal, oil and gas, and mineral exploration;
9. Insurance;
10. Real estate design or engineering;
11. Construction or construction contracting;
12. Business consulting or business brokering;

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13. Residential housing, real estate brokerage, sale or leasing businesses, or real estate development; or

14. Any business which is in violation of the law.

"Qualified investment" means a cash investment in a qualified business in the form of equity or subordinated debt. An investment shall not be qualified, however, if the taxpayer who holds such investment, or any of such taxpayer's family members, or any entity affiliated with such taxpayer, receives or has received compensation from the qualified business in exchange for services provided to such business as an employee, officer, director, manager, independent contractor or otherwise in connection with or within one year before or after the date of such investment. For purposes hereof, reimbursement of reasonable expenses incurred shall not be deemed to be compensation. A qualified investment shall not include existing investments or instruments that have been purchased, transferred, or otherwise obtained without providing new capital to a qualified business.

"Subordinated debt" means indebtedness of a corporation, general or limited partnership, or limited liability company that (i) by its terms requires no repayment of principal for the first three years after issuance; (ii) is not guaranteed by any other

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person or entity, or secured by any assets of the issuer or any other person or entity; and (iii) is subordinated to all indebtedness and obligations of the issuer to national or state-chartered banking or savings and loan institutions.

"Substantially all of its production in the Commonwealth" means 80% or more of the entity's expenses are incurred within Virginia.

23 VAC 10-110-226 Qualified Equity and Subordinated Debt Investments Tax Credit; General Credit Provisions.

A. For taxable years beginning on or after January 1, 1999, a taxpayer shall be allowed a credit against the taxes imposed by Articles 2 (Individual Income Tax; § 58.1-320 et seq.) and 6 (Taxation for Estates and Trusts; § 58.1-360 et seq.) of Chapter 3 of Title 58.1 of the Code of Virginia in an amount equal to 50% of such taxpayer's qualified investments made during such taxable year.

B. The amount of any credit attributable to a qualified investment by a partnership, electing small business corporation (S corporation), or limited liability company shall be allocated to the individual partners, shareholders, or members, as they may determine.

C. The aggregate amount of the credit that may be used by any taxpayer per taxable year shall not exceed the lesser of (i) the tax imposed for such taxable year or (ii) \$50,000. The credit is not refundable and may not be carried back. Any credit, or portion thereof, not usable for the taxable year in which the credit was allowed may be, to the extent usable, carried over for the next fifteen succeeding taxable years or until the total amount of the tax credit has been taken, whichever occurs first.

D. The total amount of tax credits available for the Commonwealth's fiscal year shall not exceed \$5 million. In the event that the total eligible credit requests exceed the Commonwealth's annual fiscal limitation, each taxpayer shall be granted a pro rata amount as determined by the department. The amount of such prorated credit shall be determined by multiplying a fraction, the numerator of which shall be the credit requested by the eligible taxpayer for such year, and the denominator of which shall be the total credits requested by all eligible taxpayers for such taxable year, to the Commonwealth's annual fiscal limitation of \$5 million.

23 VAC 10-110-227 Qualified Equity and Subordinated Debt Investments Tax Credit; Qualified Business Application Procedure.

A. Every eligible entity desiring to be designated as a qualified business for purposes of this tax credit must make an application to the department. Such

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application must be made prior to the issuance of any equity or subordinated debt; otherwise, the issuance shall not qualify for the tax credit.

1. A qualified business application must be made at least 90 days prior to the issuance of any equity or subordinated debt to ensure that the department's determination regarding the entity's qualification will be made prior to the issuance date.

2. A qualified business application may be made less than 90 days prior to the issuance of any equity or subordinated debt; however, the department cannot ensure that its determination regarding the entity's qualification will be made prior to the issuance date.

3. A qualified business application will not be accepted after the issuance date of any equity or subordinated debt, except for issuances made between January 1, 1999 and before September 1, 1999, for which applications must be made by October 1, 1999. For issuances of equity or subordinated debt made on September 1, 1999 and thereafter, qualified business applications must be made prior to the issuance date as described in paragraphs A 1 and A 2 above. For example, issuances made on September 1, 1999, will require a qualified business application no later than June 1, 1999, to ensure that the department's determination will be made prior to the issuance date.

B. The entity shall supply all information and supporting documentation the department deems necessary to properly determine whether the entity is a qualified business. Such information shall include, but shall not be limited to, the following:

1. The amount of annual gross revenues from its most recent tax year.
2. The entity's state of commercial domicile as defined in 23 VAC 10-120-140 D.
3. The state in which the entity either (i) is primarily engaged in business or (ii) does substantially all of its production.
4. The type of business in which the entity is primarily engaged or primarily organized to engage. The same method used to answer paragraph 3 shall be used in answering this paragraph.

C. If the department determines the entity is a qualified business, the department shall issue a certificate to the entity stating the same. Such designation shall be valid only for the calendar year of issuance.

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D. Upon issuance of equity or subordinated debt to taxpayers, the qualified business shall issue a statement to each taxpayer for attachment to the taxpayer's tax credit application. Such statement shall contain the following information:

1. A copy of the qualified business certification granted by the department.
2. The type of investment at issue (i.e. equity or subordinated debt) and the amount.
3. That the investment at issue meets the definition of a qualified investment for purposes of this credit.
  - a. If the investment at issue is equity, the statement must also indicate that such issuance is an original issuance which provides new capital to the qualified business, and that it is not required or subject to an option on the part of the taxpayer to be redeemed by the issuer within five years from the date of issuance.
  - b. If the investment at issue is subordinated debt, the statement must also indicate that such issuance is an original issuance which provides new capital to the qualified business, and that (i) by its terms requires no repayment of principal for the first three years after issuance; (ii) is not guaranteed by any other person or entity, or secured by any assets of the issuer or any other person or entity; and (iii) is subordinated to all indebtedness and obligations of the issuer to national or state-chartered banking or savings and loan institutions.

23 VAC 10-110-228 Qualified Equity and Subordinated Debt Investments Tax Credit; Tax Credit Application Procedure.

A. Eligible taxpayers who qualify for the equity and subordinated debt investment tax credit must make an application to the department.

1. For eligible taxpayers using the 1999 calendar year as their taxable year, an application and supporting documentation requesting the tax credit must be submitted no later than April 1, 2000.
2. For taxable years ending after December 31, 1999, and before January 1, 2001, eligible taxpayers must submit an application and supporting documentation requesting the tax credit no later than April 1, 2001.
3. For taxable years thereafter, for any taxable year that ends after January 1, and on or before December 31, eligible taxpayers must submit an application and

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supporting documentation requesting the tax credit no later than April 1 of the subsequent calendar year.

B. The department shall review all applications for completeness and notify taxpayers of any errors no later than June 1. Taxpayers must fully respond to any such notices no later than June 15.

C. All eligible taxpayers shall be notified by June 30 as to the amount of applicable tax credit that may be claimed for the taxable year for which the request was made.

D. Applications must be made on forms prescribed by the department and either hand delivered by the date specified in this section or sent by certified mail with a return receipt requested and post marked no later than the date specified in this section.

E. Each taxpayer shall timely supply all information the department deems necessary to properly determine the allowable credit amount. Such information shall include, but shall not be limited to, the following:

1. A copy of the statement issued by the qualified business pursuant to section 23 VAC 10-110-227 D.

2. The taxable year during which the qualified investment was made.

3. The name, address, federal identification number, and Virginia account number of the taxpayer.

4. A certification by the taxpayer, under penalty of perjury, that the qualified investment meets all conditions outlined in § 58.1-339.4 of the Code of Virginia and these regulations.

5. In the case of a partnership, electing small business corporation (S corporation), or limited liability company, the application shall include the name, address, social security number, and allocable credit amount for each of its individual partners, shareholders, or members. Notification of the allowable credit amount shall be sent to the entity, and a copy of such notification shall be attached to each individual taxpayer's Virginia income tax return on which the credit is claimed.

F. Eligible taxpayers who will not receive the final certification of their credits prior to the due date of their individual state income tax returns must either file the appropriate return extension request or amend their return after receiving a credit

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certification. Amended returns to claim the tax credit must be filed within the applicable statute of limitations.

23 VAC 10-110-229 Qualified Equity and Subordinated Debt Investments Tax Credit; Required Equity Holding Period.

A. Equity received in connection with a qualified business investment must be held by the taxpayer for at least five full calendar years following the calendar year for which a tax credit for a qualified investment is allocated except in any of the following instances: (i) the liquidation of the qualified business issuing such equity, (ii) the merger, consolidation or other acquisition of such business with or by a party not affiliated with such business, or (iii) the death of the taxpayer.

B. If the five calendar year holding period requirement is not met, the taxpayer shall immediately notify the department and forfeit all used and unused tax credits. The forfeiture of all used credits shall be deemed a tax assessment, to which the department shall add a penalty equal to the amount of the used credits. In addition thereto, interest on the outstanding tax and penalty shall be assessed at the rate of one percent per month, compounded monthly, from the date the tax credits were claimed by the taxpayer.



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C. Upon written request, the department shall have the discretion to abate any assessed penalty, in full or in part, if the taxpayer establishes reasonable cause for the failure to hold such equity for the five calendar year holding period. The reason for any such abatement shall be preserved among the records of the department.