

GENERAL ASSEMBLY OF NORTH CAROLINA
SESSION 2017

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HOUSE BILL DRH30149-SV-7 (02/27)

Short Title: Tax Reduction Act of 2017.

(Public)

Sponsors: Representatives Szoka, Saine, Brawley, and S. Martin (Primary Sponsors).

Referred to:

A BILL TO BE ENTITLED

AN ACT TO INCREASE THE STANDARD DEDUCTION, TO EXEMPT MILL MACHINERY FROM TAX, AND TO SIMPLIFY THE FRANCHISE TAX CALCULATION BY ELIMINATING THE REQUIREMENT THAT A CORPORATION CALCULATE THE APPRAISED VALUE OF ITS REAL AND TANGIBLE PROPERTY AND ITS TOTAL ACTUAL INVESTMENT IN TANGIBLE PROPERTY FOR PURPOSES OF DETERMINING ITS FRANCHISE TAX BASE.

The General Assembly of North Carolina enacts:

PART I. INCREASE STANDARD DEDUCTION

SECTION 1.1. G.S. 105-153.5(a)(1) reads as rewritten:

"(a) Deduction Amount. – In calculating North Carolina taxable income, a taxpayer may deduct from adjusted gross income either the standard deduction amount provided in subdivision (1) of this subsection or the itemized deduction amount provided in subdivision (2) of this subsection that the taxpayer claimed under the Code. The deduction amounts are as follows:

- (1) Standard deduction amount. – The standard deduction amount is zero for a person who is not eligible for a standard deduction under section 63 of the Code. For all other taxpayers, the standard deduction amount is equal to the amount listed in the table below based on the taxpayer's filing status:

Filing Status	Standard Deduction
Married, filing jointly/surviving spouse	\$17,500 \$18,500
Head of Household	14,000 14,800
Single	8,750 9,250
Married, filing separately	8,750 9,250."

SECTION 1.2. This Part is effective for taxable years beginning on or after January 1, 2018.

PART II. EXEMPT MILL MACHINERY FROM TAX

SECTION 2.1.(a) Article 5F of Chapter 105 of the General Statutes and G.S. 105-164.13(5a) are repealed.

SECTION 2.1.(b) G.S. 105-164.4I(b) reads as rewritten:

"(b) Exemptions. – The tax imposed by this section does not apply to the sales price of or the gross receipts derived from a service contract applicable to any of the following items:

- (1) An item exempt from tax under this Article.



- 1 (2) A transmission, distribution, or other network asset contained on
2 utility-owned land, right-of-way, or easement.
- 3 (3) A transmission, an engine, rear-end gears, and any other item purchased by a
4 professional motorsports racing team or a related member of a team for
5 which the team may receive a sales tax refund under
6 G.S. 105-164.14A(a)(5). This subdivision expires January 1, 2020.
- 7 (4) ~~An item subject to tax under Article 5F of Chapter 105 of the General~~
8 ~~Statutes.~~
- 9 (5) A qualified aircraft or a qualified jet engine."

10 **SECTION 2.2.** G.S. 105-164.13 is amended by adding the following new
11 subdivisions to read:

12 **"§ 105-164.13. Retail sales and use tax.**

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

- 16 ...
- 17 (5e) Sales of mill machinery or mill machinery parts or accessories to any of the
18 following:
- 19 a. A manufacturing industry or plant. A manufacturing industry or plant
20 does not include (i) a delicatessen, cafe, cafeteria, restaurant, or
21 another similar retailer that is principally engaged in the retail sale of
22 foods prepared by it for consumption on or off its premises or (ii) a
23 production company.
- 24 b. A contractor or subcontractor if the purchase is for use in the
25 performance of a contract with a manufacturing industry or plant.
- 26 c. A subcontractor if the purchase is for use in the performance of a
27 contract with a general contractor that has a contract with a
28 manufacturing industry or plant.
- 29 (5f) Sales to a major recycling facility of any of the following tangible personal
30 property for use in connection with the facility:
- 31 a. Cranes, structural steel crane support systems, and foundations
32 related to the cranes and support systems.
- 33 b. Port and dock facilities.
- 34 c. Rail equipment.
- 35 d. Material handling equipment.
- 36 (5g) Sales of equipment, or an attachment or repair part for equipment, that meets
37 all of the following requirements:
- 38 a. Is sold to a company primarily engaged at the establishment in
39 research and development activities in the physical, engineering, and
40 life sciences included in industry group 54171 of NAICS.
- 41 b. Is capitalized by the company for tax purposes under the Code.
- 42 c. Is used by the company at the establishment in the research and
43 development of tangible personal property.
- 44 (5h) Sales of equipment, or an attachment or repair part for equipment, that meets
45 all of the following requirements:
- 46 a. Is sold to a company primarily engaged at the establishment in
47 software publishing activities included in industry group 5112 of
48 NAICS.
- 49 b. Is capitalized by the company for tax purposes under the Code.
- 50 c. Is used by the company at the establishment in the research and
51 development of tangible personal property.

- 1 (5i) Sales of equipment, or an attachment or repair part for equipment, that meets
2 all of the following requirements:
3 a. Is sold to a company primarily engaged at the establishment in
4 industrial machinery refurbishing activities included in industry
5 group 811310 of NAICS.
6 b. Is capitalized by the company for tax purposes under the Code.
7 c. Is used by the company at the establishment in repairing or
8 refurbishing tangible personal property.
9 (5j) Sales of the following to a company located at a ports facility for waterborne
10 commerce:
11 a. Machinery and equipment that is used at the facility to unload or to
12 facilitate the unloading or processing of bulk cargo to make it
13 suitable for delivery to and use by manufacturing facilities.
14 b. Parts, accessories, or attachments used to maintain, repair, replace,
15 upgrade, improve, or otherwise modify such machinery and
16 equipment.
17 (5k) Sales of equipment, or an attachment or repair part for equipment, that meets
18 all of the following requirements:
19 a. Is sold to a person that gathers and obtains ferrous metals, nonferrous
20 metals, and items that have served their original economic purpose
21 and that converts them by processes, including sorting, cutting,
22 classifying, cleaning, baling, wrapping, shredding, or shearing into a
23 new or different product for sale consisting of prepared grades.
24 b. Is capitalized by the person for tax purposes under the Code.
25 c. Is used by the person in a conversion process described in this
26 subdivision.
27 d. Is not a motor vehicle or an attachment or repair part for a motor
28 vehicle.
29 (5l) Sales of equipment, or an attachment or repair part for equipment, that meets
30 all of the following requirements:
31 a. Is sold to a company primarily engaged at the establishment in
32 processing tangible personal property for the purpose of extracting
33 precious metals, as defined in G.S. 66-406, to determine the value for
34 potential purchase.
35 b. Is capitalized by the company for tax purposes under the Code.
36 c. Is used by the company in the process described in this subdivision.
37 (5m) Sales of equipment, or an attachment or repair part for equipment, that meets
38 all of the following requirements:
39 a. Is sold to a company that is engaged in the fabrication of metal work
40 and that has annual gross receipts, including the gross receipts of all
41 related persons, as defined in G.S. 105-163.010, from the fabrication
42 of metal work of at least eight million dollars (\$8,000,000).
43 b. Is capitalized by the company for tax purposes under the Code.
44 c. Is used by the company at the establishment in the fabrication or
45 manufacture of metal products or used by the company to create
46 equipment for the fabrication or manufacture of metal products.
47 (5n) Sales of equipment, or an accessory, an attachment, or a repair part for
48 equipment, that meets all of the following requirements:
49 a. Is sold to a large manufacturing and distribution facility.
50 b. Is used in the manufacturing process, the assembly process, or the
51 distribution process.

1 c. Is not electricity.

2 If the level of investment or employment required by G.S. 105-164.3(16f)b.
3 is not timely made, achieved, or maintained, then the exemption provided
4 under this subdivision is forfeited. If the exemption is forfeited due to a
5 failure to timely make the required investment or to timely achieve the
6 minimum required employment level, then the exemption provided under
7 this subdivision is forfeited on all purchases. If the exemption is forfeited
8 due to a failure to maintain the minimum required employment level once
9 that level has been achieved, then the exemption provided under this
10 subdivision is forfeited for those purchases occurring on or after the date the
11 taxpayer fails to maintain the minimum required employment level. A
12 taxpayer that forfeits an exemption under this subdivision is liable for all
13 past sales and use taxes avoided as a result of the forfeiture, computed at the
14 applicable State and local rates from the date the taxes would otherwise have
15 been due, plus interest at the rate established under G.S. 105-241.21. Interest
16 is computed from the date the sales or use tax would otherwise have been
17 due. The past taxes and interest are due 30 days after the date of forfeiture. A
18 taxpayer that fails to pay the past taxes and interest by the due date is subject
19 to the provisions of G.S. 105-236. This subdivision expires for sales
20 occurring on or after July 1, 2018.

21 (5o) Sales of repair or replacement parts for a ready-mix concrete mill, regardless
22 of whether the mill is freestanding or affixed to a motor vehicle, to a
23 company that primarily sells ready-mix concrete.

24 "

25 **SECTION 2.3.** G.S. 105-164.3 is amended by adding a new subdivision to read:

26 "(16f) Large manufacturing and distribution facility. – A facility that satisfies both
27 of the following conditions:

28 a. The facility is used primarily for manufacturing or assembling
29 products and distributing finished products.

30 b. The Secretary of Commerce has certified that an investment of
31 private funds of at least eighty million dollars (\$80,000,000) has been
32 or will be made in real and tangible personal property for the facility
33 within five years after the date on which the first property investment
34 is made and that the facility will achieve an employment level of at
35 least 550 within five years after the date the facility is placed into
36 service and maintain that minimum level of employment throughout
37 its operation."

38 **SECTION 2.4.** Sales of mill machinery to manufacturers and certain industrial
39 processors have historically enjoyed preferential tax treatment, whether in the form of a
40 reduced wholesale tax, a preferential rate of sales and use tax, or a one-percent (1%) privilege
41 tax with an eighty-dollar (\$80.00) cap per article. Despite the nature of the tax, the operational
42 language has remained virtually unchanged for over 60 years and lacks clear guidance with
43 regard to its application. Specifically, Article 5F of Chapter 105 of the General Statutes, and its
44 predecessors, did not define "manufacturing industry or plant" or "mill machinery." This lack
45 of guidance has resulted in a substantial body of administrative interpretation being developed
46 over the years by the Department of Revenue. These interpretations are not included in the
47 statutes and may not necessarily comport with the traditional definition of manufacturing, but
48 they may be consistent with the General Assembly's intent to provide preferential tax treatment
49 to certain industrial equipment.

50 This act repeals the one-percent (1%) privilege tax on mill machinery and mill
51 machinery parts and accessories and substitutes a sales and use tax exemption for same said

1 items. However, the General Assembly recognizes that, once this transition has occurred,
2 efforts need to be made to provide more guidance and specificity to taxpayers and the
3 Department of Revenue with respect to the treatment of manufacturing and industrial
4 processing equipment. Therefore, the Revenue Laws Study Committee is directed to study
5 ways in which to clarify the scope of the sales and use tax exemption for mill machinery, as
6 enacted by this act, by modernizing and further defining the statutory language and by
7 incorporating existing administrative interpretations of the Department of Revenue, to the
8 extent the General Assembly desires to maintain those interpretations.

9 The Committee may report its findings, together with any recommended legislation,
10 to the 2018 Regular Session of the 2017 General Assembly upon its convening. The study may
11 include an examination of the following:

- 12 (1) The criteria that had to be met under prior law to qualify for the preferential
13 rate under Article 5F of Chapter 105 of the General Statutes and whether
14 that criteria should be incorporated into or otherwise clarified in the
15 corresponding sales and use tax exemption, as enacted by this act, including
16 the following:
 - 17 a. What constitutes an eligible manufacturer or industrial processor.
 - 18 b. The extent to which a business's activities must consist of
19 manufacturing or processing items for sale in order for the sales and
20 use tax exemption, as enacted by this act, to apply.
 - 21 c. The types of activities that qualify as manufacturing or industrial
22 processing.
 - 23 d. The types of machinery, parts, accessories, and other supplies that
24 are eligible for the exemption and the degree to which they must be
25 used in that process to qualify.
- 26 (2) A review of the Department's administrative interpretations of the mill
27 machinery statute, in all its forms, and whether and how to incorporate those
28 interpretations into the statutes.
- 29 (3) Terminology used by surrounding states in their statutory provisions that
30 provide a sales and use tax exemption for manufacturing equipment.
- 31 (4) Any other issues the Committee deems relevant.

32 **SECTION 2.5.** Sections 2.1, 2.2, and 2.3 of this Part become effective July 1,
33 2017, and apply to sales made on or after that date. The remainder of this Part is effective when
34 it becomes law.
35

36 **PART III. FRANCHISE TAX SIMPLIFICATION**

37 **SECTION 3.1.** G.S. 105-120.2 reads as rewritten:

38 **"§ 105-120.2. Franchise or privilege tax on holding companies.**

39 (a) Every corporation, domestic and foreign, incorporated or, by an act, domesticated
40 under the laws of this State or doing business in this State that, at the close of its taxable year, is
41 a holding company as defined in subsection (c) of this section, shall, pursuant to the provisions
42 of G.S. 105-122, do all of the following:

- 43 (1) File a return.
- 44 (2) Determine the total amount of its net worth.
- 45 (3) Apportion its net worth to this State.

46 (b) Tax Rate. – Every corporation taxed under this section shall annually pay to the
47 Secretary of Revenue, at the time the return is due, ~~the greater of the following:~~

- 48 (4) ~~A~~ a franchise or privilege tax at the rate of one dollar and fifty cents (\$1.50)
49 per one thousand dollars (\$1,000) of the amount determined under
50 subsection (a) of this section, but in no case shall the tax be more than one

- 1 hundred fifty thousand dollars (\$150,000) nor less than two hundred dollars
2 (\$200.00).
- 3 ~~(2) If the tax calculated under this subdivision exceeds the tax calculated under~~
4 ~~subdivision (1) of this subsection, then the tax is levied at the rate of one~~
5 ~~dollar and fifty cents (\$1.50) per one thousand dollars (\$1,000) on the~~
6 ~~greater of the following:~~
- 7 a. ~~Fifty five percent (55%) of the appraised value as determined for ad~~
8 ~~valorem taxation of all the real and tangible personal property in this~~
9 ~~State of each such corporation plus the total appraised value of~~
10 ~~intangible property returned for taxation of intangible personal~~
11 ~~property as computed under G.S. 105-122(d).~~
- 12 b. ~~The total actual investment in tangible property in this State of such~~
13 ~~corporation as computed under G.S. 105-122(d).~~
- 14 (c) For purposes of this section, a "holding company" is a corporation that satisfies at
15 least one of the following conditions:
- 16 (1) It has no assets other than ownership interests in corporations in which it
17 owns, directly or indirectly, more than fifty percent (50%) of the outstanding
18 voting stock or voting capital interests.
- 19 (2) It receives during its taxable year more than eighty percent (80%) of its
20 gross income from corporations in which it owns directly or indirectly more
21 than fifty percent (50%) of the outstanding voting stock or voting capital
22 interests.
- 23 (d) Repealed by Session Laws 1985, c. 656, s. 39.
- 24 (e) Counties, cities and towns shall not levy a franchise tax on corporations taxed under
25 this section. The tax imposed under the provisions of G.S. 105-122 shall not apply to
26 businesses taxed under the provisions of this section.
- 27 (f) Repealed by Session Laws 2011-330, s. 3, effective June 27, 2011."
- 28 **SECTION 3.2.** G.S. 105-122 reads as rewritten:
- 29 **"§ 105-122. Franchise or privilege tax on domestic and foreign corporations.**
- 30 (a) Tax Imposed. – An annual franchise or privilege tax is imposed on a corporation
31 doing business in this State. The tax is determined on the basis of the books and records of the
32 corporation as of the close of its income year. A corporation subject to the tax must file a return
33 under affirmation with the Secretary at the place and in the manner prescribed by the Secretary.
34 The return must be signed by the president, vice-president, treasurer, or chief financial officer
35 of the corporation. The return is due on or before the fifteenth day of the fourth month
36 following the end of the corporation's income year.
- 37 (b) Determination of Net Worth. – A corporation taxed under this section shall
38 determine the total amount of its net worth. The net worth of a corporation is its total assets
39 without regard to the deduction for accumulated depreciation, depletion, or amortization less its
40 total liabilities, computed in accordance with generally accepted accounting principles as of the
41 end of the corporation's taxable year. If the corporation does not maintain its books and records
42 in accordance with generally accepted accounting principles, then its net worth is computed in
43 accordance with the accounting method used by the entity for federal tax purposes so long as
44 the method fairly reflects the corporation's net worth for purposes of the tax levied by this
45 section. A corporation's net worth is subject to the following adjustments:
- 46 (1) A deduction for accumulated depreciation, depletion, and amortization as
47 determined in accordance with the method used for federal tax purposes.
- 48 (1a) Repealed by Session Laws 2015-241, s. 32.15(d), effective for taxable years
49 beginning on or after January 1, 2017, and applicable to the calculation of
50 franchise tax reported on the 2016 and later corporate income tax return.

1 (2) An addition for indebtedness the corporation owes to a parent, a subsidiary,
2 an affiliate, or a noncorporate entity in which the corporation or an affiliated
3 group of corporations owns directly or indirectly more than fifty percent
4 (50%) of the capital interests of the noncorporate entity. The amount added
5 back to the corporation's net worth may be further adjusted if part of the
6 capital of the creditor is capital borrowed from a source other than a parent,
7 a subsidiary, or an affiliate. The debtor corporation may deduct a
8 proportionate part of the indebtedness based on the ratio of the borrowed
9 capital of the creditor to the total assets of the creditor. For purposes of this
10 subdivision, borrowed capital does not include indebtedness incurred by a
11 bank arising out of the receipt of a deposit and evidenced by a certificate of
12 deposit, a passbook, a cashier's check, a certified check, or other similar
13 document.

14 (2a) If the creditor corporation is taxable under this Article, the creditor
15 corporation may deduct the amount of indebtedness owed to it by a parent,
16 subsidiary, or affiliated corporation to the extent that such indebtedness has
17 been added by the debtor corporation.

18 (3) A corporation may deduct the cost of treasury stock.

19 (4) through (8) Repealed by Session Laws 2015-241, s. 32.15(c), effective for
20 taxable years beginning on or after January 1, 2017, and applicable to the
21 calculation of franchise tax reported on the 2016 and later corporate income
22 tax return.

23 ...

24 (c1) Apportionment. – A corporation that is doing business in this State and in one or
25 more other states must apportion its net worth to this State. A corporation must use the
26 apportionment method set out in subdivision (1) of this subsection unless the Department has
27 authorized it to use a different method under subdivision (2) of this subsection. The portion of a
28 corporation's net worth determined by applying the appropriate apportionment method is
29 considered the amount of net worth the corporation uses in its business in this State:

30 ...

31 ~~(d) Tax Base and Tax Rate. – After determining the proportion of its net worth as set~~
32 ~~out in subsection (c1) of this section, which amount shall not be less than fifty five percent~~
33 ~~(55%) of the appraised value as determined for ad valorem taxation of all the real and tangible~~
34 ~~personal property in this State of each corporation nor less than its total actual investment in~~
35 ~~tangible property in this State, every~~ Every corporation taxed under this section shall annually
36 pay to the Secretary of Revenue, at the time the return is due, a franchise or privilege tax at the
37 rate of one dollar and fifty cents (\$1.50) per one thousand dollars (\$1,000) of the total amount
38 of net worth ~~as provided in this section.~~ worth, or the total amount of net worth apportioned to
39 this State if the corporation is doing business in this State and in one or more other states. The
40 tax imposed in this section shall not be less than two hundred dollars (\$200.00) and is for the
41 privilege of carrying on, doing business, and/or the continuance of articles of incorporation or
42 domestication of each corporation in this State. ~~Appraised value of tangible property including~~
43 ~~real estate is the ad valorem valuation for the calendar year next preceding the due date of the~~
44 ~~franchise tax return. The term "total actual investment in tangible property" as used in this~~
45 ~~section means the total original purchase price or consideration to the reporting taxpayer of its~~
46 ~~tangible properties, including real estate, in this State plus additions and improvements thereto~~
47 ~~less reserve for depreciation as permitted for income tax purposes.~~

48 (d1) Repealed by Session Laws 2015-241, s. 32.15(c), effective for taxable years
49 beginning on or after January 1, 2017, and applicable to the calculation of franchise tax
50 reported on the 2016 and later corporate income tax return.

1 (e) Short Period. – Any corporation which changes its income year, and files a "short
2 period" income tax return pursuant to G.S. 105-130.15 shall file a franchise tax return in
3 accordance with the provisions of this section in the manner and as of the date specified in
4 subsection (a) of this section. Such corporation shall be entitled to deduct from the total
5 franchise tax computed (on an annual basis) on such return the amount of franchise tax
6 previously paid which is applicable to the period subsequent to the beginning of the new
7 income year.

8 (f) Return and Tax. – The return and tax required by this section are in addition to all
9 other reports required or taxes levied and assessed in this State.

10 (g) Local Prohibition. – Counties, cities and towns shall not levy a franchise tax on
11 corporations taxed under this section.

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

13 **SECTION 3.3.** This Part is effective for taxable years beginning on or after
14 January 1, 2019, and applicable to the calculation of franchise tax reported on the 2018 and
15 later corporate income tax returns.

16
17 **PART IV. EFFECTIVE DATE**

18 **SECTION 4.** Except as otherwise provided, this act is effective when it becomes
19 law.