

GENERAL ASSEMBLY OF NORTH CAROLINA
SESSION 2005

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SENATE DRS65156-LY-168 (3/10)

Short Title: Study State Business Taxation.

(Public)

Sponsors: Senator Clodfelter.

Referred to:

A BILL TO BE ENTITLED

AN ACT DIRECTING THE REVENUE LAWS STUDY COMMITTEE TO STUDY A PROPOSAL TO REFORM AND SIMPLIFY STATE TAXATION OF BUSINESS ENTERPRISES AND APPROPRIATING FUNDS TO THE DEPARTMENT OF REVENUE FOR INFORMATION TECHNOLOGY NECESSARY TO ESTIMATE THE REVENUE IMPACT OF PROPOSALS TO IMPROVE STATE BUSINESS TAXATION.

The General Assembly of North Carolina enacts:

SECTION 1. Findings. – The General Assembly finds the following:

- (1) In recent years, several legislative study commissions have examined North Carolina's tax system and found that restructuring is needed to achieve fairness, efficiency, and simplicity in light of the changing economics and changing needs of our State.
- (2) The Governor's Commission to Modernize State Finances built on those studies, outlining in its 2002 report the new realities of the State and the ways in which the finance structure should be revised in order to respond to modern conditions so that economic growth can continue while adequate services are provided and the tax burden is shared equitably.
- (3) These studies have found that the corporate income tax is a volatile revenue source and is complicated by excessive tax credits and special adjustments. These studies have also found that the corporate income tax is undermined by taxing corporations as separate entities, rather than allowing combined or consolidated returns.
- (4) Recent years have seen the evolution of new corporate forms not adequately addressed by business tax laws, with the inequitable result that similar businesses are taxed differently based only on the type of

1 entity. To address one part of this problem, the Modernization
2 Commission recommended that the franchise tax apply to all types of
3 business entities and that the rate be reduced to minimize the tax
4 burden and share it fairly among businesses.

- 5 (5) The General Assembly has been unable to adequately evaluate
6 proposals for reforming and simplifying the taxation of businesses
7 because North Carolina lacks the technical ability to model and
8 estimate the effect of proposed changes on State and local budgets or
9 on business operations. In order to advance the goals of the
10 Modernization Commission and other study commissions to
11 modernize the taxation of businesses, it is necessary for the
12 Department of Revenue to develop the necessary technology to model
13 and forecast the impact of proposed changes.

14 **SECTION 2.** The Revenue Laws Study Committee shall study
15 comprehensive reform and simplification of the existing State taxes on business entities,
16 including corporations, limited liability companies, partnerships, business trusts,
17 associations, and other entities engaged in business. The elements of the plan to be
18 studied shall include the following:

- 19 (1) Repealing the corporate income tax, Part 1 of Article 4 of Chapter 105
20 of the General Statutes.
- 21 (2) Including all types of business entities under a revised form of the
22 franchise tax, Article 3 of Chapter 105 of the General Statutes.
- 23 (3) Limiting the annual filing fee for all business entities to the amount of
24 the filing fee for corporations.
- 25 (4) Revising the current franchise tax to include two components, an
26 assessment based on asset values and an assessment based on gross
27 income or receipts from business activities.
- 28 (5) The revised franchise tax would be calculated and applied on a
29 consolidated basis for members of a related or affiliated group of
30 business entities, allocated and apportioned to this State using existing
31 formulas for allocating and apportioning corporate income.
- 32 (6) The tax rates to be applied to these components would be the rates that
33 are determined to yield revenue equal to the current combined revenue
34 from corporate income and franchise taxes.
- 35 (7) The Department of Revenue would annually review the revenue
36 generated by the new simplified tax to determine if rate adjustments
37 are necessary to preserve the revenue-neutrality of the simplification.
- 38 (8) Any other issues or elements the Study Committee considers
39 appropriate.

40 **SECTION 3.** The Revenue Laws Study Committee may report its findings,
41 together with any recommended legislation, to the 2006 Regular Session of the 2005
42 General Assembly and shall make a final report, together with any recommended
43 legislation, to the 2007 General Assembly.

1 **SECTION 4.** There is appropriated from the General Fund to the
2 Department of Revenue the sum of five hundred thousand dollars (\$500,000) for the
3 2005-2006 fiscal year for the purpose of creating computer modeling capability to
4 predict the fiscal effect of various proposed changes and adjustments to the State's
5 current and future system of business taxation.

6 **SECTION 5.** This act becomes effective July 1, 2005.