

110TH CONGRESS  
1ST SESSION

# H. R. 578

To amend the Internal Revenue Code of 1986 to allow a credit against income tax for qualified equity investments in certain small businesses.

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## IN THE HOUSE OF REPRESENTATIVES

JANUARY 19, 2007

Mr. POMEROY (for himself, Mr. MANZULLO, Mr. SOUDER, Mr. MOORE of Kansas, and Mr. BARTLETT of Maryland) introduced the following bill; which was referred to the Committee on Ways and Means

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## A BILL

To amend the Internal Revenue Code of 1986 to allow a credit against income tax for qualified equity investments in certain small businesses.

1 *Be it enacted by the Senate and House of Representa-*  
2 *tives of the United States of America in Congress assembled,*

3 **SECTION 1. SHORT TITLE.**

4 This Act may be cited as the “Access to Capital for  
5 Entrepreneurs Act of 2007”.

6 **SEC. 2. EQUITY INVESTMENT IN SMALL BUSINESS TAX**  
7 **CREDIT.**

8 (a) IN GENERAL.—Subpart D of part IV of sub-  
9 chapter A of chapter 1 of the Internal Revenue Code of

1 1986 (relating to business related credits) is amended by  
2 adding at the end the following new section:

3 **“SEC. 450. EQUITY INVESTMENT IN SMALL BUSINESS TAX**  
4 **CREDIT.**

5 “(a) GENERAL RULE.—For purposes of section 38,  
6 in the case of a qualified investor, the equity investment  
7 in small business tax credit determined under this section  
8 for the taxable year is an amount equal to 25 percent of  
9 the amount of each qualified equity investment made by  
10 the qualified investor during the taxable year.

11 “(b) CREDIT AMOUNT.—For purposes of determining  
12 the small business tax credit under subsection (a)—

13 “(1) LIMITATION PER QUALIFIED INVESTOR.—  
14 The amount of qualified equity investments made by  
15 the qualified investor during the taxable year shall  
16 not exceed \$500,000.

17 “(2) LIMITATION PER QUALIFIED SMALL BUSI-  
18 NESS.—The amount of qualified equity investments  
19 made by the qualified investor in a qualified small  
20 business during the taxable year shall not exceed  
21 \$250,000.

22 “(c) DEFINITIONS.—For purposes of this section—

23 “(1) QUALIFIED INVESTOR.—The term ‘quali-  
24 fied investor’ means—

1           “(A) an individual who qualifies as an ac-  
2           credited investor under rules and regulations  
3           prescribed by the Commissioner of the Securi-  
4           ties and Exchange Commission, or

5           “(B) a partnership with respect to which  
6           all of the partners are individuals who qualify  
7           as accredited investors under rules and regula-  
8           tions prescribed by the Commissioner of the Se-  
9           curities and Exchange Commission.

10          “(2) QUALIFIED EQUITY INVESTMENT.—The  
11          term ‘qualified equity investment’ means the trans-  
12          fer of cash or cash equivalents in exchange for stock  
13          or capital interest in a qualified small business.

14          “(3) QUALIFIED SMALL BUSINESS.—The term  
15          ‘qualified small business’ means a private small busi-  
16          ness concern (within the meaning of section 3 of the  
17          Small Business Act)—

18                 “(A) that meets the applicable size stand-  
19                 ard (as in effect on January 1, 2005) estab-  
20                 lished by the Administrator of the Small Busi-  
21                 ness Administration pursuant to subsection  
22                 (a)(2) of such section, and

23                 “(B) has its principal place of business in  
24                 the United States.

1 For purposes of this section, all members of the  
2 same controlled group of corporations (within the  
3 meaning of section 267(f)) and all persons under  
4 common control (within the meaning of section  
5 52(b)) shall be treated as 1 qualified small business.

6 “(d) ACTIVE BUSINESS REQUIREMENT.—

7 “(1) IN GENERAL.—Holding stock in a quali-  
8 fied small business shall not be treated as a qualified  
9 equity investment unless, during substantially all of  
10 the qualified investor’s holding period for such stock,  
11 such qualified small business meets the active busi-  
12 ness requirements of paragraph (2).

13 “(2) REQUIREMENTS.—

14 “(A) IN GENERAL.—For purposes of para-  
15 graph (1), the requirements of this paragraph  
16 are met by a qualified small business for any  
17 period if during such period at least 80 percent  
18 (by value) of the assets of such qualified small  
19 business are used by such qualified small busi-  
20 ness in the active conduct of 1 or more quali-  
21 fied trades or businesses.

22 “(B) SPECIAL RULE FOR CERTAIN ACTIVI-  
23 TIES.—For purposes of subparagraph (A), if, in  
24 connection with any future qualified trade or

1 business, a qualified small business is engaged  
2 in—

3 “(i) start-up activities described in  
4 section 195(c)(1)(A),

5 “(ii) activities resulting in the pay-  
6 ment or incurring of expenditures which  
7 may be treated as research and experi-  
8 mental expenditures under section 174, or

9 “(iii) activities with respect to in-  
10 house research expenses described in sec-  
11 tion 41(b)(4),

12 assets used in such activities shall be treated as  
13 used in the active conduct of a qualified trade  
14 or business. Any determination under this sub-  
15 paragraph shall be made without regard to  
16 whether a qualified small business has any  
17 gross income from such activities at the time of  
18 the determination.

19 “(C) QUALIFIED TRADE OR BUSINESS.—  
20 For purposes of this paragraph, the term  
21 ‘qualified trade or business’ is as defined in sec-  
22 tion 1202(e)(3).

23 “(D) STOCK IN OTHER ENTITIES.—

24 “(i) LOOK-THRU IN CASE OF SUBSIDI-  
25 ARIES.—For purposes of this subsection,

1 stock and debt in any subsidiary entity  
2 shall be disregarded and the parent quali-  
3 fied small business shall be deemed to own  
4 its ratable share of the subsidiary's assets,  
5 and to conduct its ratable share of the sub-  
6 sidiary's activities.

7 “(ii) PORTFOLIO STOCK OR SECURI-  
8 TIES.—A qualified small business shall be  
9 treated as failing to meet the requirements  
10 of subparagraph (A) for any period during  
11 which more than 10 percent of the value of  
12 its assets (in excess of liabilities) consists  
13 of stock or securities in other entities  
14 which are not subsidiaries of such qualified  
15 small business other than assets described  
16 in subparagraph (E)).

17 “(iii) SUBSIDIARY.—For purposes of  
18 this subparagraph, an entity shall be con-  
19 sidered a subsidiary if the parent owns  
20 more than 50 percent of the combined vot-  
21 ing power of all classes of stock entitled to  
22 vote, or more than 50 percent in value of  
23 all outstanding stock, of such entity.

24 “(E) WORKING CAPITAL.—For purposes of  
25 subparagraph (A), any assets which—

1           “(i) are held as a part of the reason-  
2           ably required working capital needs of a  
3           qualified trade or business of the qualified  
4           small business, or

5           “(ii) are held for investment and are  
6           reasonably expected to be used within 2  
7           years to finance research and experimen-  
8           tation in a qualified trade or business or  
9           increases in working capital needs of a  
10          qualified trade or business,

11          shall be treated as used in the active conduct of  
12          a qualified trade or business. For periods after  
13          the qualified small business has been in exist-  
14          ence for at least 2 years, in no event may more  
15          than 50 percent of the assets of the qualified  
16          small business qualify as used in the active con-  
17          duct of a qualified trade or business by reason  
18          of this subparagraph.

19          “(F) MAXIMUM REAL ESTATE HOLD-  
20          INGS.—A qualified small business shall not be  
21          treated as meeting the requirements of subpara-  
22          graph (A) for any period during which more  
23          than 10 percent of the total value of its assets  
24          consists of real property which is not used in  
25          the active conduct of a qualified trade or busi-

1           ness. For purposes of the preceding sentence,  
2           the ownership of, dealing in, or renting of real  
3           property shall not be treated as the active con-  
4           duct of a qualified trade or business.

5           “(G) COMPUTER SOFTWARE ROYALTIES.—  
6           For purposes of subparagraph (A), rights to  
7           computer software which produces active busi-  
8           ness computer software royalties (within the  
9           meaning of section 543(d)(1)) shall be treated  
10          as an asset used in the active conduct of a  
11          trade or business.

12          “(e) CERTAIN PURCHASES BY QUALIFIED INVESTOR  
13          OF ITS OWN STOCK.—

14                 “(1) REDEMPTIONS FROM QUALIFIED INVES-  
15                 TOR OR RELATED PERSON.—Stock acquired by the  
16                 qualified investor shall not be treated as a qualified  
17                 equity investment if, at any time during the 4-year  
18                 period beginning on the date 2 years before the  
19                 issuance of such stock, the qualified small business  
20                 issuing such stock purchased (directly or indirectly)  
21                 any of its stock from the qualified investor or from  
22                 a person related (within the meaning of section  
23                 267(b) or 707(b)) to the qualified investor.

24                 “(2) SIGNIFICANT REDEMPTIONS.—Stock  
25                 issued by a qualified small business to a qualified in-

1 investor shall not be treated as a qualified equity in-  
2 vestment if, during the 2-year period beginning on  
3 the date 1 year before the issuance of such stock,  
4 such qualified small business made 1 or more pur-  
5 chases of its stock with an aggregate value (as of the  
6 time of the respective purchases) exceeding 5 per-  
7 cent of the aggregate value of all of its stock as of  
8 the beginning of such 2-year period.

9 “(3) TREATMENT OF CERTAIN TRANS-  
10 ACTIONS.—If any transaction is treated under sec-  
11 tion 304(a) as a distribution in redemption of the  
12 stock of any qualified small business, for purposes of  
13 subparagraphs (A) and (B), such qualified small  
14 business shall be treated as purchasing an amount  
15 of its stock equal to the amount treated as such a  
16 distribution under section 304(a).

17 “(f) SPECIAL RULE FOR RELATED PARTIES.—

18 “(1) IN GENERAL.—No credit shall be allowed  
19 under subsection (a) with respect to a qualified eq-  
20 uity investment made by a qualified investor in a  
21 qualified small business that is a related party to the  
22 qualified investor.

23 “(2) RELATED PARTY.—For purposes of para-  
24 graph (1), a person is a related party with respect  
25 to another person if such person bears a relationship

1 to such other person described in section 267(b) or  
2 707(b), or if such persons are engaged in trades or  
3 businesses under common control (within the mean-  
4 ing of subsections (a) and (b) of section 52).

5 “(g) RECAPTURE OF CREDIT IN CERTAIN CASES.—

6 “(1) IN GENERAL.—If, at any time during the  
7 3-year period beginning on the date that the quali-  
8 fied equity investment is made by the qualified in-  
9 vestor, there is a recapture event with respect to  
10 such investment, then the tax imposed by this chap-  
11 ter for the taxable year in which such event occurs  
12 shall be increased by the credit recapture amount.

13 “(2) CREDIT RECAPTURE AMOUNT.—For pur-  
14 poses of paragraph (1), the credit recapture amount  
15 is an amount equal to the sum of—

16 “(A) the aggregate decrease in the credits  
17 allowed to the taxpayer under section 38 for all  
18 prior taxable years which would have resulted if  
19 no credit had been determined under this sec-  
20 tion with respect to such investment, plus

21 “(B) interest at the underpayment rate es-  
22 tablished under section 6621 on the amount de-  
23 termined under subparagraph (A) for each  
24 prior taxable year for the period beginning on

1           the due date for filing the return for the prior  
2           taxable year involved.

3           No deduction shall be allowed under this chapter for  
4           interest described in subparagraph (B).

5           “(3) RECAPTURE EVENT.—For purposes of  
6           paragraph (1), there is a recapture event with re-  
7           spect to a qualified equity investment if such invest-  
8           ment is sold, transferred, or exchanged by the quali-  
9           fied investor, but only to the extent that such sale,  
10          transfer, or exchange is not the direct result of a  
11          complete or partial liquidation of the qualified small  
12          business in which such qualified equity investment is  
13          made.

14          “(4) SPECIAL RULES.—

15                 “(A) TAX BENEFIT RULE.—The tax for  
16                 the taxable year shall be increased under para-  
17                 graph (1) only with respect to credits allowed  
18                 by reason of this section which were used to re-  
19                 duce tax liability. In the case of credits not so  
20                 used to reduce tax liability, the carryforwards  
21                 and carrybacks under section 39 shall be appro-  
22                 priately adjusted.

23                 “(B) NO CREDITS AGAINST TAX.—Any in-  
24                 crease in tax under this subsection shall not be  
25                 treated as a tax imposed by this chapter for

1 purposes of determining the amount of any  
2 credit under this chapter or for purposes of sec-  
3 tion 55.

4 “(h) BASIS REDUCTION.—The basis of any qualified  
5 equity investment shall be reduced by the amount of any  
6 credit determined under this section with respect to such  
7 investment.

8 “(i) REGULATIONS.—

9 “(1) IN GENERAL.—The Secretary shall pre-  
10 scribe such regulations as necessary to carry out the  
11 provisions of this section.

12 “(2) CERTIFICATION OF QUALIFIED EQUITY IN-  
13 VESTMENT.—Such regulations shall require that a  
14 qualified investor—

15 “(A) certify that the small business in  
16 which the equity investment is made meets the  
17 requirements described in subsection (e)(3), and

18 “(B) include the name, address, and tax-  
19 payer identification number of such small busi-  
20 ness on the return claiming the credit under  
21 subsection (a).

22 “(j) TERMINATION.—This section shall not apply to  
23 qualified equity investments made in taxable years begin-  
24 ning after December 31, 2011.”.

1 (b) CREDIT MADE PART OF GENERAL BUSINESS  
2 CREDIT.—Subsection (b) of section 38 of such Code is  
3 amended by striking “and” at the end of paragraph (29),  
4 by striking the period at the end of paragraph (30) and  
5 inserting “, and”, and by adding at the end the following  
6 new paragraph:

7 “(31) in the case of a taxpayer, the equity in-  
8 vestment in small business tax credit determined  
9 under section 450(a).”.

10 (c) CLERICAL AMENDMENT.—The table of sections  
11 for subpart D of part IV of subchapter A of chapter 1  
12 of such Code is amended by adding at the end the fol-  
13 lowing new item:

“Sec. 450. Equity investment in small business tax credit.”.

14 (d) EFFECTIVE DATE.—The amendments made by  
15 this section shall apply to qualified equity investments  
16 made after the date of the enactment of this Act.

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