

MEMORANDUM

ncbioscience.org



TO: NCBIO Members

FROM: Sam Taylor

DATE: June 15, 2009

RE: First Preliminary Analysis of House Tax Reform Proposal

This memorandum summarizes the tax provisions of the state budget package adopted last week by the North Carolina House of Representatives. It also provides initial analysis of their impact on life science companies. Finally, the memorandum compares key provisions of the House tax package with a parallel tax proposal currently under consideration in the State Senate. The two chambers hope to reconcile their differences with respect to both the tax and spending portions of the budget bill before the beginning of the new fiscal year on July 1, 2009.

Our goal is to finalize this memorandum by noon, Tuesday, June 16, 2009. Therefore, members with comments or concerns regarding the tax proposals addressed in this memorandum should contact me at staylor@ncbioscience.org or (919) 306-1030 as soon as possible. Our hope is to issue a revised final analysis later this week and to simultaneously begin informing legislators of our comments through direct and grassroots advocacy.

Executive Summary. The tax provisions of the budget adopted by the State House last week (i) create a system of unitary taxation (mandatory combined reporting) of holding company systems; (ii) expand the franchise tax base to include limited liability companies, (iii) impose new sales taxes on selected services, including maintenance and repair; (iv) increase the personal income tax rate; (v) and implement various other tax increases. The House package

will negatively impact innovation-based companies – including the life science sector – by taxing maintenance and calibration services for analytical equipment and complex manufacturing systems, as well as by depressing availability of private capital for start-up companies and other equity investments. The House package is inferior to tax reform proposals under consideration in the State Senate, which increase overall tax collections through a more carefully considered broadening of the State's tax base with accompanying reductions in key tax rates.

Background. The North Carolina House of Representatives approved a 2009-11 state budget that includes tax increases that will increase state revenues by \$784 million in FY 2009-10 and \$970 million in FY 2010-11. A copy of the tax provisions of the House budget is attached.

Although the tax provisions adopted by the House last week allow lawmakers to avoid potentially devastating spending cuts, many provisions of the House tax package are likely to have particularly deleterious effects on life science companies and other sectors of the State's innovation economy.

Summaries and analysis of key provisions of the House tax package are set out in the paragraphs following.

Unitary Taxation/Mandatory Combined Reporting. The House tax package will require multi-state holding company systems with subsidiaries in North Carolina to calculate state income tax based on their consolidated earnings. The provision is expected to generate \$19 million in new tax revenues for the 2009-2010 fiscal year and \$43 million in additional revenues when fully implemented in FY-2010-11.

If enacted, the unitary taxation provisions are likely to disrupt existing tax planning activities of multistate corporations and require substantial changes in corporate structure and inter-subsidiary cash flows. The proposed changes will be particularly problematic for multi-state holding companies with stand-alone



cost-centers in North Carolina – such as separately incorporated research and development entities.¹

Sales Tax on Repair & Maintenance Services. The House package imposes new state and local sales taxes on a variety of services, including warranties and installation, repair and maintenance services. These taxes are imposed at the combined sales tax rate, which is currently composed of a 4.5% state tax and local taxes of between 2% and 2.75%.² Other newly-taxed activities in the proposed package include amusements, courier services and digital downloads. House leaders familiar with the tax package say that it is not intended to tax customized software; information technology companies, however, have expressed concern that the scope of the new provisions is ambiguous. The proposed service taxes bundle is expected to produce approximately \$383 million annually in additional income when fully implemented. The proposed sales tax on warranties and installation, repair and maintenance services expected to produce \$244 million.

Taxation of maintenance services will place a significant new economic burden on technology-intensive companies, which typically use high-precision equipment with regular and extensive calibration and maintenance requirements.³ In this context, the House proposal is essentially a tax on capital assets.

Taxation of maintenance and other business services also discriminates against small businesses, which have limited internal resources (whose compensation is not subject to sales tax), and more frequently are required outsource such activities.

Increase Upper Income Tax Brackets. The House tax proposal increases North Carolina's top marginal rate for personal income tax to from 7.75% to

¹ We are aware of at least one NC BIO member with a separately incorporated research and development entity in North Carolina. We would appreciate hearing from you regarding other companies with similar structural issues.

² As noted below, the House tax package also contains a provision increasing the state's general sales tax rate by 0.25%. See *infra* at 4. If that provision becomes law, combined state and local sales tax rates will range between 6.75% and 7.5%.

³ In the context of depreciable equipment, the proposed tax runs exactly counter to existing state tax policy which provides for a nominal 1% sales tax capped at \$80 per item.



8.5%. Two additional tax brackets are added: (1) for married individuals filing jointly, taxable income between \$200,000 and \$500,000 (unmarried individuals, \$120,000 to \$300,000) annually is taxed at 8.25%, and (2) for married individuals filing jointly, taxable income in excess of \$500,000 annually (unmarried individuals, more than \$300,000) is taxed at 8.5%. The proposed increases will produce an additional \$256.7 million in tax revenue in FY 2009-10.

The increase in personal income taxes among wealthy individuals is likely to depress already low levels of angel investment in the State. In addition, because North Carolina taxes capital gains as ordinary income, the taxes paid by investors in successful exits will be higher – increasing their incentives to relocate to lower-tax jurisdictions.⁴

Franchise Tax on Limited Liability Companies. The House proposal would extend the State's existing franchise tax to cover limited liability companies.⁵ The extension is expected to generate \$131 million annually when fully implemented in FY 2010-11. Because the franchise tax is levied without regard to a business' income, it can be particularly burdensome to pre-revenue start-up companies. We are advised that most life science start-ups in North Carolina are organized as corporations; however, we seek members' feedback in this regard.

Other Changes. In addition to the tax changes outlined above, the House proposal contains other provisions that do not appear to disproportionately affect the interest of life science companies. These are:

- *Throw-Back Rule.* This proposal would alter North Carolina's apportionment formula for corporate income taxation by increasing the formula's sales factor by the share of a corporation's sales derived from

⁴ NC BIO's proposed capital gains tax exclusion for founders stock, if enacted, would mitigate the impact of proposed higher marginal tax rates on individuals exiting from successful Qualified Business Ventures.

⁵ Franchise tax is calculated on the basis of a business's capital stock, surplus and undivided profits. A firm's franchise tax basis cannot be less than 55% of the appraised value of its tangible assets in North Carolina or the total investment in tangible assets in the State. The franchise tax rate is \$1.50 per thousand dollars of assets.



shipments originating in North Carolina and delivered to states where the business is not subject to income tax. Twenty-five states have throw-back rules. The proposal is estimated to generate an additional \$14.7 million in FY 2010-11.

- *Sales Tax Rate Increase.* The House proposal increases the state's general sales tax rate by 0.25% to 4.75%.⁶ This change will produce an additional \$195 million in tax revenue during FY 2009-10.
- *Liquor Tax.* The House proposal increases the tax on spirituous liquors by 1.5% to raise an additional \$7.9 million in FY 2009-10.
- *Bank Interest Deduction.* The proposal eliminates an existing income tax deduction for certain interest allocable to interest income on tax exempt bonds. The provision is expected to raise \$8.8 million annually when fully implemented in FY 2010-11.

Comparison to Senate Tax Proposals. The House tax package differs substantially from a parallel tax package currently under consideration in the State Senate. That package was summarized by an earlier NC BIO memorandum. [Click here to download that analysis.](#)

Key differences between the House and Senate Tax packages are summarized below:

- *Unitary Taxation/Mandatory Combined Reporting.* The Senate tax package does not include these provisions.
- *Apply Franchise Tax to LLCs.* Like the House package, the Senate proposal would extend the franchise tax to limited liability companies.
- *Sales Tax on Services.* The Senate package would make North Carolina's state and local sales taxes applicable to a broader range of services, but would decrease general sales tax rate. The Senate package

⁶ As noted above, the state general rate is augmented by local sales taxes at rates between 2.0% and 2.75%.



excludes maintenance and repair of depreciable capital equipment from sales tax.

- *Personal Income Tax.* The Senate package broadens the personal income tax base and lowers personal income tax rates. The package would eliminate most personal income tax deductions and exclusions, but create analogous tax credits for certain typical personal expenses such as mortgage interest, medical expenses, dependent care and charitable contributions. Tax rates would be reduced from 7.75%, 7.0% and 6.0% to 7.5%, 6.5% and 5.25%. A new zero-rate bracket would be added for taxpayers with adjusted gross incomes of less than \$10,000.
- *Throw-Back Rule.* Like the House package, the Senate proposal would add a throw-back rule to the State's corporate income tax apportionment formula. The Senate package would also eliminate most corporate tax deductions,⁷ but also proposes to reduce the corporate income tax rate from 6.9% to 4.5% over two years.
- *Alcohol Tax Increase.* In addition to increasing the State's tax on spirituous liquors, the Senate package would also raise tax rates on beer, wine and cigarettes.

Analysis. Our preliminary conclusion is that the House tax package has a more negative impact on life science and other innovation-based companies than the Senate package. In addition, because of its more aggressive provisions broadening the tax base, the Senate tax package is more likely to reduce volatility in state tax revenues.

With respect to impacts on innovation, the most important difference between the House and Senate proposals is their treatment of maintenance services for depreciable equipment. The House package would expand the State's current state and local sales taxes to include these services. The Senate package excludes both purchases and maintenance of depreciable equipment from sales tax.

⁷ The Senate package would preserve the state's existing R&D tax credit. Article 3J tax credits for investment and job creation would be repealed by the Senate package.



Although the Senate package is more aggressive in the elimination of personal and corporate income tax deductions and exclusions, the Senate package also reduces tax rates and preserves key innovation-inducing provisions such as the R&D tax credit and the Qualified Business Venture tax credit for investors in innovation-based start-up companies.

Both packages substantially increase personal income tax collections, but the Senate package does so through a general broadening of the tax base rather than an increase in rates. By lowering overall tax rates, the Senate package reduces tax rates on capital gains and thereby has a much less deleterious effect on capital formation in start-up companies and other businesses.

Conclusion. The House tax package both increases tax rates and broadens the tax base. The package is particularly troublesome because it increases taxes on capital and on the maintenance of capital equipment. Tax changes currently under consideration in the State Senate, though also designed to increase state revenues, are generally less unfavorable to innovation-based companies, due to a variety of targeted tax credits and exclusions.

NCBIO members are requested to provide comments regarding the analysis and conclusions in this memorandum to Sam Taylor at (919) 306-1030 or staylor@ncbioscience.org. Member feedback will inform the Organization's future lobbying efforts regarding tax and budget legislation in the FY 2009-11 biennium.

SMT/st



15 **PART XXVIIA. INDIVIDUAL INCOME TAX CHANGES**

16
17 **TWO NEW TAX BRACKETS FOR UPPER INCOME**

18 **SECTION 27A.1.(a)** G.S. 105-134.2(a) reads as rewritten:

19 "(a) A tax is imposed upon the North Carolina taxable income of every individual. The
20 tax shall be levied, collected, and paid annually and shall be computed at the following
21 percentages of the taxpayer's North Carolina taxable income.

22 (1) For married individuals who file a joint return under G.S. 105-152 and for
23 surviving spouses, as defined in section 2(a) of the Code:

Over	Up To	Rate
0	\$21,250	6%
\$21,250	\$100,000	7%
\$100,000	NA \$200,000	7.75%
<u>\$200,000</u>	<u>\$500,000</u>	<u>8.25%</u>
<u>\$500,000</u>	<u>NA</u>	<u>8.5%</u>

31
32 (2) For heads of households, as defined in section 2(b) of the Code:

Over	Up To	Rate
0	\$17,000	6%
\$17,000	\$80,000	7%
\$80,000	NA \$160,000	7.75%
<u>\$160,000</u>	<u>\$400,000</u>	<u>8.25%</u>
<u>\$400,000</u>	<u>NA</u>	<u>8.5%</u>

33
34
35
36
37
38 (3) For unmarried individuals other than surviving spouses and heads of
39 households:

Over	Up To	Rate
0	\$12,750	6%
\$12,750	\$60,000	7%
\$60,000	NA \$120,000	7.75%
<u>\$120,000</u>	<u>\$300,000</u>	<u>8.25%</u>
<u>\$300,000</u>	<u>NA</u>	<u>8.5%</u>

40
41
42
43
44
45
46
47
48
49 (4) For married individuals who do not file a joint return under G.S. 105-152:
50
51

	Over	Up To	Rate
1			
2	0	\$10,625	6%
3	\$10,625	\$50,000	7%
4	\$50,000	NA \$100,000	7.75%
5	\$100,000	\$250,000	8.25%
6	\$250,000	NA	8.5%"

SECTION 27A.1.(b) This section becomes effective for taxable years beginning on or after January 1, 2009. Notwithstanding G.S. 105-163.15, no addition to tax may be made under that statute for a taxable year beginning on or after January 1, 2009, and before January 1, 2010, with respect to an underpayment of individual income tax to the extent the underpayment was created or increased by this section.

PART XXVIIB. CORPORATE INCOME TAX CHANGES

SINGLE INCOME TAX RETURN FOR UNITARY BUSINESS

SECTION 27B.1.(a) G.S. 105-130.2 reads as rewritten:

"§ 105-130.2. Definitions.

The following definitions apply in this Part:

(1) Code. – Defined in G.S. 105-228.90.

(1a) Common ownership. – The direct or indirect control or ownership of more than fifty percent (50%) of the outstanding voting stock of the persons carrying on a unitary business activity.

~~(1a)~~(1b) Corporation. – A joint-stock company or association, an insurance company, a domestic corporation, a foreign corporation, a unitary business group, or a limited liability company.

~~(1b)~~(1c) C Corporation. – A corporation that is not an S Corporation.

~~(1e)~~(1d) Department. – The Department of Revenue.

(1e) Principal reporting member. – A member of the unitary business group appointed by the group to act in its own name in all matters relating to the tax liability for the unitary business group. The principal reporting member continues to act for the group until a new principal reporting member is appointed.

(2) Domestic corporation. – A corporation organized under the laws of this State.

(3) Fiscal year. – An income year, ending on the last day of any month other than December. A corporation that pursuant to the provisions of the Code has elected to compute its federal income tax liability on the basis of an annual period varying from 52 to 53 weeks shall compute its taxable income under this Part on the basis of the same period used by the corporation in computing its federal income tax liability for the income year.

(4) Foreign corporation. – Any corporation other than a domestic corporation.

(4a) Gross income. – Defined in section 61 of the Code.

(4b) Income year. – The calendar year or the fiscal year upon the basis of which the net income is computed under this Part. If no fiscal year has been established, the income year is the calendar year. In the case of a return made for a fractional part of a year under the provisions of this Part or under rules adopted by the Secretary, the income year is the period for which the return is made.

(5) Limited liability company. – Either a domestic limited liability company organized under Chapter 57C of the General Statutes or a foreign limited liability company authorized by that Chapter to transact business in this

1 State that is classified for federal income tax purposes as a corporation. As
2 applied to a limited liability company that is a corporation under this Part,
3 the term 'shareholder' means a member of the limited liability company and
4 the term 'corporate officer' means a member or manager of the limited
5 liability company.

6 (5a) Person. – Defined in G.S. 105-228.90.

7 ~~(5a)~~(5b) S Corporation. – Defined in G.S. 105-131(b).

8 ~~(5b)~~(5c) Secretary. – The Secretary of Revenue.

9 ~~(5e)~~(5d) State net income. – The taxpayer's federal taxable income as determined
10 under the Code, adjusted as provided in G.S. 105-130.5 and, in the case of a
11 ~~corporation~~ taxpayer that has income from business activity that is taxable
12 both within and without this State, allocated and apportioned to this State as
13 provided in G.S. 105-130.4.

14 ~~(5d)~~(5e) Taxable year. – Income year.

15 (6) Taxpayer. – A corporation subject to the tax imposed by this Part.

16 (7) Tax haven country. – A country identified in G.S. 143-59.1(c)(2), or a
17 country that has no or nominal effective tax on the relevant income and
18 meets at least one of the following conditions:

19 a. Has laws or practices that prevent effective exchange of information
20 for tax purposes with other governments on taxpayers benefiting
21 from the tax regime.

22 b. Has a tax regime which lacks transparency. A tax regime lacks
23 transparency if the details of legislative, legal, or administrative
24 provisions are not open and apparent or are not consistently applied
25 among similarly situated taxpayers, or if the information needed by
26 tax authorities to determine a taxpayer's correct tax liability, such as
27 accounting records and underlying documentation, is not adequately
28 available.

29 c. Facilitates the establishment of foreign-owned entities without the
30 need for a local substantive presence or prohibits these entities from
31 having any commercial impact on the local economy.

32 d. Explicitly or implicitly excludes the jurisdiction's resident taxpayers
33 from taking advantage of the tax regime's benefits or prohibits
34 enterprises that benefit from the regime from operating in the
35 jurisdiction's domestic market.

36 e. Has a tax regime which is favorable for tax avoidance, based upon an
37 overall assessment of relevant factors, including whether the
38 jurisdiction has a significant untaxed offshore financial/other services
39 sector relative to its overall economy.

40 (8) Unitary business. – Business activities that meet one or more of the
41 following conditions:

42 a. Activities of the members are in the same general line of business.

43 b. Activities of the members are steps in a vertically structured
44 enterprise or process.

45 c. Activities of members that provide mutual benefit and produce a
46 significant sharing or exchange of value among them or a significant
47 flow of value between them.

48 d. Centralized management.

49 (9) Unitary business group. – One or more persons related through common
50 ownership who engage in a unitary business. The term does not include any
51 of the following persons:

- a. A corporation exempt from taxation under Code section 501.
- b. An S-Corporation.
- c. A partnership.
- d. An insurance company subject to tax under Article 8B of this Chapter.
- e. A corporation whose business activity outside the United States is eighty percent (80%) or more of any such corporation's total business activity is excluded from the unitary business group unless that corporation is in a tax haven country. 'United States' means the 50 states of the United States, the District of Columbia, and the United States' territories and possessions."

SECTION 27B.1.(b) G.S. 105-130.3 reads as rewritten:

"§ 105-130.3. Corporations.

A tax is imposed on the State net income of every C Corporation or unitary business group doing business in this State. An S Corporation is not subject to the tax levied in this section. The tax rate is six and nine-tenths percent (6.9%) of the taxpayer's State net income.~~is a percentage of the taxpayer's State net income computed as follows:~~

<u>Income Years Beginning</u>	<u>Tax</u>
In 1997	7.5%
In 1998	7.25%
In 1999	7%
After 1999	6.9%.

SECTION 27B.1.(c) Part 1 of Article 4 of Chapter 105 of the General Statutes is amended by adding a new section to read:

"§ 105-130.3A. Taxation of unitary business group.

(a) Return. – A unitary business group with business activity in this State must file an income tax return that includes the State net income of the unitary business group. The unitary business group's return must be filed by the principal reporting member as defined in G.S.105-130.2. The accounting period of the unitary business group is the accounting period used by members of the unitary business group for federal consolidated return purposes.

(b) Federal Taxable Income. – The federal taxable income of a unitary business group is determined by adding together the federal taxable income of each member of the unitary business group as if that member filed a separate federal income tax return and eliminating all intercompany transactions. The federal taxable income of the unitary business group shall be adjusted as required under G.S. 105-130.5 except that no adjustments shall be made with respect to intercompany transactions that have been eliminated pursuant to this subsection. If a unitary business group has income from business activity that is taxable both within and without this State, the unitary business group's federal taxable income as adjusted pursuant to G.S. 105-130.5 is allocated and apportioned to North Carolina pursuant to G.S. 105-130.4. The property, payroll, and sales factors for the unitary business group are determined by adding together the property, payroll, and sales of each member of the unitary business group after eliminating intercompany transactions. The appropriate apportionment methodology as set out in G.S. 105-130.4(m) through (s) to be used by the unitary business group is based on the unitary business group, not the individual member.

(c) Tax Credits. – Tax credits earned by a member of the group, but not fully used by or allowed to that member prior to becoming a member of the unitary business group, may be used by the group, subject to the provisions of the specific credits. Tax credits brought into the group or earned by the group remain with the group and may not be claimed by a member that is no longer a member of the group.

(d) Net Economic Losses. – Net economic losses sustained by a member of the group, but not fully used by that member prior to becoming a member of the unitary business group,

1 may be used by the group subject to the provisions of G.S. 105-130.8. Net economic losses
2 brought into the group or earned by the group remain with the group and may not be claimed
3 by a member that is no longer a member of the group.

4 (e) Liability. – Every member of the unitary business group is jointly and severally
5 liable for the unitary business group's tax liability under this Part, including any interest and
6 penalties."

7 **SECTION 27B.1.(d)** G.S. 105-228.3 reads as rewritten:

8 **"§ 105-228.3. Definitions.**

9 The following definitions apply in this Article:

10 (1) Article 65 corporation. – A corporation subject to Article 65 of Chapter 58
11 of the General Statutes, regulating hospital, medical, and dental service
12 corporations.

13 (1a) Captive insurance company. – An insurer that receives more than fifty
14 percent (50%) of its gross premiums from affiliates as defined in
15 G.S. 105-130.6.

16 (2) Insurer. – An insurer as defined in ~~G.S. 58-1-5~~ G.S. 58-1-5, other than a
17 captive insurance company, or a group of employers who have pooled their
18 liabilities pursuant to G.S. 97-93 of the Workers' Compensation Act.

19 (3) Self-insurer. – An employer that carries its own risk pursuant to G.S. 97-93
20 of the Workers' Compensation Act."

21 **SECTION 27B.1.(e)** G.S. 105-228.5 is amended by adding a new subsection to
22 read:

23 "(a1) A captive insurance company is not subject to the tax levied by this section if the
24 captive insurance company is part of a unitary business group with business activity in this
25 State."

26 **SECTION 27B.1.(f)** G.S. 105-130.14 reads as rewritten:

27 **"§ 105-130.14. Corporations filing consolidated returns for federal income tax purposes.**

28 Any corporation electing or required to file a consolidated income tax return with the
29 Internal Revenue Service shall not file a consolidated return with the Secretary of Revenue,
30 unless specifically directed to do so in writing by the ~~Secretary, and Secretary.~~ If the
31 corporation is a member of a unitary business group, it, along with the other members of the
32 group, shall file an income tax return for the unitary business group. If the corporation is not a
33 member of a unitary business group, it shall determine its State net income as if a separate
34 return had been filed for federal purposes."

35 **SECTION 27B.1.(g)** This section becomes effective for taxable years beginning on
36 or after January 1, 2010.

37 38 **EXPAND FRANCHISE TAX TO INCLUDE LIMITED LIABILITY BUSINESS** 39 **ENTITIES**

40 **SECTION 27B.2.(a)** G.S. 105-114 reads as rewritten:

41 **"§ 105-114. Nature of taxes; definitions.**

42 (a) Nature of Taxes. – ~~The taxes levied in this Article upon persons and partnerships are~~
43 ~~for the privilege of engaging in business or doing the act named.~~ This Article imposes a tax on a
44 business entity for the privilege of doing business in this State in an ownership form that
45 confers limited liability on the owners of the entity.

46 (a1) Scope. – The taxes levied in this Article ~~upon corporations~~ are privilege or excise
47 taxes levied upon:

48 (1) ~~Corporations~~ A corporation organized under the laws of this State for the
49 existence of the corporate rights and privileges granted by their charters, and
50 the enjoyment, under the protection of the laws of this State, of the powers,

- 1 rights, privileges and immunities derived from the State by the form of such
2 existence; and/or of another state.
- 3 (2) ~~Corporations not organized under the laws of this State for doing business in~~
4 ~~this State and for the benefit and protection which these corporations receive~~
5 ~~from the government and laws of this State in doing business in this State.~~A
6 limited liability company.
- 7 (3) A limited partnership.
- 8 (4) A limited liability partnership.
- 9 (5) A limited liability limited partnership.
- 10 (a2) ~~Condition for Doing Business. – If the corporation is organized under the laws of~~
11 ~~this State, the payment of the taxes levied by this Article is a condition precedent to the right to~~
12 ~~continue in the corporate form of organization. If the corporation is not organized under the~~
13 ~~laws of this State, payment of these taxes is a condition precedent to the right to continue to~~
14 ~~engage in doing business in this State.~~Payment of the taxes levied by this Article is a condition
15 precedent to the right to do business in this State.
- 16 (a3) ~~Tax Year. – The taxes levied in this Article are for the fiscal year of the State in~~
17 ~~which the taxes become due, except that the taxes levied in G.S. 105-122 are for the income~~
18 ~~year of the corporation-business entity in which the taxes become due.~~
- 19 (a4) ~~No Double Taxation. – G.S. 105-122 does not apply to holding companies taxed~~
20 ~~under G.S. 105-120.2. G.S. 105-122 applies to a corporation-business entity taxed under~~
21 ~~another section of this Article only to the extent the taxes levied on the corporation-business~~
22 ~~entity in G.S. 105-122 exceed the taxes levied in other sections of this Article on the~~
23 ~~corporation or on a limited liability company whose assets must be included in the corporation's~~
24 ~~tax base under G.S. 105-114.1.~~business entity.
- 25 (b) ~~Definitions. – The following definitions apply in this Article:~~
- 26 (1) Business entity. – A corporation, a limited liability company, a limited
27 partnership, a limited liability partnership, or a limited liability limited
28 partnership.
- 29 ~~(1a)~~ City. – Defined in G.S. 105-228.90.
- 30 ~~(1b)~~ Code. – Defined in G.S. 105-228.90.
- 31 (2) ~~Corporation. – A domestic corporation, a foreign corporation, an electric~~
32 ~~membership corporation organized under Chapter 117 of the General~~
33 ~~Statutes or doing business in this State, or an association that is organized for~~
34 ~~pecuniary gain, has capital stock represented by shares, whether with or~~
35 ~~without par value, and has privileges not possessed by individuals or~~
36 ~~partnerships. The term includes a mutual or capital stock savings and loan~~
37 ~~association or building and loan association chartered under the laws of any~~
38 ~~state or of the United States. The term includes a limited liability company~~
39 ~~that elects to be taxed as a corporation under the Code, but does not~~
40 ~~otherwise include a limited liability company.~~
- 41 (3) ~~Doing business. – Each and every act, power, or privilege exercised or~~
42 ~~enjoyed in this State, as an incident to, or by virtue of the powers and~~
43 ~~privileges granted by the laws of this State.~~
- 44 (4) ~~Income year. – Defined in G.S. 105-130.2(4b).~~
- 45 (5) Limited liability company. – An entity formed under Chapter 57C of the
46 General Statutes.
- 47 (6) Limited liability limited partnership. – A limited partnership registered under
48 G.S. 59-210.
- 49 (7) Limited liability partnership. – An entity registered under Article 3B of
50 Chapter 59 of the General Statutes.

1 (8) Limited partnership. – A partnership formed with one or more general
2 partners and one or more limited partners.
3 (c) Recodified as G.S. 105-114.1 by Session Laws 2002-126, s. 30G.2.(b), effective
4 January 1, 2003."

5 **SECTION 27B.2.(b)** G.S. 105-114.1 is repealed.

6 **SECTION 27B.2.(c)** G.S. 105-120.2 reads as rewritten:

7 "**§ 105-120.2. Franchise or privilege tax on holding companies.**

8 (a) Requirement. – Every corporation, domestic and foreign, incorporated or, by an act,
9 domesticated under the laws of this State or doing business in this State A business entity
10 which, at the close of its taxable year is a holding company as defined in subsection (c) of this
11 section, shall, pursuant to the provisions of ~~G.S. 105-122;~~G.S. 105-122, do all of the following:

12 (1) Make a report and ~~statement, and~~statement.

13 (2) Determine the total amount of its ~~issued and outstanding capital stock,~~
14 ~~surplus and undivided profits, and~~capital base.

15 (3) Apportion ~~such outstanding capital stock, surplus and undivided profits~~ its
16 capital base to this State.

17 (b) Tax. – A business entity taxed under this section must pay the tax due under this
18 subsection at the time a report is due under G.S. 105-122.

19 (1) ~~Every corporation taxed under this section shall annually pay to the~~
20 ~~Secretary of Revenue, at the time the report and statement are due, a~~
21 ~~franchise or privilege tax, which is hereby levied, at the rate of~~ The tax rate
22 is one dollar and fifty cents (\$1.50) per one thousand dollars (\$1,000) of the
23 amount determined under subsection (a) of this section, but in no case shall
24 the tax be more than seventy-five thousand dollars (\$75,000) nor less than
25 thirty-five dollars (\$35.00).

26 (2) ~~Notwithstanding the provisions of subdivision (1) of this subsection, if~~ If the
27 tax produced pursuant to application of under this paragraph (2) subdivision
28 exceeds the tax produced pursuant to application of subdivision (1), under
29 subdivision (1) of this subsection, then the tax shall be is levied at the rate of
30 one dollar and fifty cents (\$1.50) per one thousand dollars (\$1,000) on the
31 greater of the amounts of following two amounts:

32 a. Fifty-five percent (55%) of the appraised value as determined for ad
33 valorem taxation of all the real and tangible personal property in this
34 State of each such corporation plus the total appraised value of
35 intangible property returned for taxation of intangible personal
36 property as computed under ~~G.S. 105-122(d); or~~G.S. 105-122(d).

37 b. The total actual investment in tangible property in this State of such
38 corporation as computed under G.S. 105-122(d).

39 (c) Definition. – The following definitions apply in this section:~~For purposes of this~~
40 ~~section, a~~

41 (1) Capital interest. – The right of a business entity that is not a corporation to
42 receive a percentage of the business entity's assets upon dissolution after
43 payments to creditors.

44 (2) ~~'holding company' is a~~ Holding company. – A corporation business entity
45 that receives during its taxable year more than eighty percent (80%) of its
46 gross income from ~~corporations~~ a business entity in which it owns directly or
47 indirectly more than fifty percent (50%) of the outstanding voting stock or
48 voting capital interests.

49 (d) Repealed by Session Laws 1985, c. 656, s. 39.

50 (e) Prohibition on Local Tax. – Counties, cities and towns shall not levy a franchise tax
51 on corporations a business entity taxed under this section. The tax imposed under the

1 provisions of G.S. 105-122 shall not apply to businesses taxed under the provisions of this
2 section.

3 (f) Credit. – In determining the total tax payable by any holding company under this
4 section, there shall be allowed as a credit on such tax the amount of the credit authorized under
5 Part 5 of Article 4 of this Chapter."

6 **SECTION 27B.2.(d)** G.S. 105-122 reads as rewritten:

7 "**§ 105-122. Franchise ~~or privilege~~ tax on domestic and foreign corporations a business**
8 **entity.**

9 (a) Tax Imposed. – An annual franchise ~~or privilege~~ tax is imposed on a corporation
10 business entity doing business in this State. The tax is determined on the basis of the books and
11 records of the ~~corporation~~ business entity as of the close of its income year. ~~A corporation~~
12 subject to the tax must file a return under affirmation with the Secretary at the place and in the
13 manner prescribed by the Secretary. The return must be signed by the president, vice president,
14 treasurer, or chief financial officer of the corporation. The tax rate is one dollar and fifty cents
15 (\$1.50) per one thousand dollars (\$1,000) of the capital base of the business entity and may not
16 be less than thirty-five dollars (\$35.00). The return is due on or before the fifteenth day of the
17 fourth month following the end of the corporation's business entity's income year.

18 (b) ~~Determination of Capital Base.~~ Base of Corporation. – A corporation taxed under
19 this section shall determine the total amount of its issued and outstanding capital stock, surplus,
20 and undivided profits. Every corporation doing business in this State which is a parent,
21 subsidiary, or affiliate of another corporation shall add to its capital stock, surplus, and
22 undivided profits all indebtedness owed to a parent, subsidiary, or affiliated corporation as a
23 part of its capital used in its business and as a part of the base for franchise tax under this
24 section. If any part of the capital of the creditor corporation is capital borrowed from a source
25 other than a parent, subsidiary, or affiliate, the debtor corporation, which is required under this
26 subsection to include in its tax base the amount of debt by reason of being a parent, subsidiary,
27 or affiliate of the creditor corporation, may deduct from the debt included a proportionate part
28 determined on the basis of the ratio of the borrowed capital of the creditor corporation to the
29 total assets of the creditor corporation. If the creditor corporation is also taxable under the
30 provisions of this section, the creditor corporation is allowed to deduct from the total of its
31 capital, surplus, and undivided profits the amount of any debt owed to it by a parent, subsidiary,
32 or affiliated corporation to the extent that the debt has been included in the tax base of the
33 parent, subsidiary, or affiliated debtor corporation reporting for taxation under the provisions of
34 this section. ~~No~~

35 No reservation or allocation from surplus or undivided profits is allowed except as provided
36 below:

- 37 (1) Definite and accrued legal liabilities.
- 38 (2) Taxes accrued, dividends declared, and reserves for depreciation of tangible
39 assets as permitted for income tax purposes.
- 40 (3) When including deferred tax liabilities, a corporation may reduce the amount
41 included in its base by netting against that amount deferred tax assets. The
42 reduction may not decrease deferred tax liabilities below zero (0).
- 43 (4) Reserves for the cost of any air-cleaning device or sewage or waste
44 treatment plant, including waste lagoons, and pollution abatement equipment
45 purchased or constructed and installed which reduces the amount of air or
46 water pollution resulting from the emission of air contaminants or the
47 discharge of sewage and industrial wastes or other polluting materials or
48 substances into the outdoor atmosphere or streams, lakes, or rivers, upon
49 condition that the corporation claiming such deductible liability shall furnish
50 to the Secretary a certificate from the Department of Environment and
51 Natural Resources or from a local air pollution control program for

1 air-cleaning devices located in an area where the Environmental
2 Management Commission has certified a local air pollution control program
3 pursuant to G.S. 143-215.112 certifying that the Environmental Management
4 Commission or local air pollution control program has found as a fact that
5 the air-cleaning device, waste treatment plant or pollution abatement
6 equipment purchased or constructed and installed as above described has
7 actually been constructed and installed and that such plant or equipment
8 complies with the requirements of the Environmental Management
9 Commission or local air pollution control program with respect to such
10 devices, plants or equipment, that such device, plant or equipment is being
11 effectively operated in accordance with the terms and conditions set forth in
12 the permit, certificate of approval, or other document of approval issued by
13 the Environmental Management Commission or local air pollution control
14 program and that the primary purpose thereof is to reduce air or water
15 pollution resulting from the emission of air contaminants or the discharge of
16 sewage and waste and not merely incidental to other purposes and functions.

17 (5) Reserves for the cost of purchasing and installing equipment or constructing
18 facilities for the purpose of recycling or resource recovering of or from solid
19 waste or for the purpose of reducing the volume of hazardous waste
20 generated shall be treated as deductible for the purposes of this section upon
21 condition that the corporation claiming such deductible liability shall furnish
22 to the Secretary a certificate from the Department of Environment and
23 Natural Resources certifying that the Department of Environment and
24 Natural Resources has found as a fact that the equipment or facility has
25 actually been purchased, installed or constructed, that it is in conformance
26 with all rules and regulations of the Department of Environment and Natural
27 Resources, and the recycling or resource recovering is the primary purpose
28 of the facility or equipment.

29 (6) Reserves for the cost of constructing facilities of any private or public utility
30 built for the purpose of providing sewer service to residential and outlying
31 areas shall be treated as deductible for the purposes of this section; the
32 deductible liability allowed by this section shall apply only with respect to
33 such pollution abatement plants or equipment constructed or installed on or
34 after January 1, 1955.

35 (7) The cost of treasury stock.

36 (8) In the case of an international banking facility, the capital base shall be
37 reduced by the excess of the amount as of the end of the taxable year of all
38 assets of an international banking facility which are employed outside the
39 United States over liabilities of the international banking facility owed to
40 foreign persons. For purposes of such reduction, foreign persons shall have
41 the same meaning as defined in G.S. 105-130.5(b)(13)d.

42 ~~Every corporation doing business in this State which is a parent, subsidiary, or affiliate of~~
43 ~~another corporation shall add to its capital stock, surplus, and undivided profits all indebtedness~~
44 ~~owed to a parent, subsidiary, or affiliated corporation as a part of its capital used in its business~~
45 ~~and as a part of the base for franchise tax under this section. If any part of the capital of the~~
46 ~~creditor corporation is capital borrowed from a source other than a parent, subsidiary, or~~
47 ~~affiliate, the debtor corporation, which is required under this subsection to include in its tax~~
48 ~~base the amount of debt by reason of being a parent, subsidiary, or affiliate of the creditor~~
49 ~~corporation, may deduct from the debt included a proportionate part determined on the basis of~~
50 ~~the ratio of the borrowed capital of the creditor corporation to the total assets of the creditor~~
51 ~~corporation. If the creditor corporation is also taxable under the provisions of this section, the~~

1 creditor corporation is allowed to deduct from the total of its capital, surplus, and undivided
2 profits the amount of any debt owed to it by a parent, subsidiary or affiliated corporation to the
3 extent that the debt has been included in the tax base of the parent, subsidiary, or affiliated
4 debtor corporation reporting for taxation under the provisions of this section.

5 (b1) The following definitions apply in ~~this subsection~~: subsection (b) of this section:

6 (1) Affiliate. – The same meaning as specified in G.S. 105-130.6.

7 (2) Indebtedness. – All loans, credits, goods, supplies, or other capital of
8 whatsoever nature furnished by a parent, subsidiary, or affiliated
9 corporation, other than indebtedness endorsed, guaranteed, or otherwise
10 supported by one of these corporations.

11 (3) Parent. – The same meaning as specified in G.S. 105-130.6.

12 (4) Subsidiary. – The same meaning as specified in G.S. 105-130.6.

13 (b2) Capital Base for Noncorporate Business Entity. – A business entity that is not a
14 corporation must determine its net worth. Its net worth is equal to its members' and partners'
15 capital accounts, computed in accordance with generally accepted accounting principles. If the
16 business entity does not maintain its book and records in accordance with generally accepted
17 accounting principles, its net worth is computed in accordance with the accounting method
18 used by the entity for federal tax purposes, so long as the method fairly reflects the taxpayer's
19 net worth for purposes of the tax levied by this section. A business entity must add to its net
20 worth all indebtedness owed to it by a related person, as defined in G.S. 105-163.010.

21 (c) Repealed by Session Laws 2007-491, s. 2, effective January 1, 2008.

22 (c1) Apportionment. – A business entity that is doing business in this State and in one or
23 more other states must apportion its tax base to this State. A corporation that is subject to
24 income tax under Article 4 of this Chapter must use the fraction it applies in apportioning its
25 income under that Article. A business entity that is not subject to income tax under Article 4 of
26 this Chapter must apportion its net worth by using the fraction it would be required to apply in
27 apportioning its income if it were subject to that Article. A business entity that believes this
28 apportionment method subjects a greater portion of its net worth to tax under this section than
29 is attributable to its business in this State may make a written request to the Secretary for
30 permission to use an alternative method of apportionment, in the same manner as provided in
31 G.S. 105-130.4(t1). A corporation that is doing business in this State and in one or more other
32 states must apportion its capital stock, surplus, and undivided profits to this State. A
33 corporation must use the apportionment method set out in subdivision (1) of this subsection
34 unless the Department has authorized it to use a different method under subdivision (2) of this
35 subsection. The portion of a corporation's capital stock, surplus, and undivided profits
36 determined by applying the appropriate apportionment method is considered the amount of
37 capital stock, surplus, and undivided profits the corporation uses in its business in this State.

38 (1) ~~Statutory. – A corporation that is subject to income tax under Article 4 of~~
39 ~~this Chapter must apportion its capital stock, surplus, and undivided profits~~
40 ~~by using the fraction it applies in apportioning its income under that Article.~~
41 ~~A corporation that is not subject to income tax under Article 4 of this~~
42 ~~Chapter must apportion its capital stock, surplus, and undivided profits by~~
43 ~~using the fraction it would be required to apply in apportioning its income if~~
44 ~~it were subject to that Article. The apportionment method set out in this~~
45 ~~subdivision is considered the statutory method of apportionment and is~~
46 ~~presumed to be the best method of determining the amount of a corporation's~~
47 ~~capital stock, surplus, and undivided profits attributable to the corporation's~~
48 ~~business in this State.~~

49 (2) ~~Alternative. – A corporation that believes the statutory apportionment~~
50 ~~method set out in subdivision (1) of this subsection subjects a greater portion~~
51 ~~of its capital stock, surplus, and undivided profits to tax under this section~~

1 than is attributable to its business in this State may make a written request to
2 the Secretary for permission to use an alternative method. The request must
3 set out the reasons for the corporation's belief and propose an alternative
4 method. The corporation has the burden of establishing by clear, cogent, and
5 convincing proof that the statutory apportionment method subjects a greater
6 portion of the corporation's capital stock, surplus, and undivided profits to
7 tax under this section than is attributable to its business in this State and that
8 the proposed alternative method is a better method of determining the
9 amount of the corporation's capital stock, surplus, and undivided profits
10 attributable to the corporation's business in this State.

11 The Secretary must issue a written decision on a corporation's request for
12 an alternative apportionment method. If the decision grants the request, it
13 must describe the alternative method the corporation is authorized to use and
14 state the tax years to which the alternative method applies. A decision may
15 apply to no more than three tax years. A corporation may renew a request to
16 use an alternative apportionment method by following the procedure in this
17 subdivision. A decision of the Secretary on a request for an alternative
18 apportionment method is final and is not subject to administrative or judicial
19 review. A corporation authorized to use an alternative method may apportion
20 its capital stock, surplus, and undivided profits in accordance with the
21 alternative method or the statutory method.

22 (d) Alternative Tax Base. – After determining the proportion of its total capital stock,
23 surplus and undivided profits as set out in subsection (c) of this section, which amount The tax
24 imposed by this section shall not be less than fifty-five percent (55%) of the appraised value as
25 determined for ad valorem taxation of all the real and tangible personal property in this State of
26 each corporation-business entity nor less than its total actual investment in tangible property in
27 this State, every corporation taxed under this section shall annually pay to the Secretary of
28 Revenue, at the time the report and statement are due, a franchise or privilege tax at the rate of
29 one dollar and fifty cents (\$1.50) per one thousand dollars (\$1,000) of the total amount of
30 capital stock, surplus and undivided profits as provided in this section. The tax imposed in this
31 section shall not be less than thirty five dollars (\$35.00) and shall be for the privilege of
32 carrying on, doing business, and/or the continuance of articles of incorporation or
33 domestication of each corporation in this State. Appraised value of tangible property including
34 real estate is the ad valorem valuation for the calendar year next preceding the due date of the
35 franchise tax return. The term 'total actual investment in tangible property' as used in this
36 section means the total original purchase price or consideration to the reporting taxpayer of its
37 tangible properties, including real estate, in this State plus additions and improvements thereto
38 less reserve for depreciation as permitted for income tax purposes, and also less any
39 indebtedness incurred and existing by virtue of the purchase of any real estate and any
40 permanent improvements made thereon. In computing 'total actual investment in tangible
41 personal property' there shall also be deducted reserves for the entire cost of any air-cleaning
42 device or sewage or waste treatment plant, including waste lagoons, and pollution abatement
43 equipment purchased or constructed and installed which reduces the amount of air or water
44 pollution resulting from the emission of air contaminants or the discharge of sewage and
45 industrial wastes or other polluting materials or substances into the outdoor atmosphere or into
46 streams, lakes, or rivers, upon condition that the corporation claiming this deduction shall
47 furnish to the Secretary a certificate from the Department of Environment and Natural
48 Resources or from a local air pollution control program for air-cleaning devices located in an
49 area where the Environmental Management Commission has certified a local air pollution
50 control program pursuant to G.S. 143-215.112 certifying that said Department or local air
51 pollution control program has found as a fact that the air-cleaning device, waste treatment plant

1 or pollution abatement equipment purchased or constructed and installed as above described
2 has actually been constructed and installed and that the device, plant or equipment complies
3 with the requirements of the Environmental Management Commission or local air pollution
4 control program with respect to the devices, plants or equipment, that the device, plant or
5 equipment is being effectively operated in accordance with the terms and conditions set forth in
6 the permit, certificate of approval, or other document of approval issued by the Environmental
7 Management Commission or local air pollution control program and that the primary purpose is
8 to reduce air or water pollution resulting from the emission of air contaminants or the discharge
9 of sewage and waste and not merely incidental to other purposes and functions. The cost of
10 constructing facilities of any private or public utility built for the purpose of providing sewer
11 service to residential and outlying areas is treated as deductible for the purposes of this section;
12 the deductible liability allowed by this section shall apply only with respect to pollution
13 abatement plants or equipment constructed or installed on or after January 1, 1955.

14 (d1) Credits. – A corporation is allowed a credit against the tax imposed by this section
15 for a taxable year equal to one-half of the amount of tax payable during the taxable year under
16 Article 5E of this Chapter. The credit allowed by this subsection may not exceed the amount of
17 tax imposed by this section for the taxable year, reduced by the sum of all other credits allowed
18 against that tax, except tax payments made by or on behalf of the taxpayer.

19 (e) Change in Income Year. – ~~Any corporation~~ A business entity which changes its
20 income year, and files a 'short period' income tax return pursuant to G.S. 105-130.15 shall file a
21 franchise tax return in accordance with the provisions of this section in the manner and as of
22 the date specified in subsection (a) of this section. ~~Such corporation shall be~~ The business entity
23 is entitled to deduct from the total franchise tax computed (on an annual basis) on such return
24 the amount of franchise tax previously paid which is applicable to the period subsequent to the
25 beginning of the new income year.

26 (f) ~~The report, statement and tax required by this section shall be in addition to all other~~
27 ~~reports required or taxes levied and assessed in this State.~~

28 (g) Prohibition on Local Tax. – Counties, cities and towns shall not levy a franchise tax
29 on ~~corporations~~ a business entity taxed under this section.

30 (h) Repealed by Session Laws 1981 (Regular Session, 1982), c. 1211, s. 5."

31 **SECTION 27B.2.(e)** G.S. 105-125(b) reads as rewritten:

32 "(b) Certain Investment Companies. – A ~~corporation~~ business entity doing business in
33 North Carolina that meets one or more of the following conditions may, in determining its basis
34 for franchise tax, deduct the aggregate market value of its investments in the stocks, bonds,
35 debentures, or other securities or evidences of debt of other corporations, partnerships,
36 individuals, municipalities, governmental agencies, or governments:

37 (1) A regulated investment company. – A regulated investment company is an
38 entity that qualifies as a regulated investment company under section 851 of
39 the Code.

40 (2) A REIT, unless the REIT is a captive REIT. – The terms 'REIT' and 'captive
41 REIT' have the same meanings as defined in G.S. 105-130.12."

42 **SECTION 27B.2.(f)** G.S. 105-127 reads as rewritten:

43 **"§ 105-127. When franchise or privilege taxes payable.**

44 (a) Tax Due. – The taxes imposed under this Article are due when a return is due. A
45 taxpayer may ask the Secretary for an extension of time to file a return under
46 G.S. 105-263. ~~Every corporation, domestic or foreign, from which a report is required by law to~~
47 ~~be made to the Secretary of Revenue, shall, unless otherwise provided, pay to said Secretary~~
48 ~~annually the franchise tax as required by G.S. 105-122.~~

49 (b) Repealed by Session Laws 1998-98, s. 78, effective August 14, 1998.

1 (e) ~~It shall be the duty of the treasurer or other officer having charge of any such~~
2 ~~corporation, domestic or foreign, upon which a tax is herein imposed, to transmit the amount of~~
3 ~~the tax due to the Secretary of Revenue within the time provided by law for payment of same.~~

4 (d), (e) Repealed by Session Laws 2002-72, s. 11, effective August 12, 2002.

5 (f) Dissolution. – After the end of the income year in which a domestic corporation is
6 dissolved pursuant to Article 14 of Chapter 55 of the General Statutes, the corporation is no
7 longer subject to the tax levied in this Article unless the Secretary of Revenue finds that the
8 corporation has engaged in business activities in this State not appropriate to winding up and
9 liquidating its business and affairs."

10 **SECTION 27B.2.(g)** G.S. 105-128 and G.S. 105-129 are repealed.

11 **SECTION 27B.2.(h)** This section is effective for taxable years beginning on or
12 after January 1, 2010.

13 14 **THROWBACK RULE**

15 **SECTION 27B.3.(a)** G.S. 105-130.4(1)(2) reads as rewritten:

16 "(2) Sales of tangible personal property are in this State if (i) the property is
17 received in this State by ~~the purchaser.~~ a purchaser other than the United
18 States government or (ii) the property is shipped from a place in this State
19 and the purchaser is the United States government or the taxpayer is not
20 taxable in the state of the purchaser. In the case of delivery of goods by
21 common carrier or by other means of transportation, including transportation
22 by the purchaser, the place at which the goods are ultimately received after
23 all transportation has been completed shall be considered as the place at
24 which the goods are received by the purchaser. Direct delivery into this State
25 by the taxpayer to a person or firm designated by a purchaser from within or
26 without the State shall constitute delivery to the purchaser in this State."

27 **SECTION 27B.3.(b)** This section is effective for taxable years beginning on or
28 after January 1, 2010.

29 30 **CONFORM BANK EXPENSE DEDUCTION**

31 **SECTION 27B.4.(a)** G.S. 105-130.5(a) is amended by adding a new subdivision to
32 read:

33 "(a) The following additions to federal taxable income shall be made in determining
34 State net income:

35 ...

36 (2a) That portion of a financial institution's interest expense that is allocable to
37 interest income exempt from taxation under this Part. The allocable portion
38 of the interest expense is the portion for which deduction would be
39 disallowed pursuant to section 265(b) of the Code if the interest were earned
40 on a tax-exempt obligation as defined in section 265(b) of the Code.

41"

42 **SECTION 27B.4.(b)** This section is effective for taxable years beginning on or
43 after January 1, 2010.

44 45 **PART XXVIIC. SALES TAX CHANGES**

46 47 **INCREASE STATE SALES TAX BY ONE-QUARTER CENT**

48 **SECTION 27C.1.(a)** The introductory language of G.S. 105-164.4(a) reads as
49 rewritten:

1 "(a) A privilege tax is imposed on a retailer at the following percentage rates of the
2 retailer's net taxable sales or gross receipts, as appropriate. The general rate of tax is four and
3 ~~one-half percent (4.5%)-three-quarters percent (4.75%)."~~

4 **SECTION 27C.1.(b)** Subsection (a) of this section increasing the general rate of
5 State sales tax does not apply to construction materials purchased to fulfill a lump-sum or
6 unit-price contract entered into or awarded before the effective date of the increase or entered
7 into or awarded pursuant to a bid made before the effective date of the increase when the
8 construction materials would otherwise be subject to the increased rate of tax provided under
9 that subsection.

10 **SECTION 27C.1.(c)** The introductory language of G.S. 105-164.4(a) reads as
11 rewritten:

12 "(a) A privilege tax is imposed on a retailer at the following percentage rates of the
13 retailer's net taxable sales or gross receipts, as appropriate. The general rate of tax is ~~four and~~
14 ~~three-quarters percent (4.75%)-five percent (5%)."~~

15 **SECTION 27C.1.(d)** Subsections (a) and (b) of this section become effective
16 August 1, 2009, and apply to sales made on or after that date. Subsection (a) of this section is
17 repealed October 1, 2009. Subsection (c) of this section is effective October 1, 2009, and
18 applies to sales made on or after that date. The remainder of this section is effective when it
19 becomes law. This section does not affect the rights or liabilities of the State, a taxpayer, or
20 another person arising under a statute amended or repealed by this section before the effective
21 date of its amendment or repeal; nor does it affect the right to any refund or credit of a tax that
22 accrued under the amended or repealed statute before the effective date of its amendment or
23 repeal.

24 25 NEXUS CLARIFICATION AND CLICK-THROUGHS

26 **SECTION 27C.2.(a)** G.S. 105-164.3(18) is recodified as G.S. 105-164.3(33g) and
27 reads as rewritten:

28 "§ 105-164.3. Definitions.

29 The following definitions apply in this Article:

30 ...

31 (33g) ~~Mail-order-Remote sale.~~ – A sale of tangible personal property, ordered by
32 mail, by telephone, computer link, via the Internet, or other-by another
33 similar method, to a purchaser who is in this State at the time the order is
34 remitted, from a retailer who receives the order in another state and
35 transports the property or causes it to be transported to a person in this State.
36 It is presumed that a resident of this State who remits an order was in this
37 State at the time the order was remitted.

38 "

39 **SECTION 27C.2.(b)** The catch line of G.S. 105-164.8 reads as rewritten:

40 "§ 105-164.8. **Retailer's obligation to collect tax; mail-order-remote sales subject to tax.**"

41 **SECTION 27C.2.(c)** G.S. 105-164.8(b) reads as rewritten:

42 "(b) ~~Mail-Order-Remote Sales.~~ – A retailer who makes a ~~mail-order-remote~~ sale is
43 engaged in business in this State and is subject to the tax levied under this Article if at least one
44 of the following conditions is met:

- 45 (1) The retailer is a corporation engaged in business under the laws of this State
46 or a person domiciled in, a resident of, or a citizen of, this State.
- 47 (2) The retailer maintains retail establishments or offices in this State, whether
48 the ~~mail-order-remote~~ sales thus subject to taxation by this State result from
49 or are related in any other way to the activities of ~~such-the~~ establishments or
50 offices.

- 1 (3) The retailer ~~has representatives in this State who solicit business or transact~~
2 ~~business on behalf of the retailer, solicits or transacts business in this State~~
3 by employees, independent contractors, agents, or other representatives
4 whether the ~~mail order remote~~ sales thus subject to taxation by this State
5 result from or are related in any other way to such the solicitation or
6 transaction of business. A retailer is presumed to be soliciting or transacting
7 business by an independent contractor, agent, or other representative if the
8 retailer enters into an agreement with a resident of this State under which the
9 resident, for a commission or other consideration, directly or indirectly refers
10 potential customers, whether by a link on an Internet Web site or otherwise,
11 to the retailer, if the cumulative gross receipts from sales by the retailer to
12 purchasers in this State who are referred to the retailer by all residents with
13 this type of agreement with the retailer is in excess of ten thousand dollars
14 (\$10,000) during the preceding four quarterly periods. This presumption
15 may be rebutted by proof that the resident with whom the retailer has an
16 agreement did not engage in any solicitation in the State on behalf of the
17 seller that would satisfy the nexus requirement of the United States
18 Constitution during the four quarterly periods in question.
- 19 (4) Repealed by Session Laws 1991, c. 45, s. 16.
- 20 (5) The retailer, by purposefully or systematically exploiting the market
21 provided by this State by any media-assisted, media-facilitated, or
22 media-solicited means, including direct mail advertising, distribution of
23 catalogs, computer-assisted shopping, television, radio or other electronic
24 media, telephone solicitation, magazine or newspaper advertisements, or
25 other media, creates nexus with this State.
- 26 (6) Through compact or reciprocity with another jurisdiction of the United
27 States, that jurisdiction uses its taxing power and its jurisdiction over the
28 retailer in support of this State's taxing power.
- 29 (7) The retailer consents, expressly or by implication, to the imposition of the
30 tax imposed by this Article. For purposes of this subdivision, evidence that a
31 retailer engaged in the activity described in subdivision (5) ~~shall be~~ is prima
32 facie evidence that the retailer consents to the imposition of the tax imposed
33 by this Article.
- 34 (8) The retailer is a holder of a wine shipper permit issued by the ABC
35 Commission pursuant to G.S. 18B-1001.1."

36 **SECTION 27C.2.(d)** This section is effective when it becomes law.

37 38 SALES TAX BASE EXPANSION

39 **SECTION 27C.3.(a)** G.S. 105-37.1, 105-38.1, and 105-40 are repealed.

40 **SECTION 27C.3.(b)** G.S. 105-164.3 reads as rewritten:

41 "§ 105-164.3. Definitions.

42 The following definitions apply in this Article:

43 ...

44 (1b) Audio work. – A series of musical, spoken, or other sounds, including a
45 ringtone.

46 (1c) Audiovisual. – A series of related images and any sounds accompanying the
47 images that impart an impression of motion when shown in succession.

48 ~~(1b)~~(1d) Bundled transaction. – A retail sale of two or more distinct and identifiable
49 products, at least one of which is taxable and one of which is exempt, for
50 one nonitemized price. Products are not sold for one nonitemized price if an
51 invoice or another sales document made available to the purchaser separately

- 1 identifies the price of each product. A bundled transaction does not include
 2 the retail sale of any of the following:
- 3 a. A product and any packaging item that accompanies the product and
 4 is exempt under G.S. 105-164.13(23).
 - 5 b. A sale of two or more products whose combined price varies, or is
 6 negotiable, depending on the products the purchaser selects.
 - 7 c. A sale of a product accompanied by a transfer of another product
 8 with no additional consideration.
 - 9 d. A product and the delivery or installation of the product.
 - 10 e. A product and any service necessary to complete the sale.
- 11 ~~(1d)~~(1e) Business. – Includes any activity engaged in by any person or caused to be
 12 engaged in by him with the object of gain, profit, benefit or advantage, either
 13 direct or indirect. The term 'business' shall not be construed in this Article to
 14 include occasional and isolated sales or transactions by a person who does
 15 not hold himself out as engaged in business.
- 16 ...
- 17 (7a) Digital code. – A code that gives a purchaser of the code a right to receive an
 18 item by electronic delivery or electronic access. A digital code may be
 19 obtained by an electronic means or by a tangible means. A digital code does
 20 not include a gift certificate or a gift card.
- 21 ~~(7a)~~(7h) Direct mail. – Printed material delivered or distributed by the United States
 22 Postal Service or other delivery service to a mass audience or to addresses
 23 on a mailing list provided by the purchaser or at the direction of the
 24 purchaser when the cost of the items is not billed directly to the recipients.
 25 The term includes tangible personal property supplied directly or indirectly
 26 by the purchaser to the direct mail seller for inclusion in the package
 27 containing the printed material. The term does not include multiple items of
 28 printed material delivered to a single address.
- 29 ...
- 30 (33e) Repair, maintenance, and installation services. – The term includes the
 31 activities listed in this subdivision:
- 32 a. Repairing tangible personal property to restore it to proper working
 33 order.
 - 34 b. Maintaining tangible personal property to keep the property in
 35 working order, to avoid breakdown, or to prevent unnecessary
 36 repairs.
 - 37 c. Installing tangible personal property.
- 38 ...
- 39 (35f) Ringtone. – A digitized sound file that is downloaded onto a device and that
 40 may be used to alert the user of the device with respect to a communication.
- 41 (36) Sale or selling. – The transfer of title or possession of ~~tangible personal~~
 42 ~~property, an item,~~ conditional or otherwise, in any manner or by any means
 43 whatsoever, for a consideration paid or to be paid. ~~The~~ ~~The~~ term includes the
 44 ~~fabrication~~ following:
- 45 a. Fabrication of tangible personal property for consumers by persons
 46 engaged in business who furnish either directly or indirectly the
 47 materials used in the fabrication work. ~~The term also includes the~~
 48 ~~furnishing~~
 - 49 b. Furnishing or preparing for a consideration of ~~any~~ tangible personal
 50 property consumed on the premises of the person furnishing or

preparing the property or consumed at the place at which the property is furnished or prepared. ~~The term also includes a~~

c. A transaction in which the possession of the property an item is transferred but the seller retains title or security for the payment of the consideration.

d. Transfer of a digital code.

~~If a retailer engaged in the business of selling prepared food and drink for immediate or on premises consumption also gives prepared food or drink to its patrons or employees free of charge, for the purposes of this Article the property given away is considered sold along with the property sold. If a retailer gives an item of inventory to a customer free of charge on the condition that the customer purchase similar or related property, the item given away is considered sold along with the item sold. In all other cases, property given away or used by any retailer or wholesale merchant is not considered sold, whether or not the retailer or wholesale merchant recovers its cost of the property from sales of other property.~~

...

(38b) Service contract. – A warranty agreement, a maintenance agreement, a repair contract, or a similar agreement or contract by which the seller agrees to maintain or repair tangible personal property.

...."

SECTION 27C.3.(c) G.S. 105-164.4(a), as amended by Section 3.1 of this act, reads as rewritten:

"(a) A privilege tax is imposed on a retailer at the following percentage rates of the retailer's net taxable sales or gross receipts, as appropriate. The general rate of tax is five percent (5%).

...

(6b) The general rate applies to the sales price of an item that is listed in this subdivision, is delivered or accessed electronically, and would be taxable under this Article if sold in a tangible medium. The tax applies regardless of whether the purchaser of the item has a right to use it permanently or to use it without making continued payments. The tax does not apply to telecommunications service, video programming service, satellite digital audio radio service, or any other service that is taxed under another subdivision of this subsection. A person who sells an item that is taxable under this subdivision is considered a retailer under this Article. The following items are subject to tax under this subdivision:

a. An audio work.

b. An audiovisual work.

c. A book.

...

(9) The general rate of tax applies to the gross receipts derived from a service contract and from repair, maintenance, and installation services.

(10) The general rate of tax applies to the gross receipts from charges for any of the activities listed in this subdivision. Gross receipts may take the form of a single or multioccasion ticket, a seasonal pass, a permanent seat license, a charge for a luxury suite, a cover charge, a membership fee, periodic dues, or any other form of payment. A person engaged in the business of providing any of these activities is considered a retailer under this Article:

a. Admission to a live performance or other live event of any kind.

b. Admission to a movie or other audiovisual work.

(11) The general rate of tax applies to the gross receipts derived from providing air, surface, or combined courier delivery services of parcels."

SECTION 27C.3.(d) Part 2 of Article 5 of Chapter 105 of the General Statutes is amended by adding a new section to read:

"§ 105-164.4E. When an item given away is considered sold.

An item that is given away or used by a retailer or a wholesale merchant is not considered sold, whether or not the retailer or wholesale merchant receives its cost of the item from sales of other items, except as follows:

(1) If a retailer engaged in the business of selling prepared food and drink for immediate or on-premises consumption also gives prepared food or drink to its patrons or employees free of charge, for the purposes of this Article the property given away is considered sold along with the property sold.

(2) If a retailer gives an item of inventory to a customer free of charge on the condition that the customer purchase similar or related property, the item given away is considered sold along with the item sold."

SECTION 27C.3.(e) G.S. 105-164.7 reads as rewritten:

"§ 105-164.7. ~~Sales tax part of purchase price.~~Retailer to collect sales tax from purchaser as trustee for State.

~~Every retailer subject to the tax levied in G.S. 105-164.4 shall at the time of selling or delivering or taking an order for the sale or delivery of taxable tangible personal property or a taxable service, or collecting the sales price, add to the sales price the amount of tax due. The tax constitutes a part of the purchase price, is a debt from the purchaser to the retailer until paid, and is recoverable at law in the same manner as other debts. The tax must be stated and charged separately from the sales price, shown separately on the retailer's sales records, and paid by the purchaser to the retailer as trustee for and on account of the State. The retailer is liable for the collection of the tax and for its payment to the Secretary. The retailer's failure to charge the tax to or to collect the tax from the purchaser does not affect this liability. It is the intent of this Article that the tax be added to the sales price of tangible personal property and services when sold at retail and be borne and passed on to the customer, instead of being borne by the retailer.~~

The sales tax imposed by this Article is intended to be passed on to the purchaser of a taxable item and borne by the purchaser instead of by the retailer. A retailer must collect the tax due on an item when the item is sold at retail. The tax is a debt from the purchaser to the retailer until paid and is recoverable at law by the retailer in the same manner as other debts. A retailer is considered to act as a trustee on behalf of the State when it collects tax from the purchaser of a taxable item."

SECTION 27C.3.(f) G.S. 105-164.13 reads as rewritten:

"§ 105-164.13. Retail sales and use tax.

~~The sale at retail and the use, storage, or consumption in this State of the following tangible personal property and services items~~ are specifically exempted from the tax imposed by this Article:

...
(25) ~~Sales by merchants~~a merchant on the Cherokee Indian Reservation ~~when such merchants are who~~ is authorized to do business on the Reservation and ~~are paying~~pays the tribal gross receipts levy to the Tribal Council.

...
(60) A service contract for, and the repair, maintenance, or installation of, an item that is exempt from tax under this Article, other than an item exempt from tax under G.S. 105-164.13(32).

(61) Admission charges to any of the following recreational or entertainment activities:

a. An event at an elementary or secondary school.

- 1 b. A commercial agricultural fair that meets the requirements of
 2 G.S. 106-520.1, as determined by the Commissioner of Agriculture.
 3 c. A festival or other recreational or entertainment activity that lasts no
 4 more than seven consecutive days and is sponsored by a nonprofit
 5 entity that is exempt from tax under Article 4 of this Chapter and
 6 uses the entire proceeds of the activity exclusively for the entity's
 7 nonprofit purpose. This exemption applies to no more than two
 8 activities sponsored by the entity during a calendar year.
 9 d. An entertainment activity produced by local talent exclusively, for
 10 the benefit of religious, charitable, benevolent, or educational
 11 purposes, as long as no compensation is paid to the local talent.
 12 e. The North Carolina Symphony Society, Incorporated, as specified in
 13 G.S. 140-10.1.
 14 f. All outdoor historical dramas, as specified in Article 19C of Chapter
 15 143 of the General Statutes.
 16 g. A youth athletic contest with an admissions price that does not
 17 exceed ten dollars (\$10.00) sponsored by a person exempt from
 18 income tax under Article 4 of this Chapter. For the purpose of this
 19 sub-subdivision, a youth athletic contest means a contest in which
 20 each participating athlete is less than 20 years of age.
 21 h. A choral or theatrical performance promoted and managed by a
 22 nonprofit entity that is exempt from tax under Article 4 of this
 23 Chapter.
 24 i. A recreational or an entertainment activity exclusively for teenagers
 25 and sponsored by a nonprofit entity that is exempt from tax under
 26 Article 4 of this Chapter.
 27 j. A farm-related entertainment activity offered on land used for bona
 28 fade farm purposes as defined in G.S. 153A-340."

29 **SECTION 27C.3.(g)** G.S. 105-467(a) is amended by adding two new subdivisions

30 to read:

- 31 "(8) The sales price of an item that is delivered or accessed electronically and is
 32 subject to the general rate of tax under G.S. 105-164.4(a)(6b).
 33 (9) The gross receipts derived from providing a service subject to the general
 34 rate of tax under G.S. 105-164.4(a)(9), (a)(10), or (a)(11)."

35 **SECTION 27C.3.(h)** Section 4 of Chapter 1096 of the 1967 Session Laws, as
 36 amended, reads as rewritten:

37 "Sec. 4. Scope of Sales Tax. The sales tax which may be imposed under this division after
 38 the holding of a special election is limited to a tax at the rate of one per cent (1%) of: (1) the
 39 sale price of ~~those articles of tangible personal property now the items~~ subject to the general
 40 rate of sales tax imposed by the State under ~~G.S. 105-164.4(a)(1) and (4b);~~ G.S. 105-164.4(a)(1),
 41 (4b), and (6b); (2) the gross receipts derived from the lease or rental of tangible personal
 42 property when the lease or rental of the property is subject to the general rate of sales tax
 43 imposed by the State under G.S. 105-164.4(a)(2); (3) the gross receipts derived from the rental
 44 of any room or lodging furnished by any hotel, motel, inn, tourist camp or other similar public
 45 accommodations now subject to the general rate of sales tax imposed by the State under G. S.
 46 105-164.4(a)(3); (4) the gross receipts derived from services rendered by laundries, dry
 47 cleaners, cleaning plants and similar type businesses now subject to the general rate of sales tax
 48 imposed by the State under G.S. 105-164.4(a)(4); (5) The sales price of food and other items
 49 that are not otherwise exempt from tax pursuant to G.S. 105-164.13 but are exempt from the
 50 State sales and use tax pursuant to G.S. 105-164.13B; ~~and~~ (6) The sales price of prepaid
 51 telephone calling service taxed as tangible personal property under ~~G.S. 105-164.4(a)(4d).~~ G.S.

1 105-164.4(a)(4d); and (7) The gross receipts derived from providing a service subject to the
2 general rate of tax under G.S. 105-164.4(a)(9), (a)(10), or (a)(11). The sales price of prepaid
3 telephone calling service taxed as tangible personal property under G.S. 105-164.4(a)(4d). The
4 taxes authorized by this division do not apply to sales that are taxable by the State under
5 G.S. 105-164.4 but are not specifically listed in this section.

6 The exemptions and exclusions contained in G.S. 105-164.13 and the sales and use tax
7 holiday contained in G.S. 105-164.13C and G.S. 105-164.13D apply with equal force and like
8 manner to the local sales tax authorized to be imposed and levied under this division. The
9 county shall have no authority, with respect to the local sales and use tax imposed under this
10 division, to change, alter, add, or delete any exemptions or exclusions contained under
11 G.S. 105-164.13.

12 The local sales tax authorized to be imposed and levied under the provisions of this division
13 shall be applicable to such retail sales, leases, rentals, rendering of services, furnishing of
14 lodging or accommodations and other taxable transactions which are made, furnished or
15 rendered by retailers whose place of business is located within the taxing county. The tax
16 imposed shall apply to the furnishing of rooms, lodging or other accommodations within the
17 county which are rented to transients. The sourcing principles in G.S. 105-164.4B apply in
18 determining whether the local sales tax applies to a transaction. Provided, however, no tax shall
19 be imposed where the tangible personal property sold is delivered by the retailer or his agent to
20 the purchaser at a point outside this State."

21 **SECTION 27C.3.(i)** This section becomes effective October 1, 2009, and applies
22 to sales occurring on or after that date. This act does not affect the rights or liabilities of the
23 State, a taxpayer, or another person arising under a statute amended or repealed by this act
24 before the effective date of its amendment or repeal; nor does it affect the right to any refund or
25 credit of a tax that accrued under the amended or repealed statute before the effective date of its
26 amendment or repeal. G.S. 105-164.4(a)(10), as enacted by this section, applies to gross
27 receipts received from admissions purchased on or after that date and to gross receipts received
28 on or after that date from other recreational and entertainment activities occurring on or after
29 that date.

30 31 **PART XXVIII. ALCOHOL EXCISE TAX CHANGE**

32 33 **INCREASE TAX ON LIQUOR**

34 **SECTION 27D.2.(a)** G.S. 105-113.80(c) reads as rewritten:

35 "(c) Liquor. – An excise tax of ~~twenty five percent (25%)~~ twenty-six and one-half
36 percent (26.5%) is levied on liquor sold in ABC stores. Pursuant to G.S. 18B-804(b), the price
37 of liquor on which this tax is computed is the distiller's price plus (i) the State ABC warehouse
38 freight and bailment charges, and (ii) a markup for local ABC boards."

39 **SECTION 27D.2.(b)** This section becomes effective August 1, 2009.

40