



# Corporate Tax Reduction as an Alternative to Economic Development Tax Incentives

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## Scope of the Project

- Calculate the revenue neutral corporate income tax rate that would offset the income tax and franchise tax lost as a result of the Bill Lee tax credits, JDIG and One North Carolina Fund incentives
- Calculate the estimated economic impact of a reduction in the corporate tax rate
- Analyze the distribution of this economic impact and compare to the distribution of the economic impact provided by the incentives

## ● ● ● | North Carolina's Corporate Income Tax and Franchise Tax

- In 2006, corporate income tax collections totaled \$1.3 billion and franchise tax collections totaled about \$618.5 million.
- Generally accounts for less than 10% of total state tax revenue
- The income tax applies to all corporations that do business in NC that do not elect S-corp status
- The income tax is assessed at a flat rate of 6.9%

# ● ● ● | North Carolina's Corporate Income Tax and Franchise Tax

- The franchise tax applies to C-corps and S-corps and is imposed at a rate of \$1.50 per \$1,000 of taxable assets on the largest of 3 alternate asset bases:
  - Capital stock, surplus and undivided profits apportioned to NC
  - 55% of the appraised value of real and tangible property in NC subject to local taxation
  - Book value of real and tangible property in NC



## North Carolina's Corporate Income Tax and Franchise Tax

- In tax year 2004, 80,629 corporate income tax returns were filed in North Carolina
- The 199 returns with NC taxable income exceeding \$10 million paid 57.71% of the corporate income tax and the 1,532 returns with NC taxable income exceeding \$1 million paid 86.32% of the tax

## ● ● ● | North Carolina's Corporate Income Tax and Franchise Tax

- Corporations that operate exclusively within NC made up over 63% of the returns filed but paid only 16% of the total tax
- On the other hand, 45% of the corporate income tax in 2004 was attributable to 1,700 large multi-state firms with federal taxable income exceeding \$25 million that apportioned less than 25% of their income to North Carolina



## North Carolina's Corporate Income Tax and Franchise Tax

- The 6.9% corporate tax rate is the highest rate in the Southeast (our neighbor states range from 5% in SC to 6.5% in Tennessee) but about average nationwide
- Corporate income taxes per capita were \$148 and ranked 23rd highest in the country
  - Per capita burdens ranged from a low of \$59 in Missouri to a high of \$1,226 in Alaska.
- When measured as a percent of personal income, the corporate income tax ranks 21<sup>st</sup> highest in the country



# Incentives to be Examined

- Tax Incentives
  - For purposed of this research, we will focus on Bill Lee Tax Credits
  - Bill Lee credits can be taken against State income taxes, franchise taxes or gross premiums taxes
  - Credits may not exceed 50% of the tax against which they are taken
  - Unused credits may be carried forward



## Bill Lee Tax Credits

	2002- 2003	2003- 2004	2004- 2005	2005- 2006	2006- 2007
Credits Generated	\$198.4 million	\$175.5 million	\$167.9 million	\$207.2 million	\$174.5 million
Credits Taken	\$74.2 million	\$79.3 million	\$66.4 million	\$90.5 million	\$93.8 million



## Incentives to be Examined

- Other tax “incentives” described in the Economic Development Inventory such as special sales and use tax exemptions and special weighting of the corporate tax apportionment formula will not be examined



## Incentives to be Examined

- General Fund Appropriations
  - JDIG
  - One North Carolina Fund
- In 2007/08, these two programs received 81% (\$26.4 million) of the \$32.5 million appropriated to direct incentive programs



## Analysis

- Tax years examined include 2002 – 2006 for the Bill Lee and One North Carolina Fund incentives and 2003-2006 for JDIG
- If data are available, we will determine the revenue-neutral rate for each component of the economic incentives examined and the various components of the Bill Lee Act credits (job creation, investment, worker training, and research and development)



## Economic Impact of Reducing the Corporate Income Tax Rate

- Assuming that we can obtain corporate tax data by Tier or other geographic area, we will examine the distributional impact of the change