

# 1999

## North Carolina S Corporation Tax Return Instructions

### Important 1999 Legislative Changes

#### 1. Clarification of Apportionment

G.S. 105-122(c)(1) was amended to clarify that a corporation that is subject to the general business franchise tax but exempt from income tax under Article 4 of Chapter 105 must apportion its capital stock, surplus, and undivided profits base by using the apportionment factor it would have used had it been subject to the income tax. (Effective July 22, 1999)

#### 2. Reference to the Internal Revenue Code Updated.

G.S. 105-228.90 (b)(1a) was amended to update the reference to the Internal Revenue Code from September 1, 1998 to June 1, 1999, including any provisions enacted as of that date which became effective on or after that date.

#### 3. Changes to Article 3A Tax Incentives for New and Expanding Businesses

Several changes were made to the New and Expanding Business Tax Credits as enacted in the 1996 Session of the North Carolina General Assembly. G.S. 105-129.6 was amended to revise the fee structure for applications for certification of eligibility for a tax credit. Under the revised structure, the \$75.00 per application fee was deleted and was replaced with a \$500.00 per application fee that applies only to credits claimed in a Tier 3, 4, or 5 area. A maximum fee of \$1,500.00 per taxpayer per year was established. No fee applies to an application for a credit in a Tier 1 or Tier 2 area.

G.S. 105-129.7 was revised to add a new subsection (b) that sets out the information a taxpayer must provide with its return to substantiate an Article 3A credit it claims. The information is to be in a form prescribed by the Secretary of Revenue, signed by the taxpayer, and included with the return on which each installment or carryforward is claimed. The NC-478 A-F tax credit forms enclosed in this booklet reflect these changes.

#### 4. Changes to Article 3B Business and Energy Tax Credits

The name of Article 3B of Chapter 105 was changed from "Business Tax Credit" to "Business and Energy Tax Credits." This change was necessary due to the addition of a new affordable housing tax credit and the consolidation of various energy tax credits that were previously in Article 4. The changes are effective for taxable years beginning on or after January 1, 2000.

#### 5. Historic Rehabilitation Tax Credit

Chapter 105 was amended to add Article 3D, "Historic Rehabilitation Tax Credit." This new Article was enacted to place the corporation income tax and individual income tax credits for rehabilitating historic structures into one common Article. G.S. 105-130.42 in the corporation income tax laws and G.S. 105-151.23 in the individual income tax laws were repealed and recodified as part of new Article 3D. These changes are effective for taxable years beginning on or after January 1, 1999.

## General Information

### Corporations Required to File

Every S corporation doing business in North Carolina and every inactive S corporation chartered or domesticated here must file an annual tax return using the name reflected by the corporate charter, if incorporated in this State, or by the certificate of authority, if incorporated outside this State. A franchise tax is imposed on corporations for the privilege of doing business in this State even though the activities are exempt from the income tax under P.L. 86-272. For a corporation that is subject to both income tax and franchise tax, its apportionment factor is the same for both taxes. For a corporation that is subject to franchise tax but not income tax, its apportionment factor for computing the amount of franchise tax due is the same factor that would be used if its activities that are protected by P.L. 86-272 were subject to income taxes in this State.

### New S Corporations

A new S corporation (newly incorporated, newly domesticated out-of-state corporation, or other corporation commencing business in the State) is required to file within seventy-five (75) days following the close of its first income year of twelve (12) months or less a tax return with this Department. The taxable year for a new corporation in this State is presumed to end the calendar month preceding the month of incorporation unless otherwise established by the filing of the required return indicating the taxable year adopted. In no case may the first taxable year exceed twelve months unless it is clearly shown that the corporation has adopted a method of accounting using the 52-53 week reporting period. A tax return is due annually so long as the corporation remains incorporated, domesticated, or continues to do business in this State.

### Check-the-Box and QSSS Requirements

North Carolina follows the federal treatment for income tax purposes for selection of entities under the federal check-the-box regulations. Qualified Subchapter S Subsidiaries must file separate franchise tax returns (CTAM-97-13). Limited Liability Companies are not subject to the franchise tax imposed by G.S. 105-122.

### Election to be S Corporation

There is no separate S election for North Carolina income tax purposes. There is no provision to elect a different filing method for State income tax purposes.

### Termination of S Election

The S corporation election will terminate for North Carolina purposes at the same time and for the same taxable period the termination is effective for federal tax purposes.

### Tax Rates

The franchise tax rate is \$1.50 per \$1000.00 of capital stock, surplus and undivided profits or other alternative tax base. The minimum franchise tax is \$35.00 with no maximum except for qualified holding companies. The corporate income tax rate for composite filers is based on current individual income tax rates.

### Time and Place for Filing

The S corporation tax return is due on the 15th day of the third month following the close of the income year. **Returns should be filed with the North Carolina Department of Revenue, P.O. Box 25000, Raleigh, NC, 27640-0530 or at one of the Department's local branch offices.**

### Extension of Filing Date

An extension of time to file the tax return may be granted for seven (7) months if the extension application is received timely. Without a valid extension, a return filed after the statutory due date will be delinquent and subject to all applicable penalties provided by law. Taxpayers filing an application for extension, Form CD-419, must report the full amount of tax paid with the extension on Schedule F, Line 16a. **Note: A properly filed federal extension does not constitute a North Carolina extension.**

### Estimated Income Tax

Estimated income tax payments are not required on behalf of nonresident shareholders filing a composite tax return; however, if the S corporation makes any prepayments of income tax, the S corporation must claim these prepayments on Schedule F, Line 16b.

### Amended Returns

The Department no longer uses Amended North Carolina Form CD-444 or CD-444A. If filing an amended return for taxable years beginning on or after January 1, 1999 use Form CD-401S and fill in the appropriate circle.

### Suspended Corporation Reinstatement Fee

A S corporation that has its articles of incorporation or certificate of authority suspended for failure to comply with this State's revenue laws is required to file all delinquent returns and remit the tax, penalty, and interest due plus pay a fee of \$25.00 for reinstatement of its corporate rights.

## Line Instructions for Filing Form CD-401S

### Schedule A - Computation Of Franchise Tax

#### Lines 1 through 5 - Tax Bases

The S corporation law for income tax purposes does not affect the franchise tax liability of corporations doing business in this State. Franchise tax is computed by applying the tax rate of \$1.50 per \$1,000.00 to the largest of the following three bases:

- (1) Capital stock, surplus, and undivided profits (Schedule C)
- (2) Actual investment in tangible property in N.C. (Schedule D)
- (3) Fifty-five percent of appraised ad valorem tax value of all tangible property in N.C. (Schedule E)

**The minimum franchise tax is thirty-five dollars, (\$35.00). Follow the specific instructions for each schedule to determine the amount of each tax base.**

**Inactive Corporations.** A S corporation that is inactive and without assets is subject annually to a minimum franchise tax of \$35. A return is required containing a statement of the status of the corporation. Failure to file this return and pay the minimum tax will result in suspension of the articles of incorporation or certificate of authority. Any corporation that intends to dissolve or withdraw through suspension for nonpayment of franchise tax should indicate its intention in writing to the Department.

**Dissolution or Withdrawal of Corporate Rights.** Since franchise taxes are paid in advance or at the beginning of the income year, corporations are not subject to franchise tax after the end of the income year in which articles of dissolution or withdrawal are filed with the Secretary of State unless they engage in business activities not reasonably incidental to winding up their affairs. This applies, however, only to those corporations officially filing articles of dissolution or withdrawal with the Secretary of State of North Carolina.

## Line 6 - Tax Credits

The following is a list of the more utilized franchise tax credits:

- Machinery & Equipment Investment Tax Credit
- Job Creation Tax Credit
- Research and Development Tax Credit
- Worker Training Tax Credit
- Central Administrative Office Property Tax Credit
- Business Property Tax Credit

To claim a franchise tax credit on Line 6, S corporations must complete Form CD-425, Corporate Tax Credit Summary, and staple it to the completed tax return. Taxpayers claiming a credit limited by statute to 50% of tax must also complete Form NC-478, Summary of Tax Credits Limited to 50% of Tax. Computational worksheets for many of these credits, as well as the CD-425 and NC-478, are enclosed in this booklet.

**Application for Franchise Tax Extension.** A timely filed application for extension not only extends the time to file a corporate income tax return, but also extends the time to file the franchise tax return. Prior returns included a line for corporations to claim a franchise tax payment made with the application for extension. The 1999 Application for Extension has been revised and requires the corporation to total its estimated franchise and corporate income tax due and remit one payment. When filing the tax return, taxpayers filing an application for extension must claim the full amount of the tax paid with the extension on Schedule F, Line 16a. Any overpaid income tax can offset an underpaid franchise tax liability in the same tax year. (See Schedule B, Lines 9 and 10)

**Change of Income Year.** A change of income year automatically establishes a new franchise year. Credit is allowed against the franchise tax on the short-period return to the extent that the new franchise year overlaps the old franchise year. In order to claim this credit, Form CD-425, Corporate Tax Credit Summary, must be attached to the completed tax return.

**Mergers.** Since franchise tax is prepaid, a special computation is sometimes required to prevent a duplication of tax when two or more corporations with different income years merge or otherwise transfer the entire assets from one corporation to the other. For specific information and the procedure for making this computation, refer to the Franchise Tax and Corporate Income Tax Rules and Bulletins.

## Schedule B - Tax Due or Refund

A S corporation that overpays its franchise or income tax may elect to have its refund applied to an underpaid tax liability in the same tax year. The netting of an overpaid tax to an underpaid liability is calculated by adding or subtracting Lines 9(a), 9(b), 10(a), and 10(b).

## Line 11 - Balance of Tax Due

If Line 9(a) plus Line 10(a) is larger than the total of Lines 9(b) and 10(b), additional tax is due. Enter the amount of additional tax due on Line 11.

## Line 12 - Interest

Interest at the rate established by G.S. 105-241.1 is due and payable with all payments of tax not remitted by the due date established by statute. The rate is established semiannually by the Secretary and is listed on the Department's website.

## Line 13 - Penalties

A tax return filed after the statutory due date or after the approved extended due date will incur a penalty for failure to file of five percent (5%) for each month or fraction of a month delinquent, with a maximum penalty of twenty-five percent (25%) of the tax and a minimum of five dollars (\$5.00). Additionally, a penalty of ten percent (10%) will be assessed for failure to timely pay any tax shown due with a return and on other remittances not made within thirty days.

## Line 14 - Payment of Taxes

Include a check or money order made payable to the North Carolina Department of Revenue in U.S. currency only for the full amount of any balance due. Any income tax payment made on behalf of shareholders included in the composite return is due and payable at the time the return is due to be filed. Interest and a 10% late payment penalty must be calculated on any tax paid after the original due date.

## Line 15 - Overpayment

If the total of Lines 9(b) and 10(b) is greater than Line 9(a) plus 10(a), the corporation has overpaid its tax. Enter the amount of overpayment on Line 15.

## Line 16 - Estimated Income Tax

A corporation may elect to apply part or all of the overpayment shown on Line 15 to its estimated tax for the following year by entering the amount to be applied on Line 16. This election cannot be changed after the return is filed.

## Line 17 - Amount to be Refunded

Corporations enter the amount of overpayment to be refunded on Line 17.

## Schedule C - Capital Stock, Surplus, and Undivided Profits

In addition to the items listed on the schedule, include stock subscribed, deferred taxes, and all other surplus, reserves, deferred credits, and inventory valuation reserves, including amounts deferred as result of a LIFO valuation method (LIFO reserves), and liabilities except: (a) reserve for depreciation permitted for income tax purposes; (b) accrued taxes; (c) dividends declared; (d) definite and accrued legal liabilities (accounts, notes, mortgages payable, etc.). Deferred income resulting from customer advances for goods or services may be excluded from this base provided: (1) there exists a definite legal liability to render the service or deliver the goods; (2) no part of the advances has been reported or is reportable for income tax purposes; and (3) all related costs and expenses are reflected in the balance sheet as assets. Deferred income net of related deferred income taxes arising from the usual installment sale is not deductible because the corresponding liability would have been discharged at the time of delivery.

Indebtedness owed to a parent, subsidiary, or affiliated corporation is considered a part of the debtor corporation's capital and must be added to the debtor corporation's capital stock, surplus, and undivided profits. If the creditor corporation has borrowed a part of its capital from outside sources (i.e., sources other than a parent, subsidiary, or affiliated corporation), the debtor corporation may exclude a proportionate part of the debt determined on the basis of the ratio of the creditor corporation's capital borrowed from outside sources to the creditor corporation's total assets.

The creditor corporation, if subject to the tax, can deduct from its capital stock, surplus, and undivided profits the amount of indebtedness owed to it by a parent, subsidiary, or affiliated corporation to the extent that the indebtedness has been added by the debtor corporation on a return filed with this State. **The exclusion permitted the debtor corporation and the deduction permitted the creditor corporation are applicable only to indebtedness owed to or due from a parent, subsidiary, or affiliated corporation.**

The term "indebtedness" includes all loans, credits, goods, supplies, or other capital of whatsoever nature furnished by a parent, subsidiary, or affiliated corporation. The terms "parent," "subsidiary," and "affiliate" have the meanings specified in G.S. 105-130.6. The capital stock base may be reduced by the excess of assets of an international banking facility employed outside the United States over liabilities of the corporation owed to foreign persons.

**Cash Basis Corporations.** S corporations using the cash basis method of accounting for income tax purposes cannot compute the capital stock, surplus, and undivided profits base by this method. Assets and liabilities must be accrued and reported for franchise tax purposes.

## Schedule D - Investment in Tangible Property in N.C.

Include all tangible assets located in North Carolina at book value (original purchase price less reserve for depreciation permitted for income tax purposes). In addition to the types of property listed in the schedule, include all other tangible property owned such as supplies and tools. **LIFO valuation is not permitted for inventories.**

A deduction from the tangible property base is allowed for indebtedness incurred and existing by virtue of the purchase or permanent improvement of real estate located in North Carolina. The deductible amount cannot exceed the book value (cost less depreciation) of the real estate acquired or improvements made. Debts incurred in the purchase of personal property are not deductible even though the funds borrowed are secured by a lien against real estate. Indebtedness owed to a parent, subsidiary, or affiliated corporation constitutes a part of the debtor corporation's capital and, therefore, cannot be deducted from the tangible property tax base (except to the extent explained below) even though the indebtedness was incurred in the purchase or permanent improvement of real estate. The extent to which the indebtedness can be deducted is the amount of the total debt excluded by the debtor corporation from its capital stock, surplus, and undivided profits base by application of the creditor corporation's borrowed capital ratio.

## Air or Water Pollution Abatement and Recycling Resource Recovering Facilities

A corporation may deduct from Schedule C and Schedule D the cost of any air cleaning device or sewage or waste treatment plant and pollution abatement equipment described in G. S. 105-122(b). **A deduction is allowed only upon certification from the Department of Environment and Natural Resources.**

## Schedule E - Appraised Valuation of Property in N.C.

Enter 55% of the appraised value, not book value, of all property listed for county ad valorem tax in North Carolina. This value includes the appraised value of all vehicles for which the county tax assessor has issued a billing during the income tax year. **Values are to be determined as of the dates specified on Schedule D of the return.**

## Schedule F - Computation of Income Tax

### Lines 1 through 9 - N.C. Taxable Income

To compute N.C. taxable income, **all taxpayers** must enter the amount of State net income subject to tax from Schedule I, Line 6 on Line 1. If the amounts on Lines 1 - 3, 5-7, 9, or 10 calculate to be less than zero, enter the number in the appropriate box and fill in the circle completely. **Do not use brackets or other symbols to indicate a negative number.**

The apportionment factor requested on Line 4 is calculated on Schedule J.

### Line 10 through 13 - Composite Tax Returns

Lines 10-13 are to be completed only by an S corporation filing a composite income tax return on behalf of its nonresident shareholders. A composite return is an income tax return that combines and reports the income and tax due of participating nonresident shareholders. A nonresident individual shareholder is not required to file a N.C. Individual Income Tax Return, Form D-400, if the only income in N.C. is reported by the S corporation. If the nonresident shareholder is a trust or another S corporation, the entity must file a separate N.C. tax return.

To determine tax due for nonresidents filing composite, use the Tax Rate Schedule found in these instructions, and on page 10 of the CD-401S return. N.C. income tax must be separately computed for each nonresident shareholder filing composite. The S corporation must total the separate income tax for each participating nonresident shareholder and enter the total on Line 11.

### Line 12 - Tax Credits

The following are some of the more utilized income credits for corporations:

- Machinery & Equipment Investment Tax Credit
- Job Creation Tax Credit
- Research and Development Tax Credit
- Worker Training Tax Credit
- Central Administrative Office Property Tax Credit
- Business Property Tax Credit
- Credit for the construction of poultry composting facilities
- Credit for the Rehabilitation of Historic Structures
- Credit for use of North Carolina Ports

In order for nonresidents filing composite to claim income tax credits, the S corporation must complete Form CD-425, Corporate Tax Credit Summary, and staple it to the completed tax return. The S corporation must include only the amount of income tax credits allocated to nonresident shareholders on whose behalf a composite return is filed. In order for composite filers to claim an income tax credit limited by statute to 50% of tax, the S corporation must also complete Form NC-478, Summary of Tax Credits Limited to 50% of Tax. Computational worksheets for many of these credits, as well as the CD-425 and the NC-478, are enclosed in this booklet.

### Line 14 - Annual Report Fee

All domestic corporations and foreign corporations authorized to transact business in North Carolina except for insurance companies, limited liability companies, nonprofit corporations, professional corporations, and professional associations must, on an annual basis, complete Form CD-479 and remit a twenty dollar (\$20.00) fee. The annual report, Form CD-479, must be completed in its entirety and attached **to the front page** of the completed tax return. Failure to submit the Annual Report with the tax return may result in an administrative dissolution of the Corporate Articles or Certificate of Authority by the Secretary of State's Office as prescribed by statute. For instructions on how to complete the Annual Report, see the Check List for Business Corporations Annual Report located on the reverse side of that form.

### Line 16 - Tax Payments

- a. **Application for Extension.** Taxpayers filing a Form CD-419 enter the full amount of tax paid with the extension on Line 16a.
- b. **1999 Estimated Tax.** Enter any estimated income tax payments for 1999 (including any portion of the 1998 overpayment that was applied to the 1999 estimated income tax).
- c. **Partnerships** - If the S corporation is a nonresident partner enter the amount of tax paid to North Carolina on behalf of the corporate partner.
- d. **Nonresident Withholding** - Enter the amount of tax withheld from a nonresident S corporation during the taxable year.

## Schedule G- Ordinary Income (Loss)

The computation of net income from trade or business activities follows the determination of ordinary income as defined by the Internal Revenue Code effective June 1, 1999. S corporations must transfer the information from federal Form 1120S, U.S. Income Tax Return for an S Corporation (Lines 1 through 21), to Schedule G, or attach a copy of the federal form along with all supporting schedules.

**Attach a copy of federal Form 1120S along with all supporting schedules only if the N.C. return is not completed in its entirety.**

## Schedule H - Computation of Income (Loss)

### Line 1 - Ordinary Income (Loss)

Enter the ordinary income from trade or business activities as taken from federal Form 1120S, Line 21 or from N.C. Schedule G, Line 21.

### Lines 2 through 6 - Total Adjustments of Ordinary Income

Add income or deduct losses on Lines 2 through 6 that are directly passed to the shareholders as shown on federal Schedule K, Lines 2 through 6.

### Line 7 - Total Income (Loss)

Add Lines 1 through 6 and enter total on Schedule H, Line 7 and on Schedule I, Line 1.

## Schedule I - Adjustment to Income (Loss)

Guidelines for adjustments required as a result of the differences existing between federal and State income tax are set forth in G.S. 105-130.5. Schedule I provides some of the differences but is not an all inclusive list. N.C. Form CD-415, Instructions for Filing C Corporation Tax Returns, list all the provisions of G.S. 105-130.5. **In situations where differences exist between corporate income tax law and individual income tax law relative to the tax liability of any taxpayer, the requirements of the levying statute, i.e. individual income tax, will normally prevail over the law requiring informational reporting.**

**Line 1** - Enter on Line 1 the total income or loss from federal Form Schedule K, Lines 1-6, or from N.C. Schedule H, Line 7.

**Line 2** - The following additions to federal taxable income are required in calculating North Carolina State Income Subject to Tax to the extent the additions are not included in federal taxable income but are reportable for corporate income tax purposes under State law. These additions should be entered on Line 2 and allocated to individual shareholders on Schedule K, Line 6.

Additions to federal taxable income include:

- (1) Any state, local, or foreign income tax deducted on the federal return,
- (2) Interest on bonds and other obligations of states and political subdivisions other than North Carolina, if not included in federal taxable income,
- (3) Any capital loss carry-over or percentage depletion in excess of cost depletion

**Line 4** - The following items must be deducted from federal taxable income in calculating North Carolina Income Subject to Tax to the extent the deductions are included in federal taxable income. These total deductions should be entered on Line 4 and allocated to individual shareholders on Schedule K, Line 7.

Deductions from federal taxable income include:

- (1) Interest from obligations of the United States or its possessions,
- (2) Deductible dividends
- (3) Any capital loss not deducted on the federal return

**Note: Deductions which are subject to personal limitations such as IRC Section 179, charitable contributions, and net economic losses are no longer deductible in the calculation of North Carolina Income Subject to Tax. Taxpayers wishing to deduct its pro rata share of these items must do so on its own income tax return.**

## Schedule J - Computation of Apportionment Factor

### Part 1 - Domestic Corporations

Domestic S corporations and other S corporations not apportioning franchise or income outside of N.C. must enter 100% in the area provided. **Domestic corporations** are those corporations created or organized under the statutory laws of N.C. Foreign S corporations doing business in N.C. but not taxable in another state must also enter 100% for its apportionment factor.

**Part 2 - Multistate Corporations**

S corporations with business income attributable to sources both within and outside of N.C. are required to apportion its business income. The S corporation law requires that the provisions of the corporate income tax law, G.S. 105-130.4, be followed in computing the amount of income, adjustments, and credits attributable to N.C.

To determine the apportionment factor, complete Part 2 of this schedule. These factors express a percent for tangible property in N.C., for wages and salaries in N.C., and for sales in N.C. These factors are to be added together and divided by the number of factors present (typically 4) to arrive at the N.C. apportionment factor calculated to **four decimals**.

**Lines 1 through 8 - Property Factor**

The property factor is a fraction, the numerator of which is the average value of the corporation's real and tangible personal property owned or rented and used in this State during the income year and the denominator of which is the average value of all the corporation's real and tangible personal property owned or rented and used during the income year. The numerator includes not only inventories actually located in North Carolina but also inventories in transit with a North Carolina destination.

Property owned by the corporation is valued at its original cost. Property rented by the corporation is valued at eight times the net rent paid during the current income year. Net annual rent is the annual rent paid by the corporation less any annual rent received by the corporation from subrentals except that subrentals are not deductible when they constitute business income. Any property under construction or any property not actually used or operated in the corporation's business during the income year and any property the income from which constitutes nonbusiness income are excluded in the computation of the property factor.

The average value of property is determined by averaging the values at the beginning and end of the income year, but in all cases the Secretary may require the averaging of monthly or other periodic values during the income year if required to reflect properly the average value of the corporation's property. A corporation that ceases its operation in this State before the end of its income year for any reason whatsoever must use property values as of the first day of the income year and the last day of its operations in this State in determining the average value of property; however, the Secretary may require the averaging of monthly or other periodic values during the income year.

**Lines 9 through 11 - Payroll Factor**

The payroll factor is a fraction, the numerator of which is the total compensation paid in this State during the income year by the corporation and the denominator of which is the total compensation paid everywhere during the income year. All compensation paid to general executive officers and all compensation paid in connection with nonbusiness income shall be excluded in computing the payroll factor. General executive officers include the chairman of the board, president, vice-presidents, secretary, treasurer, comptroller, and any other officer serving in similar capacities.

Compensation is paid in this State if any of the following applies:

- (1) The individual's service is performed entirely within the State; or
- (2) The individual's service is performed both within and without the State, but the service performed without the State is incidental to the individual's service within the State.
- (3) Some of the service is performed in this State and the base of operations, or, if there is no base of operations, the place from which the service is directed or controlled, is in this State.
- (4) Some of the service is performed in this State and the base of operations or the place from which the service is directed or controlled is not in any state in which some part of the service is performed, but the individual's residence is in this State.

**Part 2, Lines 12 and 13 - Sales Factor**

The sales factor is a fraction, the numerator of which is the total sales of the corporation in this State during the income year, and the denominator of which is the total sales of the corporation everywhere during the income year. The receipts from any casual sale of property are excluded from both the numerator and the denominator of the sales factor. If a corporation is not taxable in another state on its business income but is taxable in another state only because of nonbusiness income, all sales are treated as having been made in this State.

Sales of tangible personal property are in this State if the property is received in this State by the purchaser. In the case of delivery of goods by common carrier or by other means of transportation, including transportation by the purchaser, the place at which the goods are ultimately received after all transportation has been completed is considered the place at which the goods are received by the purchaser. Direct delivery into this State by the taxpayer to a person or firm designated by a purchaser from within or without the State constitutes delivery to the purchaser in this State.

Other sales are in this State if any of the following applies:

- (1) The receipts are from real or tangible personal property located in this State.
- (2) The receipts are from intangible property and are received from sources within this State.
- (3) The receipts are from services and the income-producing activities are in this State.

**Part 3 - Excluded Corporations and Public Utilities**

**Contractors.** A multistate building or construction contractor must use a one factor sales (gross receipts) formula to apportion its business income to this State. A building or construction contractor is a business so classified under the North American Industry Classification System.

Special apportionment provisions apply to the business income of public utility corporations and excluded corporations. The respective tax statutes should be consulted for specific allocation requirements.

**Air and Water Transportation.** All business income of an air or water transportation company is apportioned by the ratio of revenue-ton miles in North Carolina to total revenue-ton miles. A revenue-ton mile is one ton of passenger, freight, mail, or other cargo carried one mile; each passenger is deemed to weigh 200 pounds.

**Part 4 - Telephone Companies and Motor Carriers**

**Motor Carriers.** All business income of a motor carrier of property or passengers must be apportioned by multiplying the income by a fraction, the numerator of which is the number of vehicle miles in this State and the denominator of which is the total number of vehicle miles of the company everywhere. The words "vehicle miles" mean miles traveled by vehicles owned or operated by the company hauling property for a charge, carrying passengers for a fare, or traveling on a scheduled route.

**Telephone Companies.** All business income of a telephone company must be apportioned by multiplying the income by a fraction, the numerator of which is gross operating revenues earned in this State plus other revenue items attributed to this State specifically listed in G.S. 105-130.4(n) and the denominator of which is the total gross operating revenue from all business done by the company everywhere less uncollectible revenue.

Motor carriers and telephone companies complete the following worksheet and enter the factor computed on Schedule J, Part 4.

<b>Computation of Apportionment Factor for Certain Public Service Corporations</b>	
<b>A. Vehicle Miles Factor - for corporations whose business is the operation of a motor carrier of property or passengers</b>	
1. Number of vehicle miles traveled in N.C. ....	_____
2. Total number of vehicle miles traveled everywhere .....	_____
3. <b>Percentage of Mileage to N.C. Factor</b> (Divide Line 1 by Line 2; enter amount here and on Schedule J, Part 4) .....	_____ %
<b>B. Gross Operating Revenue Factor - for corporations whose income is derived from the operation of a telephone company</b>	
<b>1. Gross Operating Revenues in North Carolina</b>	
a. Gross operating revenue from local service in N.C. ....	_____
b. Gross operating revenue from toll services within N.C. ...	_____
c. N.C. portion of revenue from interstate toll services .....	_____
d. Gross operating revenues in N.C. from other services ..	_____
e. Total gross operating revenues assignable to N.C. (Add Lines 1a through 1d) .....	_____
f. N.C. uncollectible revenue .....	( _____ )
g. Total adjusted gross operating revenues assignable to N.C. (Line 1e minus Line 1f) .....	_____
<b>2. Gross Operating Revenues Everywhere</b>	
a. Total gross operating revenues .....	_____
b. Total uncollectible revenue .....	_____
c. Total adjusted gross revenues everywhere (Line 2a minus 2b) .....	( _____ )
<b>3. Gross Operating Revenue Factor</b>	
(Divide Line 1g by Line 2c; enter amount here and on Schedule J, Part 4) .....	
	_____ %

**Schedule K - Shareholders' Share of Income, Adjustments, and Credits**

This schedule is provided primarily as a worksheet to the S corporation to summarize all the shareholders' shares of income, N.C. adjustments, and N.C. tax credits, and to show the amount of these items that are apportioned or allocated to nonresident shareholders. The name, address, and percentage of ownership of each shareholder must be listed on Schedule K. A North Carolina resident is required to report its full share of corporate income or loss. A nonresident shareholder, however, is only required to report to N.C. its share of apportioned and allocated income or loss.

The S corporation must give each shareholder a copy of form NC K-1. The NC K-1 is the form used to report each shareholder's share of these items. The cumulative total of a given line on all of the shareholder's NC K-1s must equal the amount that the corporation reports in the Shareholders' Total column of Schedule K. Nonresident shareholders filing a composite income tax return must be provided with its share of net tax paid on its behalf by the S corporation. (For more information on NC K-1, see the specific instructions for this form.)

## Schedule L - Balance Sheet

## Schedule M-1 - Federal Schedule M-1

Complete schedules only if you do not attach a copy of the federal 1120S along with all supporting schedules.

## Schedule M-2 - Analysis of N.C. Accumulated Adjustments Account

All corporations must maintain the "accumulated adjustments account" (AAA) for federal and state purposes. The computation of the N.C. accumulated adjustments account and N.C. adjustments account is made using the same procedures as the federal computation applying the North Carolina amounts. See instructions for federal Form 1120S and IRC §1368.

## Schedule N - Nonbusiness Income

Rents and royalties from real or tangible personal property, gains and losses, interest, dividends, patent and copyright royalties, and other kinds of income, if these income items are nonbusiness income, less related expenses are required to be allocated. (A detailed explanation of nonbusiness income is contained in Corporation Income Tax Rules and Bulletins. Copies are available upon request.)

**Rents and Royalties from Real and Tangible Property.** Net rents and royalties from real property located in this State are allocable to this State. Net rents and royalties from tangible personal property are allocable to this State:

- (1) if and to the extent that the property is utilized in this State, or
- (2) in their entirety if the corporation's commercial domicile is in this State and the corporation is not organized under the laws of, or is not taxable in, the state in which the property is utilized.

The extent of utilization of tangible personal property in a state is determined by multiplying the rents and royalties by a fraction, the numerator of which is the number of days of physical location of the property in the state during the rental or royalty period in the income year and the denominator of which is the number of days of physical location of the property everywhere during all rental or royalty periods in the income year. If the physical location of the property during the rental or royalty period is unknown or unascertainable by the corporation, tangible personal property is utilized in the state in which the property was located at the time the rental or royalty payer obtained possession.

**Gains or Losses on Disposition of Property.** Gains and losses from sales or other disposition of real property located in this State are allocable to this State. Gains and losses from sales or other disposition of tangible personal property are allocable to this State if:

- (1) the property had a situs in this State at the time of the sale, or
- (2) the corporation's commercial domicile is in this State and the corporation is not taxable in the state in which the property had a situs.

Gains and losses from sales or other disposition of intangible personal property are allocable to this State if the corporation's commercial domicile is in this State.

**Interest and Dividend Income.** Interest income and dividend income, net of any dividends deducted in computing State net income or loss pursuant to G.S. 105-130.7, are allocable to this State if the corporation's commercial domicile is in this State.

**Royalties and Similar Income from Intangible Property.** Royalties or similar income received from the use of patents, copyrights, secret processes, and other similar intangible property are allocable to this State:

- (1) if and to the extent that the patent, copyright, secret process, or other similar intangible property is utilized in this State, or
- (2) if and to the extent that the patent, copyright, secret process, or other similar intangible property is utilized in a state in which the taxpayer is not taxable and the taxpayer's commercial domicile is in this State.

A patent, secret process, or other similar intangible property is utilized in a state to the extent that it is employed in production, fabrication, manufacturing, processing, or other use in the state or to the extent that a patented product is produced in the state. If the basis of receipts from such intangible property does not permit allocation to states or if the accounting procedures do not reflect states of utilization, the intangible property is utilized in the state in which the taxpayer's commercial domicile is located.

A copyright is utilized in a state to the extent that printing or other publication originates in the state. If the basis of receipts from copyright royalties does not permit allocation to states or if the accounting procedures do not reflect states of utilization, the copyright is utilized in the state in which the taxpayer's commercial domicile is located.

**Other Nonbusiness Income.** The income less related expenses from any other nonbusiness activities or investments is allocable to this State if the business situs of the activities or investments is located in this State.

## General Corporate Information

MUST BE COMPLETED BY ALL TAXPAYERS

## Line 6- Escheat Law (Abandoned and Unclaimed Property)

Every corporation holding property of North Carolina residents that is unclaimed and abandoned under General Statutes Chapter 116B must certify the holding on its income tax return by filling in the appropriate circle. Information requests as to required reports, types of property, etc. should be directed to: **Escheat Officer, Department of State Treasurer, Albemarle Building, 325 N. Salisbury Street, Raleigh, North Carolina 27611.**

## Tax Rate Schedule

An S corporation that fails to timely file NC-NA agreement(s) for its nonresident shareholders will become liable for income tax at the current individual income tax rates on the portion of N.C. income attributed to those shareholders not complying with the filing requirement. Nonresident shareholders filing composite must also separately compute its state taxable income and pay any income tax due based on the current individual income tax rates.

1999 individual income tax rates for each shareholder is 6% of the first \$12,750; 7% of the amount over \$12,750 but less than \$60,000; and 7.75% of the amount over \$60,000.

## Signature and Verification

An authorized officer must sign and date the completed tax form and enter his or her corporate title. If a paid preparer is used, the preparer must also sign and date the return and enter the firm's federal employer ID number, social security number, or PTIN as assigned by the IRS.

## Specific Instructions for Schedule NC K-1, Shareholder's Share of North Carolina Income, Adjustments, and Credits

Schedule NC K-1 is the form used by the S corporation to report to each shareholder its share of the S corporation's income, adjustments, tax credits, etc. Prepare and give a Schedule NC K-1 to each entity that was a shareholder in the S corporation at any time during the year. Schedule NC K-1 must be provided to each shareholder on or before the due date of the S corporation tax return.

Shareholders that are **residents of N.C.** must be provided with the total amount of their proportionate share of the following items (Lines 1 - 5):

1. N.C. adjustments to federal taxable income, NC K-1, Lines 2 and 3.
2. Shareholder's distributive share of tax credits, NC K-1, Line 4. When reporting the distributive share of tax credits, a list of the amount and type of each tax credit must be provided to the shareholder.
3. Any tax withheld from nonwage compensation for personal services in N.C. by the S corporation, NC K-1, Line 5.

Shareholders that are **nonresidents of N.C.** must be provided with their share of the same items listed above for N.C. residents, along with the following items (Lines 6 and 7):

1. N.C. net income apportioned and allocated for business activities occurring outside of N.C., NC K-1, Line 6.
2. Any N.C. income tax paid by the S corporation on behalf of the nonresident shareholder, NC K-1, Line 7.

## Specific Instructions for Schedule NC-NA, Nonresident Shareholder Agreement Form

S corporations with nonresident shareholders are required to submit with the first North Carolina S corporation return an agreement from each nonresident shareholder. In the agreement, Schedule NC-NA, the nonresident agrees to be subject to the individual income tax laws of this State and to be liable for the tax on its pro rata share of S corporation income attributable to such individual in this State. A separate agreement is required for each nonresident including a separate agreement for each owner if the stock is jointly owned. A schedule NC-NA is available from the Department or on the Department's website.

## Instructions for Form NC-478 Series

**Purpose of Form NC-478 Series.** Use the Form NC-478 series to calculate and report tax credits that are limited to 50% of tax less the sum of all other tax credits claimed. Forms NC-478A through NC-478F are used to calculate the specific credits without regard to the 50% limitation. Form NC-478 is used to total the specific credits, to determine if the 50% limitation applies, and if so, to allocate the limited total credit among the specific credits.

### **General Instructions for NC-478 Series**

Listed below are the tax credits that are subject to the 50% of tax limitation and the NC-478 series form on which the credit is claimed:

- Creating Jobs (Form NC-478A)
- Investing in Machinery and Equipment (Form NC-478B)
- Research and Development (Form NC-478C)
- Worker Training (Form NC-478D)
- Investing in Central Administrative Office Property (Form NC-478E)
- Investing in Business Property (Form NC-478F)
- Use of North Carolina Ports (Form NC-478, Line 7)
- Manufacturing Cigarettes for Export (Form NC-478, Line 7)

Each of the above tax credits are available to individuals, partnerships, estates, trusts, and corporations except the tax credit for manufacturing cigarettes for export, which is available only to corporations. Insurance companies may claim the credits for research and development, worker training, and the investing in central administrative office property against their gross premiums tax in 1999.

These forms are to be used by each individual, partnership, corporation (domestic or foreign), estate, trust, and insurance company that claims a tax credit that is subject to the 50% of tax limitation. Form NC-478 and the applicable form for the specific credit must be stapled to the front page of your tax return if you are eligible to claim a tax credit, regardless of whether your tax liability is great enough to claim a tax credit in the current period. Corporations staple these forms behind CD-479, Annual Report Form. Certification received from the Secretary of Commerce must also be attached if you are claiming the credit for creating jobs, investing in machinery and equipment, research and development, worker training, or investing in central administrative office property. Failure to attach these forms to your tax return may result in the disallowance of these tax credits.

**Pass-through entities.** A pass-through entity must provide sufficient information about the tax credits to its owners or beneficiaries to allow the owner or beneficiary to complete the Form NC-478 series. The information must be provided on, or as an attachment to, the NC K-1 provided to the owner or beneficiary.

### **Specific Instructions for NC-478 Letter Series**

#### **NC-478 – Summary of Tax Credits Subject to 50% Limit**

**Part 1.** After completing the applicable Forms NC-478A through NC-478F, enter the totals from those forms on the appropriate lines in Part 1 of Form NC-478. If you are claiming the credit for use of North Carolina ports or the credit for manufacturing cigarettes for export, complete and attach a separate schedule to show the calculation of that credit and enter the name and amount of the credit on Line 7. Add Lines 1 through 7 and enter the total on Line 8. This is the total amount of tax credits subject to the 50% of tax limitation. Individuals, partnerships, trusts, and estates enter the credits only in the Income column because those taxpayers do not owe franchise tax. Corporations may elect for each credit, other than the credit for use of North Carolina ports or the credit for manufacturing cigarettes for export, whether to claim the credit against franchise or income tax. The credit for use of North Carolina ports and the credit for manufacturing cigarettes for export can only be claimed against income tax. The election is made at the time the first installment of a credit is claimed and is binding for all future installments of that credit. Insurance companies may claim the credits against their gross premiums tax by completing the Franchise column. S corporations enter the total amount of credit if the credit is being applied against franchise tax; however, if the credit is being applied against income tax, enter only the portion of each credit that is allocable to nonresident shareholders on whose behalf a composite return is filed.

**Part 2.** Complete Part 2 to determine if the total credits reported in Part 1 must be reduced because the total credits exceed 50% of tax less other credits.

**Line 9 -** C corporations enter the amount of franchise tax due from Form CD-405, Schedule A, Line 5, in the Franchise column, and the amount of income tax due from Form CD-405, Schedule F, Line 13, in the Income column. S corporations enter the amount of franchise tax due from Form CD-401S, Schedule A, Line 5, in the Franchise column, and the amount of income tax due for nonresident shareholders filing composite from Form CD-401S, Schedule F, Line 13, in the Income column.

**Line 10 -** Corporations enter the total amount of tax credits not subject to the 50% of tax limit from Form CD-425, Line 6, in the Franchise or Income column, whichever is elected. S corporations enter the total amount of franchise tax credits not subject to the 50% of tax limit from Form CD-425, Line 6, in the Franchise column; however, enter only the amount of income tax credits not subject to the 50% of tax limit allocated to nonresidents on whose behalf a composite return is filed in the Income column.

**Line 13 -** Enter the lesser of Line 8 or Line 12. If Line 8 exceeds Line 12, complete Part 3; otherwise, enter the amount of Line 13 on Line 21.

**Part 3.** If Line 8 exceeds Line 12, your total tax credits in Part 1 exceeded 50% of your tax less other credits and must be reduced to the amount on Line 13. You may choose to allocate the allowable amount of credit (Line 13) among the credits for which you are eligible (Lines 1 through 7) by completing Lines 14 through 20. If the amount of eligible credit in Part 1 exceeds the amount of allocated credit in Part 3, you may be eligible to carry forward the excess amount and claim it next year.

**Line 21 -** Add lines 14 through 20 and enter the total. This amount must equal the amount on Part 2, Line 13. Corporations enter the total amount of tax credits from the Franchise and Income columns on Form CD-425, Part 3, Line 7.

**Part 4.** If you claimed a tax credit for investing in business property on Line 6, enter the cost of business property placed in service during the current year for which the credit is allowed. Enter that amount even if you were required to allocate credits in Part 3 and elected to enter \$0 on Line 19. S corporations enter the total cost of business property if the credit is being applied against franchise tax. If the credit is applied against income tax, S corporations enter only the portion of the cost of business property that is allocable to its nonresident shareholders on whose behalf a composite return is filed.

#### **NC-478A – Tax Credit for Creating New Jobs**

Corporations claiming this credit against franchise tax, complete NC-478A and enter the amount from Part 4, Line 6 on Form NC-478, Line 1. S corporations claiming the credit against income tax, complete Parts 1 and 2 as one taxpayer, then allocate the amount from Part 1, Line 7 among the shareholders. Complete Parts 3 and 4 by including only the amounts allocated to nonresident shareholders on whose behalf a composite return is being filed. On Part 4, Line 5, include only the amount of carryforward for nonresident shareholders on whose behalf a composite return is filed in both the prior year and the current year.

#### **NC-478B – Tax Credit for Investing in Machinery and Equipment**

Corporations claiming this credit against franchise tax, complete NC-478B and enter the amount from Part 3, Line 5 on Form NC-478, Line 2. If M & E was placed in service over a two-year period, reduce the amount on Part 1, Line 6, by the amount entered on Line 9 of the 1998 Form CD-478B. S corporations claiming the credit against income tax, complete Parts 1 and 4 as one taxpayer, then allocate the amount from Part 1, Line 9 among the shareholders. Complete Parts 2 and 3 by including only the amounts allocated to those nonresident shareholders on whose behalf a composite return is being filed. On Part 3, Line 4, include only the amount of carryforward for nonresident shareholders on whose behalf a composite return is filed in both the prior year and the current year.

#### **NC-478C – Tax Credit for Research and Development**

Corporations claiming this credit against franchise tax, complete NC-478C and enter the amount from Part 3, Line 4 on Form NC-478, Line 3. S corporations claiming the credit against income tax, complete Parts 1 and 2 as one taxpayer, then allocate the amount from Part 1, Line 7, or Part 2, Line 6 among the shareholders. Complete Part 3 by only including the amounts allocated to nonresident shareholders on whose behalf a composite return is being filed. On Part 3, Line 2, include only the amount of carryforward for nonresident shareholders on whose behalf a composite return is filed in both the prior year and the current year.

#### **NC-478D – Tax Credit for Worker Training**

Corporations claiming this credit against franchise tax, complete NC-478D and enter the amount from Part 2, Line 3 on Form NC-478, Line 4. S corporations claiming the credit against income tax, complete Parts 1 and 3 as one taxpayer. Add Part 1, Lines 4 and 8 and allocate the total amount among the shareholders. Complete Part 2 by including the amounts allocated to those nonresident shareholders on whose behalf a composite return is being filed. On Part 2, Line 2, include only the amount of carryforward for nonresident shareholders on whose behalf a composite return is filed in both the prior year and the current year.

#### **NC-478E – Tax Credit for Investing in Central Adm. Office Property**

Corporations claiming this credit against franchise tax, complete NC-478E and enter the amount from Part 3, Line 4 on Form NC-478, Line 5. S corporations claiming the credit against income tax, complete Parts 1 and 4 as one taxpayer, then allocate the amount from Part 1, Line 11 among the shareholders. Complete Parts 2 and 3 by including the amounts allocated to nonresident shareholders on whose behalf a composite return is being filed. On Part 3, Line 3, include only the amount of carryforward for nonresident shareholders on whose behalf a composite return is filed in both the prior year and the current year.

#### **NC-478F – Tax Credit for Investing in Business Property**

Corporations claiming this credit against franchise tax, complete NC-478F and enter the amount from Part 3, Line 6 on Form NC-478, Line 6. S corporations claiming the credit against income tax, complete Part 1 as one taxpayer, then allocate the amount from Line 5 among the shareholders. Complete Parts 2 and 3 by including the amounts allocated to nonresident shareholders on whose behalf a composite return is being filed. On Part 3, Line 5, include only the amount of carryforward for nonresident shareholders on whose behalf a composite return is filed in both the prior year and the current year.